RICE UNIVERSITY

THE USE OF SPECIAL DISTRICTS
IN FINANCING AND FACILITATING URBAN GROWTH

by

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Abstract

THE USE OF SPECIAL DISTRICTS IN FINANCING AND FACILITATING URBAN GROWTH
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Legal restrictions on debt limit and municipal taxing authority are almost universal in the United States. These restrictions have contributed to an inability on the part of many cities to provide basic support for the additional growth and development of urban areas. In most instances, political considerations have prevented state legislatures from lifting these financial limitations.

In order to sustain urban growth and support the development of new urban areas, several states have developed alternatives to continued reliance on existing municipal governments. I submit that the most satisfactory alternative is the use of special district governments to finance all or part of the required utility and community support facilities. The particular variety of special district developed in Texas for this purpose has produced a record of successful and basically satisfactory operations unmatched in other parts of the nation. Therefore, particular attention is accorded the functioning of Texas water districts.

The thesis of this paper is that increased reliance on the use of special districts, patterned after the Texas variety, offers a valuable, flexible and appropriate instrument for effectuation of plans for urban growth whether as extensions of existing growth areas or as
new communities. The thesis will be developed in the following way:

In section 1000 the problems inherent in providing utility support and community service facilities to developing areas are introduced and characterized. Several alternatives for financing needed improvements are briefly discussed and the most acceptable alternative, the use of special district government, is explored more fully. This section is concluded with a glossary of terms and a brief description of agencies referred to frequently in other sections by abbreviated titles.

In section 2000 the history, methods of formation and operating capabilities of Texas water districts are explored. Commentary on peculiarities, problems and areas for improvement is offered. The section is concluded with a summation of important points relative to the Texas experience with water districts.

In section 3000 the relationships between urban growth and the use of water districts is explored. General principles that seem to apply to this relationship and to the development of urban form are established. Ways in which similar districts might be used as a tool for implementation of regional growth policies are explored and the particular advantages of water districts over other types of districts are pointed out.

In section 4000 the analysis is summarized and a general conclusion is drawn based on the use of promotional special districts as a tool for implementing policy in areas destined to experience rapid growth.
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Introduction
Water, sewer and drainage improvements ordinarily represent a greater investment than any other utility necessary in the development of land. The extent of this investment is not generally realized because periodic municipal water and sewer charges seldom represent all of the capital costs involved. As an indication of the cost, a current practice by land developers in Houston is to use a range of $5000 to $6000 per acre as a general rule of thumb for water, sewer and drainage improvements for single family subdivisions.

Historically, reliance for provision and operation of water related utilities in urban areas has been placed upon established units of local government. Policy for the extension of water and sewer services in an unserved area usually stipulates that the city will extend the trunk line at its own expense and requires that the developer pay half the cost of the lateral lines and a connection charge for each hookup. Imposition by state constitutions and statutes of stringent tax and debt ceilings, combined with the political problem of convincing one constituency to incur debt for the benefit of another, make execution of this municipal policy practically impossible. Because of municipal inability, refusal, or reluctance to provide access to a trunk line for outlying or suburban areas, developers, in many instances, have sought relief from dependency on cities.

The United States is unique in that we continue to place almost total reliance for development of new land areas on the private sector of
the economy. Governmental intent to continue this reliance was expressed as recently as January 25, 1972, in HUD Secretary Romney's remarks to the convention of the National Association of Homebuilders in Houston. Mr. Romney indicated a desire to phase out all HUD programs of governmental interference with housing production except programs involving direct subsidy saying, "We want to unleash the housing industry."

If we begin with the premise that some type of urban development and growth is to be encouraged, and that primary reliance for its delivery will continue to be placed upon the private developers and promoters, consideration of the incentives offered to this group are of paramount importance. The criteria for judgement are the following:

1. What problems of control are introduced?
2. What are the probable complications and undue demands for time and effort (red tape involvement)?
3. How effective is the method in minimizing demands for front end investment?
4. What are the marketing effects in terms of product cost?
5. What are the long range effects on the developers' reputation?

The most important single characteristic of any financing mechanism or early government in a developmental situation is assurance of control by the developer. Because of this crucial issue, the developer can immediately exclude many possibilities from the list of options which includes:

a) Incorporation
b) Annexation to another unit of government
c) Use of developer's equity
d) Formation of a private utility company
e) Formation of one or a series of special districts

Incorporation of an unpopulated tract is almost always precluded because of statutory requirements for a minimum population. Even when
they are possible, incorporations are often used as a negative sanction to stifle unwanted development. This is evidenced in this area by the experience of Nassau Bay. In that instance, the early residents of the development incorporated and enacted a zoning ordinance. This action had the effect of forcing Holly Enterprises, Inc., the developer, to abandon the development plan. In effect, the developer was zoned out of his own development at a great loss in expected profits. The potential of an incorporation to have this effect is not likely to encourage real estate developers to elect that option.

Annexation to an existing government immediately puts the developer in the position of a petitioner for service with no assurance that his needs will be met. In addition to this, application for annexation of undeveloped land will probably be looked upon by the existing city as an opportunity to incur an instant liability with no improvement to the tax base and consequently the application would be rejected.

Use of the developer's equity money is frequently the only option available within the limits of a municipality. Where other alternatives do exist, consideration of this option by the developer will be brief as its effect on financial leverage is disastrous and the opportunity cost of investing more money in the project than necessary is great. If he chooses this option, disregarding its failure to satisfy his third criterion, he will probably be financially limited to considering private wells and septic tanks. Though this solution was widely used in the past, it is now likely to receive necessary approval in few metropolitan areas.

Formation of a private utility company, perhaps the most apparent option,
contains a number of pitfalls. The operation of utilities was as in the past and is now a potentially lucrative enterprise. Except for a few areas of the country with large established private operations, the private utility option may be a poor choice because of the following two characteristics:

a) Developers are characteristically financed to the extent of their credit. This condition adds to the already formidable problems of raising the capital required to begin a private utility company.

b) Except in protracted developments such as new communities, the developer does not desire continuing control of the utility systems. His interests are best served by extricating himself from a development as soon as possible and going on to new ventures. As the market for private utility companies is unpredictable at best, choice of this option would probably require continuing operation of a utility business.

Finally, consideration of the special district alternative, where it is available, nicely satisfies all five criteria. Demands on the developers' "front end" equity investment are limited to retainers for the attorneys and engineers who provide professional services and the cost of advertising elections and bond issues.

Once the district is established and the bonds are sold, the operation of the district is autonomous and businesslike. Control over the development rests entirely with the developer except for design review and approval authority retained by state agencies. It is recognized by all that control will pass to the homeowners in future elections of directors. This usually occurs two to three years after the first house is sold. The long range effects on the developer's reputation will depend largely upon the way the affairs of the district were discharged during the period of his control and on his forthrightness in calling the attention
of his customers to the existence of the district debt.

In addition to satisfying the primary criteria, a hidden benefit is realized by the developer from use of a governmental entity to provide site improvements. Because he is categorized by the Internal Revenue Service as a dealer in land, he must pay income tax rather than capital gains on the difference between his cost for unimproved land and his selling price for lots. Deferment of improvement costs results in a lower sales price thus lowering the developer's taxes without lowering his profit. At this juncture the options discussed can be categorized:

**Phantom Options**

1. Incorporation
2. Annexation to another unit of government

**Real Options**

1. Use of developer's equity
2. Private utility company (in some areas)
3. Special district

Regardless of the specific solution, the use of either a private utility company or developer's equity to finance needed improvements creates a "pay as you go" situation in which the improvements are paid off in pro rata shares with the purchase of improved land. This practice contrasts with a high degree of debt financing of other utility systems such as telephone, electricity and natural gas and creates a situation in which the price of the subdivided unit is inflated by the cost of a pro rata share of the water utility system.

1020 **CHOICE OF THE SPECIAL DISTRICT OPTION**

A great deal of the land occupied by the Houston metropolitan area is in a flood plain, poorly drained or composed of non-percolating soils.
These conditions are incompatible with the extensive use of septic tanks and other borderline solutions to sewage disposal problems. They result in a need for elaborate sewage facilities and the frequent need for significant drainage improvements. As a consequence, the feasibility of diminished expenditures has been an unacceptable solution to development problems in the Houston area. This situation stimulated the early formulation of a unique solution.

In the absence of local or federal assistance, state governments come under a great deal of pressure to assist in procuring needed services for growth areas. State officials, already concerned with the problems of meeting current obligations with existing tax monies, have sometimes viewed permissiveness in the use of developer formed special districts as a "free" subsidy in that it gets the job done with no increase in state expenditures. Thus the unusual ability under Texas law to finance water, sewer and drainage improvements by formation of special district governments became a major factor in encouraging and sustaining the growth of the Houston metropolitan area. By obtaining favorable debt financing for water related utility improvements, special districts allow deferment of payment for the system over the life of a bonded debt which is usually twenty to thirty years. This practice places all utilities on a similar basis in that they are all primarily debt financed. In addition to granting independence from the city, district services, when supplemented in some manner, are adequate for provision of the sub-metropolitan services needed in a new area. As the district is formed initially to provide facilities to the developers' subdivisions, there is little likelihood of reluctance on the part of the district to perform. Finally, the use of a water district permits the developer to
avoid financing some of the improvements he would otherwise be required to provide. Since repayment of the district debt in a successful development will be accomplished by the buyers of subdivided land, the developers are incurring debt and making improvements on behalf of future owners.

1030 SPECIAL DISTRICT DEFINITION

Special districts are local governmental entities that can be formed in both urban and rural areas of every state for an almost limitless variety of purposes. Among the types that are familiar are: hospital districts, school districts, water districts, irrigation districts, drainage and flood control districts, river authorities, urban renewal districts, etc. Since special districts may be endowed with special powers and can be tailored to perform one or more specific functions, they are highly flexible and efficient tools for stimulation of urban growth. This flexibility enables them to be adapted to function in development of commercial, industrial and residential properties and in projects ranging in scale from small subdivisions to new communities.

Special districts enjoy many of the same powers and privileges as municipalities. However, municipalities possess broad based powers, while special districts are generally restricted by enabling legislation to performance of one or more specific functions. Privileges and powers often include tax exempt status, authority to issue "municipal" securities, power to levy ad valorem taxes and eminent domain authority. It is not unusual for certain privileges, notably taxing authority and debt limit, to be greater for special districts than for general purpose (city or county) governments. The general concern of special districts is to provide a particular service to particular users on the theory that
when general purpose governments cannot or will not provide a necessary service to an area, it is appropriate to form a specialized agency to do the job. In this sense, special districts are the embodiment of grass roots government.

Table 1000-1 contains a breakdown by type of special districts operating in the United States. Note that 63.1% of districts operating sewage systems and 45% of districts operating an urban water supply were within a SMSA. The increasing popularity of special district use to transcend ineffective general units of government is indicated by figures 1000-2, 1000-3, and 1000-4. This phenomenon is partially attributable to a significant change in the use of certain types of special districts in rapidly urbanizing states among which California, Florida, and Texas are notable. In these states, special districts may use their powers to provide services to undeveloped areas, whereas the use of their powers was previously limited to improvement of existing communities. These changes are usually the result of adaptations of existing special district statutes to satisfy pre-developmental needs of urban growth areas.

1040 TEXAS WATER DISTRICTS

Since the idea was first applied in the era immediately after the end of World War II, the use of special districts in Texas has increased in number at an astonishing rate. Figure 1000-5 plots the growth in numbers of water districts in Harris County.

Unlike the larger multi-purpose special districts that have been used in other states, Texas water districts are usually subdivision sized and ordinarily perform only the three primary water related utility functions
<table>
<thead>
<tr>
<th>Type of special district</th>
<th>United States</th>
<th>Within SMSA's</th>
<th>Outside SMSA's</th>
<th>Percent in SMSA's</th>
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<tr>
<td>Total</td>
<td>21,264</td>
<td>7,049</td>
<td>14,215</td>
<td>33.1</td>
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<tr>
<td>Natural resources</td>
<td>6,539</td>
<td>1,275</td>
<td>5,264</td>
<td>19.5</td>
</tr>
<tr>
<td>Other than natural</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Resources</td>
<td>14,725</td>
<td>5,774</td>
<td>8,951</td>
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<td>Cemeteries</td>
<td>1,397</td>
<td>142</td>
<td>1,255</td>
<td>10.2</td>
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<tr>
<td>Fire protection</td>
<td>3,665</td>
<td>1,383</td>
<td>2,282</td>
<td>37.7</td>
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<tr>
<td>Highways</td>
<td>774</td>
<td>195</td>
<td>579</td>
<td>25.2</td>
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<tr>
<td>Hospitals</td>
<td>537</td>
<td>105</td>
<td>432</td>
<td>19.6</td>
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<tr>
<td>Housing and urban</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>renewal</td>
<td>1,565</td>
<td>522</td>
<td>1,043</td>
<td>33.4</td>
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<tr>
<td>Libraries</td>
<td>410</td>
<td>131</td>
<td>279</td>
<td>32.0</td>
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<tr>
<td>Parks and recreation</td>
<td>613</td>
<td>305</td>
<td>308</td>
<td>49.8</td>
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<tr>
<td>School buildings</td>
<td>956</td>
<td>588</td>
<td>368</td>
<td>61.5</td>
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<tr>
<td>Sewerage</td>
<td>1,233</td>
<td>778</td>
<td>455</td>
<td>63.1</td>
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<tr>
<td>Urban water supply</td>
<td>2,140</td>
<td>964</td>
<td>1,176</td>
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<td>Other single-function</td>
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<td></td>
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<tr>
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<td>982</td>
<td>380</td>
<td>602</td>
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<tr>
<td>Multiple-function</td>
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<tr>
<td>districts</td>
<td>453</td>
<td>281</td>
<td>172</td>
<td>62.0</td>
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**TABLE 1000-1: BREAKDOWN OF SPECIAL DISTRICTS: 1966**

TABLE 1000-2: NUMBER OF LOCAL GOVERNMENTS IN EXISTENCE

TABLE 1000-3: NUMBER OF NON-SCHOOL SPECIAL DISTRICTS IN EXISTENCE

TABLE 1000-4: NUMBER OF WATER RELATED SPECIAL DISTRICTS IN EXISTENCE


TABLE 1000-5: NUMBER OF WATER DISTRICTS IN HARRIS COUNTY

of providing and maintaining water, sewer, and drainage improvements. The Texas Water Code allows a majority of landowners, or the owners of land representing a majority of the assessed valuation in an area, to petition for formation of a water district. Upon creation of the district, a simple majority vote of the resident owners of the land confirms the creation of the district and authorizes issuance of bonds. Following confirmation of the district, the directors may proceed with the implementation of the district's projects.

In the decade of the 1960's, the Houston SMSA experienced the second largest growth among the twenty largest SMSA's in the United States measured in per cent of population increase. The sustained economic vitality of this region through the recession experienced by the nation over the past several years is partially attributed to this continuing development. The importance of special district use in this expansion appears to have been in the easy and temporary alliance that was provided between the private and public sectors of the economy to facilitate rapid growth. The association more closely resembles a limited partnership than an instrument of state credit subsidy.

\( \text{50 NATIONAL URBAN GROWTH NEEDS} \)

A growing awareness of acute pollution problems in urban areas has influenced the United States to take dramatic steps to eliminate the problems associated with poorly financed urban growth. Chief among these problems is the practice of relying on inadequate sewage collection and treatment facilities. In executing the mandate to stop pollution, enforcement agencies have temporarily arrested growth in several rapidly urbanizing parts of the country.
An analysis of all federal programs designed to subsidize the provision of basic water, sewer and drainage improvements indicated that only one was capable of being exercised in a situation involving undeveloped and unoccupied land. The one program having limited applicability is Title VII of the Housing and Urban Development Act of 1970 which enables developers of qualifying new communities to receive federal loan guarantees for monies to be expended on these facilities. Because of this situation, urban areas must look to the state for assistance in accommodating rapid growth. The unique class of special districts functioning in the Houston area to assist in financing land improvements are appropriate for consideration as the basic component of a growth system which might be adopted by other areas where significant urban growth is to be facilitated.

By adapting public procedure to the developmental needs of promotional projects, the developer in effect makes the special district a temporary operating division of his organization, thus using a public agency to eliminate the necessity for personally financing certain needed improvements. This practice brings up political, ideological and public policy issues that have been hotly contested and are likely to remain controversial.

Occasionally, the privilege of special district creation and use has been abused by real estate promoters and the possibility of further abuse exists. It is recognized that more effective, though not necessarily more stringent, controls are needed, and the activities of individual developers must somehow be orchestrated to achieve a desirable and co-ordinated pattern of regional development.
**automatic homeowners association** - an association in which continuing membership is mandatory concurrent with the ownership of land within a development. The association maintains certain facilities and makes services available to its members and assesses its membership for support.

**confiscatory** - (when describing a tax) onerous or burdensome to the degree that confiscation of the object may be alleged.

**full faith and credit** - a pledge of all resources or potential revenue as security for a loan. This pledge obligates a political entity to use all of its power to insure the repayment of an obligation.

**refund contract** - agreement by a unit of government to reimburse a developer for improvement or extension of a public system. The amount refunded is usually limited to a percentage of the costs.

**sinking fund** - the aggregate of sums of money, set apart usually at fixed intervals, and deposited or invested to extinguish a debt, or for other purposes.

**tertiary treatment** - term indicating third degree treatment of wastewater. Quality of effluent after tertiary treatment should be similar to fresh water quality.

**VATS** - Vernon's Annotated Texas Statutes, the standard set of volumes containing all of Texas statutory law.

**ABBREVIATED AGENCY TITLES**

**COGS** - councils of government.

**FWSD** - Fresh Water Supply District.

**MUD** - Municipal Utility District.

**SMSA** - Standard Metropolitan Statistical Area; This term is used by the U.S. Census Bureau in defining the extent of urbanized area around a dominant municipality.

**TWQB** - Texas Water Quality Board; State agency for supervision over matters involving environmental aspects of pollution regulation and water quality.

**TWRC** - Texas Water Rights Commission; State agency charged with power to create water related special districts and to regulate their activities.

**WCID** - Water Control and Improvement District.
1000 FOOTNOTES


2. Ellen Middlebrook, Staff reporter for the Houston Post, personal interview, 2/21/72.


4. Ibid.

5. Woodworth G. Thrombley, Special Districts and Authorities in Texas, with a foreword by Lynn F. Anderson (Austin, Texas: University of Texas Printing Division, 1959), page 2.


2000
Special Districts in the Houston Metropolitan Area
Evolution of Texas Water Districts

STATE CONSTITUTION AND POLITICAL MAKE-UP

The Constitution of the State of Texas was written by individuals united in their mistrust of concentrations of governmental power. Cities, towns, villages and counties are most notably restricted in terms of their power to generate revenue. These restrictions make it difficult to amass a great deal of power in any one agency and thereby avoid excessively large government and its political entanglements.¹

A phenomenon of the nineteenth century constitutes a second important element of rationale behind conservative state constitutions. During this era, it was not uncommon for municipalities to extend credit or grant concessions to private corporations. To some extent, high municipal debt and election requirements for issuing bond or raising taxes were occasioned by the excesses of some cities engaged in trying to persuade railroads to build lines through or near their corporate limits.²

As a result of the municipal limitations that grew out of these situations, a tradition has grown in Texas, as well as in several other western and southwestern states, of ad hoc problem solving. Out of this tradition came several ingenious adaptations of the special district, including water districts, which are the topic of study here.

In the latter part of the nineteenth century, Texas experienced a series of floods and droughts that called attention to the need for developing and conserving state water. In 1904, the system of laws under which
water districts were to be created and maintained in Texas began to develop. In that year, the conservation movement had gained sufficient popular acceptance for the adoption of the first constitutional amendment providing for taxing units or "districts" to husband the states' water resources and put them to beneficial use. The amendment became Article III, Section 52 of the Texas State Constitution.\(^3\)

Special district problem solving was reinforced by a second constitutional amendment passed in 1917 which offered broader constitutional authority and a more acceptable means by which the capital improvements could be advantageously financed. This amendment which created the unique situation under which water districts have unlimited tax and debt limit while all units of general government have limited indebtedness, is commonly referred to as the "conservation amendment". The resulting Article XVI, Section 59 of the Texas constitution is the significant authority under which all of the districts concerned with here are formed.\(^4\) A clear understanding of the motives behind its adoption and the mandate articulated thereby may best be had by reference to its language which provides in part:

"The conservation and development of all of the natural resources of this State, including the control, storing, preservation and distribution of its storm and flood waters, the waters of its rivers and streams, for irrigation, power and all other useful purposes--the reclamation and drainage of its overflow lands and other lands needing drainage are and are hereby declared public rights and duties; and the Legislature shall pass all laws as may be appropriate thereto."

and further that:

"There may be created within the State of Texas or the State may be divided into, such number of conservation and reclamation districts as may be determined to be essential--which districts shall be governmental agencies and bodies politic and corporate with such powers of government and with the authority to exercise such rights, privileges and functions concerning the subject matter of this amendment as may be conferred by law."

It then makes specific provision for such districts to incur a bonded debt
and for the levy of all such taxes as may be necessary to pay such bonds. 

In order for indebtedness to be incurred or bonds issued, the proposition must have been adopted by the taxpaying resident voters of the district. 

The importance of the situation thus created is illustrated by the fact that although the first amendment of 1904 permitted districts to issue bonds in any amount up to 25% of the district's real property valuations, districts formed under the 1917 amendment have no limitations on indebtedness and bonds may be issued without limit as to tax rates or amount.

2120 THE NATURE OF TEXAS DISTRICTS

The nature of water districts is recognized in the following excerpts from decisions by the Texas Supreme Court:

"The people of Texas, in adopting the Conservation Amendment Article XVI, Section 59, have very plainly set forth that they decree these districts to be "governmental agencies and bodies politic." The representatives of the people assembled in the Legislature, in carrying into effect the constitutional amendment, have likewise so decreed. It is the duty of the courts to give effect to the will of the people as so plainly expressed."

"Regardless of what our individual opinion upon that question may be, it is our duty to obey the mandate of the people of Texas when they have spoken so clearly in the adoption of Section 59, Article XVI of our present Constitution. Our Government is one in which the people are the sole repository of all power. They are limited only and solely as they have delegated their powers to the various branches of the State government. The people had the right to declare organizations such as respondent to be bodies politic and governmental bodies. This they have done in no uncertain terms."

"Districts, including Water Control and Improvement Districts created by or pursuant to statutes enacted under the aforesaid provisions of the Constitution have been consistently recognized by our courts as being political subdivisions of the State which perform governmental functions and which stand upon the same footing as counties and other political subdivisions established by law."

It can be seen from these remarks that in safeguarding against oppressive government the Texas Constitution firmly established a continuing pattern
to encourage government by functional specialization.

For years water districts in Texas were thought of as financing mechanisms for drainage or irrigation of existing rural communities. In addition to the smaller, scattered districts serving the agricultural, flood control or navigational needs of communities, the 1917 amendment authorized the formation of river authorities. They have extensive borrowing powers but limited taxing authority and rely primarily on user charges and grants for their subsistence. Each river authority covers an extensive area and some of its duties overlap or relate to those of the water districts within its boundaries.

About 1945, two significant new aspects of water districts were recognized. The first aspect was that the statutes were sufficiently flexible to permit the use of districts in a suburban context to supply needed water, sewer and drainage improvements for urban growth. The second revelation was that the districts could be formed in advance of development and used to help finance needed improvements. If the land were subdivided and sold, the debt on the land would be divided into pro rata shares and assumed by the new owners.

There are several varieties of water districts provided for in the Texas statutes. Of these, two have played an historic role in the urban use of developmental districts. These two are the Fresh Water Supply District (FWSD) and the Water Control and Improvement District (WCID). A new statute was passed in the 1971 (62nd) Legislature authorizing a streamlined general law method of creation for Municipal Utility Districts (MUD) making it the current choice for nearly all developmental urban districts.
In addition to the FWSD, the WCID and the MUD, several other varieties of water districts have been used for promotional purposes, but the distinctions between types are technical. Except for an occasional reference to a particular type, the generic term water district will be used.

Although broader powers have been given to special developmental districts used in California and Florida, Texas water districts are limited to the performance of water-related functions. Generally, Texas districts have exercised their powers only to provide the three basic services of water, sewer and drainage improvements. This restraint is largely responsible for the high regard in which Texas water district bonds are held all over the country. The reasons are:

1. Two of the three functions (water and sewer) are revenue producers leaving drainage improvements as the only non-revenue function. The part of the debt represented by drainage improvements must be retired from taxes and/or from water and sewer revenue.

2. The limitation of power forces the developer personally to finance roads and other non-water related improvements. Requiring the developer to make substantial investments in addition to those made by the water district is a practical safeguard against ill-advised or uncommonly speculative use of district funds.

The service provided by water districts and the method of payment by those directly benefited tend to place them in the category of a public utility. Of all improvements provided in the development of land, the water and sewer system represents the greatest sunken cost in capital improvements.

In a typical subdivision of single family detached units, the cost of installing water, sewer and drainage improvements often exceeds the cost of the undeveloped land and is from one to three times as great as the cost of other necessary improvements. The magnitude of the investment required makes the method of financing a matter of major consequence to the present owner or developer, future owners, lenders, and to general purpose governments that may fall heir to the assets and liabilities upon annexation.
PRIVATE UTILITY ALTERNATIVE

A discussion of water district use in Texas would be incomplete without reference to the most apparent alternative, the private utility company. For years, private utility companies were active in providing basic utility services to small Texas communities. The largest of the operators was the Texas Water Company with headquarters in Chicago. 9

Water districts authorized under the 1904 and 1917 constitutional amendments provided the first challenge to the domain of the private operators in Texas. An apparent desire for complete control, the tax exempt status of water districts and their taxation, bonding and eminent domain authority appealed to many of the communities served by private utilities. When presented with the option, these communities often elected to form special districts and buy out the operations of the private operators. The option of incorporation was occasionally elected in larger communities to replace the private utility company. Reluctant private operators were influenced to sell at a negotiated price by the ever present threat that the new government might parallel the service being offered by the private utility company. A negotiating position was also held by the private utility company in these situations by virtue of the natural reluctance of bond buyers to buy the bonds of a water district in an area already being served. 10

COMPARISON OF PRIVATE UTILITY AND SPECIAL DISTRICT BENEFITS

While it is realized that this is partially a reflection of the developer's concern for marketability, the options outlined in the introduction should
be surveyed from the consumer's point of view. If use of the developer's equity is dismissed as unrealistic, the options are narrowed to private utility company or special district. The following criteria are applicable:

1. Initial product cost
2. Ongoing taxes or assessments
3. Quality and completeness of service

If a private utility company is used, the homeowner can expect to see a large part of the pro rata share of the utility system reflected in the cost of the unit he purchases. This is necessary because of the high interest rate and poorer terms on which loans are available to private utilities and because the future revenue for operation and retirement of debt must come solely from user charges -- the monthly water and sewer bill.

The private utility company enjoys no refuge from state and federal taxes and these taxes are reflected in the cost of service to the homeowner. As his service comes from a private company with no immediate competitors, he is at the mercy of their rate structure and must rely on indirect rate control through the State Utility Commission. In Texas there is no utility commission. The extent of service will be limited to revenue producers such as water, sewer and garbage removal while another means must be found to supply the required non-revenue-producing services such as drainage improvements, police and fire protection.

On the other hand, the use of a special district has several distinctly beneficial effects on the buyers. A good portion of the site improvements may be deferred thus allowing the price of the products to be reduced. Year to year operating costs for the district include amortization of the
bonded debt and is necessarily higher than for some other options in which the improvements are paid for upon purchase or financed as a part of the mortgage. As the district debt was incurred on reasonable terms, the extended retirement schedule is to be preferred to initial payment or inclusion of the amount in the mortgage. All payments of taxes to the district are deductible from the homeowners federal income tax and operating costs are diminished by special district exemption from federal income tax, sales, excise, use and ad valorem taxes of other jurisdictions. The range of services provided will vary from state to state, but ideally, the promotional special district will be empowered to provide water supply, sewage disposal, garbage pickup, drainage improvements, fire protection and maintenance of all public streets, parks and other facilities--a more complete range than the private utility company.

2160 MUNICIPAL UTILITY DISTRICTS

Most of the experience in Texas with the use of water districts has occurred within the extraterritorial jurisdiction of Houston. Though the WCID statute possessed broader powers, the city exercised the prerogative of limiting the power of all water districts to the functions of water, sewer and drainage.

The new MUD statute clarifies and states more succinctly some of the additional powers which have existed for some time in the WCID statutes, but a conscious effort was made in drafting the new MUD statute to "plow no new ground" in terms of constitutional novelty that would increase district powers.\[1\]

It may be presumed that as more development occurs outside the extra-
territorial jurisdiction of Houston and other municipalities, the use of these other district powers will become more common. Among those enunciated in the MUD statute are the ability to finance acquisition, improvement and operation of parks and recreational facilities and the ability to accomplish navigational improvements which may include channel dredging and shoreline improvements.

Maintenance of reasonable limits on the ratio of bond debt to assessed valuation has been cited as a reason for the stability of Texas districts. The desirability of maintaining this limit may well dictate a situation in which developers finance expensive site improvements and dedicate these improvements to the district. The district may then exercise its expanded powers only in operating and maintaining these improvements.
2100 FOOTNOTES

3. Woodworth G. Thrombley, Special Districts and Authorities in Texas, with a foreword by Lynn F. Anderson, (Austin, Texas: University of Texas Printing Division, 1959) page 43.
5. Alan D. Carey and John P. Owen, "Water districts, An Asset or a Liability?", The Houston Homebuilders Association, (March 1959), page 15.
6. Cyril Smith, partner with Smith, Rowe, Fisher & Hay; attorneys, personal interview 2/24/72.
7. Ibid.
9. Ibid.
10. Ibid.
Formation & Capitalization of Water Districts

REGULATION AND REQUIREMENTS

Notwithstanding claims to the contrary made by detractors of promotional water districts, reference to the Texas Water Code or to legal notices in almost any edition of the Post or Chronicle illustrates that a tremendous amount of "due process" is required for district creation. Procedures are so strenuous that the average elapsed time between petition and creation is from five to nine months, and a record of the procedural steps often fills a loose leaf binder two inches thick.

In addition to review of the plans for the facilities to be constructed with the proceeds from the bond sale, the Texas Water Rights Commission reviews the entire district financing program prior to approval. The bonds must also be approved as to legality by the Attorney General and registered by the Comptroller of Public Accounts, as well as reviewed and approved by the Texas Water Quality Board and the State Health Department. In addition to regulations provided for in the enabling legislation are requirements prescribed by operational prerogatives of the agencies from whom approval must be obtained and by other legislation.

An example of regulation by the operational prerogative of an approving agency is the requirement of the Texas Water Quality Board that districts in certain areas conform to the Regional Waste Disposal Plan which has been drawn and adopted by the members of the appropriate planning council. Issuance of the required permit to operate a sewage system is made conditional to conformity.
Certain local controls were added to the state regulation of water districts by the enactment of the Municipal Annexation Act of 1963 giving cities limited jurisdiction over certain territory outside their boundaries. The extent of area over which jurisdiction is exercised depends on the population of the municipality. This is particularly significant with regard to water districts inasmuch as they may not be created within a city's extraterritorial jurisdiction without that city's consent. In the case of districts within the extraterritorial jurisdiction of Houston, compliance with the following requirements for bond sales is a condition to approval on the theory that the district will be annexed by the city before the bond debt is totally retired. This control has proved effective in guarding against shoddy practices in the sale of bonds, contracting irregularities and other problems with the use of district funds.

1. Bonds may be issued only for waterworks, sanitary sewer and drainage purposes;

2. Bonds shall be redeemable within fifteen years of the date of issuance without premium;

3. Bonds may be sold only at public sale;

4. Bonds must be sold at not less than 95% of par and the net effective interest rate may not exceed 2% above the highest average interest rate reported by the Daily Bond Buyer's "20 Bond Index" during the one month period next preceding the date Notice of Sale of such bonds is given.

And further that:

1. The district must submit plans and specifications to the city for approval, and such plans shall conform to city requirements;

2. The city will inspect construction of the district's facilities;

3. If the district is a development district, the developers must obtain approval of the city's planning commission and must comply with the commission's rules and regulations.
METHODS OF CREATION

There are basically two methods for accomplishing the formation of a petitioned-for district:

1. general law enactment
2. special act of the State Legislature

The distinction is that general law procedures are for the accomplishment of some governmental purpose through a prescribed agency of government in a standard way, while special law procedures are those "one time" measures which require an act of the Legislature for their enactment.

General Law Methods

The 1904 and 1917 constitutional amendments and resulting statutes provided for several different types of water districts with significant variations in powers. A particular procedure for general law creation of each type of district is provided. Either the Texas Water Rights Commission (formerly the Board of Water Engineers) or the county commissioners' court having jurisdiction were vested with power to create a particular type of general law district. The choice of agency depends on the extent of the powers exercised by the particular type of district.

The county commissioners' courts were frequently relied upon for creation of developer-inspired districts in the earlier days of their use because of convenience and speed. When the Texas Water Rights Commission was given exclusive jurisdiction over multi-county districts or districts with power to provide sanitary sewage systems, the county commissioners' courts became unacceptable for use in the creation of promotional districts.
The Texas Water Rights Commission is now the predominant regulatory and supervisory agency for creation of water districts. As a result of the workload and statutory requirements for reviews, advertisements, waiting periods etc., creation of a district by the Commission was, until recently, a time consuming and unwieldy process. The 1971 (62nd) Legislature adopted a new measure for creation by the Commission of Municipal Utility Districts which eliminates many of the unnecessary and archaic procedures previously required. It is anticipated that almost all future creation of developmental districts will be done under this streamlined provision.

Special Law Method

One of the complaints leveled against the promotional water districts in the past pertained to the workload created for the Legislature by the popularity of special law districts. Until the streamlined general law MUD provisions were adopted in 1971 by the 62nd Legislature, the majority of promotional districts were created by the legislature. Illustrative of this fact are the 134 special law districts created in 1971 by the 62nd Legislature. Prior to the present time, the special law alternative was preferred because of the procedural exemptions allowed. This exemption power included the district's right to waive the confirmation election, exclusions hearing and the plan of taxation - all of which were previously required for general law districts. Legislative bills are carried on the local and uncontested calendar and their approval is all but assured. It should be pointed out that the bonds of special law districts also require approval by the Texas Water Rights Commission.

Procedure for general and special law creation of the WCID and for the
new general law MUD are shown in Appendix A.

2230 FACTORS AFFECTING MINIMUM SIZE

The smallest feasible size of a water district is determined by the factors of time, cost and development density. Probably the most important single determinant of minimum district size is the considerable time required for executing the administrative procedures for district formation. For smaller projects, the developer is seldom prepared to wait a minimum of five months for authority to install the utility improvements. In addition to legal and engineering fees, which are usually nominal, considerable miscellaneous expense and bother accrue from the publication of legal notices and other required actions. Perhaps as significant as the time and expense required for district formation is the advance planning required. If vacant land is to be developed, several individuals who are qualified voters in the county must be placed in residence in the district to qualify as resident voters for the anticipated bond election.

The minimum practical size for a water district relates to the volume of use to be placed on the water, sewer and drainage systems and the value of the required improvements. Thus, as a rule of thumb, a single family subdivision with three units per gross acre must exceed one hundred acres to warrant formation of a water district. Another factor to be considered is that the Texas Water Rights Commission, because of administrative workload and knowledge of past bad experience with the marketing of securities from miniscule districts, is not likely to react favorably to such a petition.
Financing of water district projects is authorized by the issuance of tax, revenue or combination bonds. Tax and combination bonds are payable from the district's ad valorem taxing authority. Revenue bonds are payable only from the user charges generated by sale of services on contract or monthly water and sewer sales to land owners within the district. Bonds authorized in a bond election are issued on an as needed basis and provisions exist for the cancellation of unsold bonds.

The voters of the district must authorize bonds supported entirely or in part by a tax levy, while bonds supported entirely by pledged revenues usually may be issued by action of the district's board of directors. In the past, only combination bonds supported by an ad valorem tax and the full faith and credit of the district have been enthusiastically received by bond brokers and buyers.\(^7\)

Prior to the enactment of the Municipal Annexation Act of 1963, water district bonds were sold locally to or through developers - often at a higher interest rate than is now permitted and at substantial discounts. This practice led to several questionable situations in which developers and city politicians bought bonds at a discount just prior to annexation of the issuing district. The bonds were redeemed by the city at par, and the entire procedure subjected water district bonds to a speculative and fraudulent reputation. Additionally, a general lack of knowledge and information about water districts had been detrimental to the marketability of their securities.\(^8\)
After prerogatives for limitation of interest rate and discount points were extended to Texas cities in 1963 for use within their extraterritorial jurisdiction, water district bonds assumed a greater air of security and respectability. Several nationally recognized brokerage houses now actively market district bonds and one of the leaders, in order to bridge the information gap, now offers the services traditionally performed by fiscal agents for districts. They now perform the following services for districts whose securities they market.  

1. Provide a complete bookkeeping service to the district on all of its accounts;  
2. Assist in the management and investment of all funds of the district;  
3. Assist the district in preparation of its annual budget;  

In this way, complete fiscal data concerning each of the districts represented is available to investors at all times and can be furnished to bond holders on a regular basis.

In forming a promotional special district, demands on the developer's "front end" equity investment are limited to a modest outlay. Even these are normally considered as organizational expenses and therefore payable from the sale of bonds. Depending on the method of formation, additional expenses in the nature of political campaign contributions may be incurred, but the likelihood exists that these miscellaneous expenses would be far less in the formation of a special district than in pursuit of any other developmental method. Though the complicated procedures necessary for the formation of special districts are significant, they are fairly predictable and can usually be minimized by retaining a first rate law firm, with experience in this area, to assist in the
establishment of the district, i.e., securing regional permits, the election and issuance of bonds, and contracting for needed improvements.

HIGH RATE OF DISTRICT BONDS/DAMAGE TO MUNICIPAL CREDIT

The criticism that water districts must pay a higher rate of interest for the money it borrows than large cities with sound fiscal structures cannot be refuted. The criticism is based on the fallacious assumption, however, that the water district and the municipality are competitive, rather than complementary, instruments for developing water, sewer and drainage facilities.

Since the alternatives generally facing suburban residents living outside the corporate limits of Texas municipalities appear to be between water districts, private utilities or individual septic tanks and wells, the significant question is the relative cost of borrowing among these alternatives. As a general rule, the water district can raise capital more cheaply than the homeowner, the developer, or the private utility. This ability of the water district to borrow on better terms and interest rate than its competitors is attributable to two powers of the water district:

1. Its ability to issue tax-exempt bonds, and
2. Its ability to levy public taxes upon its residents.

The mistake is often made of assuming that a high rate is paid for borrowed funds because that rate appeared on the notice or on the ballots of the bond election as a maximum rate. No instance could be found of a water district in the Houston area paying an interest rate over 9% on its bonds and a recent offering, a million dollar bond issue on WCID 140 on February 29, 1972, had an interest rate of .6.68%.
The interest rate that city of Houston bonds would bring on the same day was estimated to be 4.75%. This difference in interest rate reflects the realization among investors that water district bonds are more speculative in nature than rated municipal bonds.

Whereas only one Harris county district has ever defaulted on its bonds, there have been problems with district use (or misuse) in other parts of Texas. About 1952, a series of very large districts were promoted in Travis county (Austin) by a group of mortgage bankers, lawyers and engineers apparently interested in the professional fees involved. The districts averaged about 3000 acres and were sparsely settled. No development was contemplated and it is clear that they were ill advised because it was impossible for the bond debt to be paid from the tax base reasonably anticipated. That the districts were ever formed is a curiosity in light of the statutory requirement instituted in 1925 that all proposed districts be reviewed as to feasibility by the TWRC. A more stringent review procedure is now used by the Commission, and since 1963, the city has been a second level of review.

The credit rating of Houston was recently elevated from A-1 to AA status, a move that reflects no disapproval by the rating services of Houston's policy of tolerance toward water districts. If the use of promotional districts has an effect on the credit rating of larger municipalities, it may be a beneficial one. The ability to annex areas already served by first rate utility systems and to acquire them when a sufficient tax base has been established is immensely more beneficial to a city's financial position than to annex raw acreage or tracts with substandard utilities.
2200 FOOTNOTES


2. Ron Heiser, Assistant Director, Houston City Planning Department, personal interview 2/2/72.


5. Charles Lee Schroer, "Water Control and Improvement Districts", page 726.

6. James Gustafson, President, Gustafson Group/Real Estate, lecture to class in Urban Law, Rice University, 2/11/72.

7. Burrell Rowe, partner with Smith, Rowe, Fisher & Hay; attorneys, telephone interview, 2/25/72.


9. Services performed by the Municipal Bond Department of Underwood Neuhaus & Co., as per John Fainter, Manager, personal interview, 1/31/72.

10. Cyril Smith, partner with Smith, Rowe, Fisher & Hay; attorneys, personal interview, 2/24/72.


13. Frank Ildebrando, telephone interview, 2/24/72.
Most of Houston's growth has occurred in peripheral land areas. The fiscal strength of the city is largely due to liberal annexation powers enjoyed under Texas law. This power has enabled Houston and many other Texas cities to absorb areas with new tax base through periodic territorial expansion. This continuing expansion has been possible because relatively few suburban incorporations occurred. Water districts operating beyond the city limits provided basic but limited municipal services before these areas were sufficiently developed to need or sustain the burden of full municipal services. Water districts, by serving as precursors to municipal government, removed the major incentive to incorporate. For years before the Municipal Annexation Act of 1963 granted control over the formation of suburban governments to Texas cities, this effect was largely responsible for saving not only Houston, but several Texas cities from encirclement by small suburban municipalities. The relationship benefited the city because encirclement by a proliferation of water districts is temporary in that districts, unlike smaller municipalities that might perform in their absence, can be annexed at will.

Reference to illustrations 2300-1 and 2300-2 indicates that the number of surrounding municipalities in Dallas, a city without a history of tolerance to promotional special district use, vastly exceeds the number in the Houston area. Further evidence that this relationship was played upon can be had by reference to the standard contract in use by the city of Austin prior to 1963 for the sale of water to suburban water districts. A provision of the
contract states:

"This contract shall be automatically terminated in the event District sells or delivers water to any customer at any point which is within any city, town, or village other than the City of Austin."
SOURCE: Municipal Advisory Council of Texas (various reps reports)
liability for several years. Since this time, critics have complained that annexed water districts are consuming funds from the city's general fund to subsidize the retirement of the district debt. Auditors from the firm of Phillips, Sheffield and Luther were hired by the city to investigate and several instances of irregularities and conflicts of interest in contracting procedures were indicated among district directors. Partially as a result of this publicity, the following safeguards were enacted or established:

1. The 1963 Municipal Annexation Act gave cities the authority to exercise some supervision over water districts and city approval is conditioned on agreement by the water district to comply with the rules and regulations of the city planning department and to allow city inspection of construction.

2. To terminate the practice of a developer installing needed improvements as an unregulated private utility and selling the improvements to the district at an exorbitant price, the Texas Water Rights Commission adopted rule 650.1 note 2 which prohibits districts from purchasing completed facilities without express special permission.

3. The Texas Water Rights Commission has adopted the practice of sending a representative to selected bid openings unannounced. This practice has discouraged irregularities in analysis of competitive bids.

With the adoption of these provisions, the established cities are no longer threatened with encroachments in their hinterland by other incorporations. With the threat of municipal encirclement removed, cities are no longer forced to rely on premature annexation. Districts can now be allowed to financially ripen to the point that they are net assets upon annexation. It is clear that assessed valuation increases with district maturity while the bonded debt is constantly being retired. At some point an annexation beneficial to the city can occur. Over the long run, annexed water districts have clearly been a net asset to Houston.

Many of the criticisms of water districts heard today stem from the magnitude of the 1956 annexation and problems attributed to the lack of regulation of the districts absorbed into the city at that time. The belief is still
encouraged that water districts are unregulated free agents which operate
outside the framework of cooperation between other units of local govern­
ment. In contrast to this image, a working partnership between cities
and water districts has evolved and was observed to be functioning in Houston
as well as several other Texas cities.

2330 ASSERTION THAT DEVELOPERS AND BUILDERS MAKE EXCESSIVE PROFITS

The contention that builders and developers make excessive profits on
developments served by water districts is based on an idea that lots are
sold at prices that are not adjusted to reflect the developers' deferment
of the expense for utility improvements. Whether such charges are true
depends upon the extent of monopoly in the residential construction industry.
The home construction industry has generally been considered one of the
nation's most fiercely competitive industries. It is characterized, par­
ticularly in Houston, by the presence of a large number of small and aggres­
sive firms. Furthermore, the ability of developers to sponsor water dis­
tricts and thus launch large residential projects would tend to increase the
supply of housing and keep down the cost of lots. The validity of this
reasoning could not be thoroughly tested, but a comparison of residential
lot prices between Houston and the Dallas/Fort Worth area, where districts
are seldom tolerated, seems to verify the conclusion.

2340 FACTORS AFFECTING MAXIMUM DISTRICT SIZE

Of the special districts formed annually in Texas, between 75 and 90 per
cent are located in or around the Houston metropolitan area. This is
explained by the two phenomena of ready availability of subsurface water
and developmental incentives and pressures created by a steadily growing
population. Based on the Houston experience, the single most important aspect of successful water district operation in the early developmental stages is control.

The developer nominates the first five directors carefully, considering their allegiance to him and their interest in promoting and financing the project. The statutes provide, however, that a director's term of office shall be two years and that an election for two of the five directors be held on the second Saturday in January following the confirmation election. An election for the other three positions is held on the second Saturday of the second January after the confirmation election and so on in continuing sequence. \(^\text{13}\) This feature and the two year term of office limits the length of time for which the developer's nominees will go uncontested in their director's chairs.

The experience of Friendswood Development Company with the Clear Lake City Water Authority is particularly illustrative of what can happen when the developer loses control prematurely. The Clear Lake City Water Authority was formed in 1963 and is a special law water district which includes 12,268.85 acres. The developers chose to form a single large district rather than a series of smaller districts because of the following circumstances: \(^\text{14}\)

1. The Houston City Council and administration from whom approval for formation was required under the Municipal Annexation Act were at that time ill disposed toward the use of special districts. This sentiment was largely a result of the 1956 annexation and the resulting controversy. The developers felt that in this climate a single large district would have a better chance for approval than a series of smaller districts.

2. Certain economies of scale could be had by comprehensive treatment of the improvements and an improved bond rating by Moody's Investment Service and other rating agencies, resulted in a lower bond interest rate.
3. A lack of experience in dealing with larger districts failed to alert the developer to the danger of premature loss of control. The developer believed that good relations would be maintained with the early homeowners by conscientious efforts and that problems could be easily averted.

The development of Clear Lake City served by the Clear Lake City Water Authority proceeded according to plan for about four years. At that point, the board of directors, which was by then controlled by the new residents, began interfering with the activities of the developer. The interference was primarily manifested by the following:

1. Delays in approving the extension of service to several new sections which had obtained all other required approvals and were otherwise ready to proceed.

2. Conditioning the services of the Water Authority on elaborate concessions from the developer such as dedication of parks and playgrounds that had not been anticipated.

The effects of the delays resulted in a disastrous loss of sales momentum by the developer and had an adverse effect on the return realized for the entire project. This example was sufficiently strong to demonstrate the fallacy to all developers anticipating the use of promotional districts in future years. Based on common sense and the experience of Friendswood Development Company with the Clear Lake City Water Authority, Houston developers have uniformly adopted the practice of limiting the size of predominantly single family residential water districts to four or five hundred acres. This size has been found by trial and error to be well suited to the housing absorption rate in this area, thus enabling the developer to "build-out" in a project before he relinquishes control of the district to the new residents.

CONTROLS OVER DISTRICT OPERATION

In order for a sewage disposal system to be operated, a waste disposal permit
must be obtained from the Texas Water Quality Board. The permit must be renewed periodically and the plant is subject to periodic inspection to insure compliance with the terms of the permit. Because of this requirement, the Texas Water Quality Board is the primary state agency for operational control of water districts as well as other entities engaged in sewage treatment or disposal operations.

In the past, it was common for each district to have a package sewage treatment plant and to hold a waste disposal permit for its operation from the Texas Water Quality Board. Recently, the extent of development in some areas and the resulting pollution of water courses pointed out the inherent inefficiency with which small treatment plants are operated. In an effort to correct this situation, the Houston-Galveston Area Council acted under its mandate to accomplish regional planning and adopted an "Official Regional Interim Plan for Collection, Treatment and Disposal of Domestic and Industrial Waste". Because of the lack of enforcement power by the H-GAC, the Texas Water Quality Board has assumed this responsibility. Enforcement is accomplished by requiring a pledge of compliance with the regional plan as a prerequisite to the granting of a permit.

By threat of withholding or delaying approval of a waste disposal permit, the H-GAC and Texas Water Rights Commission have brought pressure to bear on developers inclining them to cooperate in planning for the activities of the water districts created to serve their projects. It is no longer uncommon for several developers to agree that one will build a large sophisticated treatment plant and the others will transmit their sewage for treatment under a contract. A factor easing the burden of compliance is the availability of federal 55% matching funds under Public Law 660 for construction of the transmission lines.
In some parts of the Houston metropolitan region, growth is taking place at a greatly accelerated rate. In the Cypress Creek watershed, the number of water districts created almost doubled between 1970 and 1971. With each district operating a low efficiency package sewage treatment plant, the problems of water pollution became particularly acute. To correct this problem, a plan was adopted by the Texas Water Quality Board in Board Order 69-54 issued on November 21, 1969. The Board Order stipulates that ownership and operation of all sewage treatment facilities within the Cypress Creek watershed would be by the San Jacinto River Authority.

Water districts function routinely under this plan except that they are now compelled to transmit their sewage to a subregional plant for treatment under a contract with the River Authority. Each subregional sewage plant is built in accordance with the H-GAC regional plan to serve several water districts. Thus, the source of financing continues to be from multiple jurisdictions but the functions are consolidated. The subregional plants are paid for proportionately by the served districts but are owned and operated by the River Authority. Each subregional plant site is adequate for conversion to tertiary sewage treatment when required.

One effect of the Cypress Creek plan is that developers whose projects are served by water districts have less autonomy than they previously enjoyed. In order to avoid impeding development, the River Authority allows the earlier water district in an area to use package treatment plants in the interim while the subregional plant is being constructed.
As the district must pay for the interim plant, as well as their pro rata share of the subregional plant and the transmission lines, some hardship is experienced by tax payers in "pioneer districts". However, some of the initial expense is reimbursed as the salvage value of the package plant is about 50% of its cost and monthly sewage costs should reflect the increased operating efficiency of the larger treatment plant. It is ironic that several recently formed districts have received adverse publicity because of the seemingly excessive amount of bonded indebtedness when the extra expense was incurred in the process of complying with the regional waste disposal plan.

A second effect of the plan is that smaller developments will become feasible under conditions that do not require enough units to justify a package plant or application for a waste disposal permit.

The plan is working well in the Cypress Creek area and the San Jacinto River Authority plans to assume operation and ownership of other sewage treatment facilities in its jurisdiction. The Gulf Coast Waste Disposal Authority and other regional Texas authorities are adopting similar practices.

In the natural course of events, the new residents of an area will assume control of the water district board of directors. The transition is eased somewhat by the provision for overlap between old and new directors. In this way, the outgoing directors have an opportunity to inform the new directors about the operation of the district.

Intergovernmental contracting for water supply and waste water treatment
is becoming increasingly common and has averted many of the transitional problems of the past. This method of discharging district functions eliminates, in many cases, any necessity for the directors to be concerned with troublesome operational problems or the necessity to maintain a staff.

A second practice, which minimizes the transition difficulty and establishes continuity, is the comprehensive professional services offered by the better law firms and now by at least one brokerage house. For an annual fee, these agents will perform bookkeeping services, keep tax records, offer legal and tax advice and perform generally in a pilot capacity to offer needed advice in all aspects of district management.

The second transition of control occurs when the district is annexed by a municipality or consolidated with another special district. This transition is accomplished with the same ease as the district is simply dissolved with all assets and liabilities assumed by the annexing government.
2300 FOOTNOTES

1. Letter with enclosures from Curtis E. Johnson, Director of Water and
Wastewater Department, City of Austin, 3/29/72.

2. Alan D. Carey and John P. Owen, "Water Districts; An Asset or a Liability?", The Houston Homebuilders Association, (March, 1959), page 23.

3. Tax Research Association, "Water Districts in Harris County," (Mimeographed, February, 1969), page 7. (footnote pertains to statistic only.)

4. Ibid. page 12.


6. Alan D. Carey and John P. Owen, "Water Districts; An Asset or a Liability?" page 98.


8. Ron Heiser, Assistant Director, Houston City Planning Department, personal interview, 2/2/72.


10. Alan D. Carey and John P. Owen, "Water Districts; An Asset or a Liability?" page 55.


13. VATS Water Code Volume, Section 54, 103.


15. Ibid.

16. Ibid.

18. Ibid.


20. Cypress Creek Plan, authored by Don Howell of Vinson, Elkins, Searls & Connally; attorneys, as per telephone interview with Bill Evans, Staff Engineer with San Jacinto River Authority, 3/28/72.


Evaluation of the Houston Experience

As indicated in previous chapters, several objectionable aspects of water district use which existed some years ago have long since been cured by the Municipal Annexation Act of 1963 and other enactments. Revised administrative procedures by cognizant agencies have solved other related problems. Unfortunately, opponents of their use sometimes fail to take note that these solutions have been affected. In addition, a number of erroneous characteristics are attributed to the use of water districts.

Bond indebtedness is one of the economic facts of life that must be faced today by all levels of government if the ever increasing demands for services are to be met. A dominant theme arising from this investigation of water district activity in the Houston area was that water districts have become the predominant means for meeting demands for service to an expanding population. It is estimated that perhaps 85% of the residential development that occurred in the Houston SMSA in 1971 was assisted by a water district. From the preceding description of water district development and operation in the Houston area, a pattern of special district characteristics has emerged. In spite of the imperfections pointed out herein, the practice of special district use has been essentially beneficial to the developers, the home buyer and the central city. The following recapitulation of the salient characteristics and problems that have surfaced in the investigation of the local situation seems appropriate:
1. Prior to the 1963 Municipal Annexation Act, an opportunity existed for developers and city politicians to enrich themselves at the expense of the annexing city. Because there was no restriction on the amount by which bonds could be discounted, those which were about to be redeemed by the city at par upon annexation of a district could be purchased at a substantial discount by individuals with privileged information. Cities now have the prerogative to limit the discounting of district bonds within its extraterritorial jurisdiction.

The absence of city power to inspect the construction of suburban facilities offered an incentive for the developer and the contractor to install a substandard system and split the difference in costs. City prerogative to inspect water district construction within the extraterritorial jurisdiction has lessened the likelihood of this occurrence.

2. The speculative and promotional nature of water district use has often been assailed. There have been several instances in which water districts have defaulted on their bonds and damage to municipal credit has been alleged. The relatively high interest rate paid by water district bonds as compared to most municipal bonds represents, to critics, a high cost of borrowing.

The somewhat speculative nature of most projects served by water districts is acknowledged. The very nature of the use to which they are put is less secure than the support of an existing population. However, the feasibility of each water district is now subject to several levels of review. Automatic review by the Texas Water Rights Commission and the Attorney General's office at the state level is required. If the district is within the extraterritorial jurisdiction of a city, it is also subject to the review at that level. In several of the more rapidly urbanizing regions, a review is required by the regional authority having jurisdiction. Compared with the other alternatives for financing needed improvements in developing areas, the water district option is certainly the most closely regulated. When compared with developer financing or the private utility alternative, the water district is clearly the least expensive medium through which to borrow the necessary funds.

3. The proliferation of water districts in several rapidly urbanizing parts of the state has been listed as a problem. The problem seems to arise as a result of the multiplicity of small, inefficient waste disposal plants rather than as a problem of political jurisdiction. Increasing numbers of water districts as political entities appear to be no problem because the water districts, unlike general units of local government which might perform in their absence, can be easily consolidated or annexed into another government when they have served their establishmentarian purpose. Functionally, the proliferation of small and relatively inefficient sewage treatment plants leaves something to be desired, but either the use of septic tanks or uncontrolled private utilities would have been even less desirable alternatives. The "Cypress Creek Plan" and other efforts at regionalizing urban waste disposal
promise to co-ordinate the functioning of water districts in the future.

4. An argument sometimes advanced is that districts prey upon the financial resources of an area by unilaterally determining their budgets and therefore are not subject to a machinery for balancing allocations of these resources among all of the competing service needs which prevail in the metropolitan area. The following is an excerpt from the Texas Municipal Report on Wilcrest Improvement District and is representative of the number of taxing jurisdictions that might overlap in a similar situation throughout the state:

<table>
<thead>
<tr>
<th>TAXING BODY</th>
<th>AMOUNT</th>
<th>AS OF</th>
<th>% APPLICABLE</th>
<th>A AMOUNT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Harris County</td>
<td>$88,762,751</td>
<td>6/30/69</td>
<td>0.03</td>
<td>$26,629</td>
</tr>
<tr>
<td>Harris County Flood Control</td>
<td>$20,410,954</td>
<td>6/30/69</td>
<td>0.03</td>
<td>$6,123</td>
</tr>
<tr>
<td>District</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Harris County Hospital</td>
<td>$3,430,418</td>
<td>6/30/69</td>
<td>0.03</td>
<td>$1,029</td>
</tr>
<tr>
<td>District</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Harris County Houston Ship</td>
<td>$9,508,544</td>
<td>9/30/69</td>
<td>0.03</td>
<td>$2,853</td>
</tr>
<tr>
<td>Channel Naval District</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Houston Ind. School</td>
<td>$181,791,867</td>
<td>8/31/68</td>
<td>0.05</td>
<td>$90,896</td>
</tr>
<tr>
<td>District</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Net Overlapping Debt</td>
<td></td>
<td></td>
<td></td>
<td>$127,530</td>
</tr>
<tr>
<td>Wilcrest Imp. District</td>
<td>$1,662,467</td>
<td>6/30/69</td>
<td>100.00</td>
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</tr>
<tr>
<td>Total Direct &amp;</td>
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<td>$1,789,997</td>
</tr>
<tr>
<td>Overlapping Debt</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note that in the Wilcrest example, six jurisdictions levied property taxes. If Wilcrest Improvement District were annexed to Houston, the City of Houston would replace the Improvement District leaving exactly the same number of taxing jurisdictions as before. Because promotional districts serve as sub-municipal entities, this criticism does not apply. The counterpoint to this argument is that the use of smaller taxing jurisdictions provides an eminently equitable method of assessing those directly benefited for the cost of the improvement.
5. It has been alleged that developers and builders fail to adjust the selling price of lots to reflect the deferment of water, sewer and drainage improvements. The competitive nature of the business and a comparison of lot prices in Houston and elsewhere tend to dispel this notion.

2420 AREAS FOR IMPROVEMENT

The third category of issues are those real imperfections for which remedies have not yet been affected. In each instance an improvement which seems to be in order is proposed:

2421 Nature of the First Bond Election

The nature of the initial debt of the water district does not seem to fit the common conception which has been broadcast by the Houston Post and other members of the news media with such misleading headlines as "Millions in Bonds Authorized by as Few as Two Persons." Such language by a city newspaper says by implication that the debt is upon the public at large or upon the citizens of the city. Essentially the owners of land in a water district, in having a bond issue passed, are merely incumbering their own land with debt. By subdividing and conveying this same land to others, the original owner is accomplishing no act of subterfuge. In a credit society, it is not uncommon to convey improved real property which is incumbered with tax liabilities in addition to whatever liens might be outstanding. Article XVI, Section 59(c) of the Texas Constitution requires that all bond elections in political jurisdictions be voted by resident electors in that jurisdiction. Because promotional district bonds are usually sold to harness land owned by a single individual, partnership or corporation with debt, the district cannot function in a democratic way during the developmental phase of its existence. What is
required is an oligarchy that transforms itself cocoon fashion into a democratic government as it matures.

Because the district cannot function as the constitution and the election code require, the developer is compelled to masquerade his operation as democratic, thus making a mockery and a sham of the required proceedings. The developer must perform such suspicious acts as placing employees or associates in residence in the district, occasionally in temporary quarters, to qualify them to vote in the bond election.

Proposal:
A constitutional amendment is needed authorizing jurisdictions with no resident voter to hold the bond election with non-resident land owners as electors. If an amendment relieves the need for an election by resident voters, but an election by non-resident voters proves onerous for some reason, willingness on the part of the land owners to incur and be responsible for the bond debt could be recorded through a deed of trust, thus eliminating the need for the election altogether.

2422 Risk Born By Early Residents
Because the American property tax places most of its emphasis on real estate improvements, the early residents risk being held responsible for a greater than normal share of the debt if the subdivision fails to develop as planned. In acknowledging this problem it must be pointed out that it has been over emphasized by reports such as one indicating that WCID 84 has "thirteen water customers who each owwed $73,077 toward the debt". This report is clearly erroneous as it assumes that the thirteen home owners in the district are shouldering the burden of the debt alone. It ignores the fact that the developer and other owners
of unimproved lots must pay their share of taxes to retire the district debt.

Further delving into the record of WCID 84 indicates that the plight of the thirteen homeowners is far less serious than would be indicated by the above report. For the same period of time that the article was written, WCID 84 charged a tax rate of $2.00 per $100.00 valuation based on valuation at 100% of market value. While this rate is high, it is not confiscatory. If each of the thirteen houses was valued at $30,000, their individual water district taxes would be $600 and their combined annual contribution would be $7,800. The total tax levy for 1968, the year in question, was $61,079 which indicated that $53,279, or about 87% of the tax bite was felt by the owners of undeveloped land.

It is interesting to note that the extent of the additional taxation risked is perhaps the difference between a $1.00 and a $2.00 tax rate. On a $30,000 house, this amounts to $300 per year and is insignificant compared to the risk of greatly diminished property values if the subdivision fails.

Proposal:
The Texas Water Rights Commission should require that in all developer districts, the owners commit themselves to install the nonutility improvements such as streets before granting approval to issue bonds. Though the commitment need not be for concurrent installations, it would give more assurance that the total development will be carried out. This procedure would not completely remove the early owners from peril, however slight it might be.
If special assessment authority were included in the powers of the district, the citizens could cause the district to assess a "standby charge" against all undeveloped land to supplement the tax levy.

2423 Lack Of Continuing Supervision By Regulatory Agencies

Many water district experts insist that autonomy of operation, the grass roots control of water districts, and their imperviousness to excessive bureaucratic meddling constitute perhaps their strongest advantages. After formation and bond election, districts operate almost as if they were private corporations whose list of stockholders includes all land owners within their boundaries.

Arguments in favor of continued efficient and businesslike operation by the districts are convincing and it is with caution that this subject is approached. However, the problems of water supply, pollution and wasteful duplication of functions and facilities are expanding in proportion to the extent of urban growth. The need to order the functioning of small jurisdictions becomes increasingly clear.

Proposal:

The Texas Water Rights Commission is vested with the needed regulatory power. A sufficient state appropriation should be made to equip them to exercise their powers. As soon as this is done, the commission should:

1. Promulgate rules to require uniform accounting and annual auditing procedures including among other items, pertinent information on:

   a) Insurance in force
   b) Income
   c) Expenses
   d) Water and sewer rates
   e) Tax rates and per cent of collection

2. Require other information reports on a quarterly or semi-annual basis.
3. Investigate promptly incomplete, erroneous or late reports and assess penalties for violations of rules.

The Commission should also decree that in areas served by a regional authority, waste disposal permits will be issued only to the authority for exercise on behalf of the water districts and other customers within their cognizance. This action would assure surveillance over the operation of the sewage plant through an intergovernmental contract between the district and the regional authority.

2424 Absence of Fire Protection

In the case of Orange County WCID v. Deason which was decided by the Texas Supreme Court in 1952, the fire fighting function of water districts was declared unconstitutional due to the court's opinion that the state constitution was not sufficiently broad to allow this power. Since that decision, the lack of fire protection has been the largest gap in the infrastructure of sub-municipal services provided by water districts. The same limiting aspect of the state constitution precludes the operation of county fire fighting units. Only the option of using volunteer fire departments remains. At this time, at least one volunteer fire department is refusing service to some residents of water districts who have not adequately contributed to its support.

Proposal:
Passage of a constitutional amendment to broaden the provisions of the constitution to allow exercise of fire fighting power by any unit of local government seems to be indicated. As an interim measure, ownership of property in a district, or in several contiguous districts, could be made conditional to membership in an automatic homeowner's association or trust. A person buying or renting property in the area would automatically
become a member of the association and be subject to dues or assessments based, for convenience, on the tax valuation records. These assessments could be used to support a fire department as well as various other community buildings and service facilities. Like the water district, the board of directors of this private, nonprofit corporation would initially be controlled by the developer's appointees with the residents, in time, gaining control.

Use Of Bond Principal To Pay Interest

Section 54.511 of the Texas Water Code provides in part that:

The district may use bond proceeds to pay interest, administrative and operating expenses expected to accrue during the period of construction which shall not be more than three years...

This aspect of the water district operation grew out of a problem inherent to the nature of development; the improvements and facilities must be provided for anticipated demand at a time when property values and economic activity do not produce sufficient revenue in the form of ad valorem taxes to support such expenditures. As an administrative policy, the Texas Water Rights Commission now allows only two years of interest payments from principal. Although this option has been almost uniformly exercised by promotional districts, the provision itself and practices which it permits have been responsible for much of the criticism and ill will directed at promotional water districts. The two salient points of criticism are:

1. By servicing the bond debt and operational costs largely or entirely from bond proceeds during the sales phase of a project, a developer can create an illusion of low taxes which has a beneficial but deceptive marketing effect.

2. The practice has the effect of discounting the amount borrowed, thereby increasing the real interest rate on the bonds, which must be paid by the homeowners who inherit the assets and liabilities from the developer.
The following example of the discounting effect of this practice is based on figures taken from the Texas Municipal Report and on the 1971 Annual Audit of Wilcrest Improvement District. Because there were two separate bond issues at different times and different interest rates, an average interest rate is imputed. For simplicity, the two bond issues were considered as one issue bearing the average interest rate:

Interest paid annually on actual bonded district debt of $2,965,000 for two years during construction at a stated interest rate of 7.096% = $210,000

Interest during construction period of two years at $210,400 per year = $420,800

Actual bonded debt necessary in the absence of a need to meet interest requirements from bond principal $2,965,000 - $420,800 = $2,544,200

Effective interest rate generated by annual interest based on necessary debt. $210,000 ÷ $2,544,200 = 8.269%

Excess of effective interest over stated interest 8.269% - 7.096% = 1.173%

Because our present system of ad valorem taxation places heaviest reliance on the improvements to land, a reasonable tax applied to the developer's vacant lands in the earlier years would seldom raise enough revenue to pay all of the interest on the bonds leaving a portion of the interest, the sinking fund for payment of bonds, and other miscellaneous charges to be taken from bond principal.

Proposal:

By requiring the levy of a reasonable tax during development, the developer may be made to sustain a part of the interest and sinking fund during the construction phase, thereby decreasing the debt burgeoning effect that failure to do so has on those who fall heir to the assets.
and liabilities of the district. The Commission, in approving the feasibility of bonds, should determine and require the district to levy a tax roughly equivalent to the rate that will be required after development.

The water district is theoretically separate and distinct from the developer's business and technically, the accounting propriety of charging the interest on district bonds during the construction phase as a capital cost is unimpeachable. However, the situation is colored by the fact that the developer has essentially chosen the first board of directors and the district is performing a service that he would perform under other circumstances. For all intents and purposes, the water district is an operating division of the development company during the early years. Consequently, it would seem only logical to require that the developer be responsible for payment of a reasonable tax on his vacant land and inventory of unsold units while the water district is under his operational control. The possibility is recognized that forcing the developer to incur this additional cost may have the indirect effect of raising the selling price of the units slightly, but it is deemed worthwhile because it discourages fly by night or low budget operators and removes a source of criticism.

As further reasons for this reform, it is suggested that making the developer responsible for the payment of reasonable taxes in early years would provide an additional incentive for frugality in causing initial district expenses to be incurred. The deceptive marketing practice of selling units during an unreasonably low tax period would be curtailed, and the discounting effect of supporting interest payments with bond principal would be lessened.
The charge has been levied that attorneys and consulting engineers have made excessive profits on the formation of water districts. Consulting engineers to the water district generally charge a fee that is calculated as a percentage of the cost of the construction of the project. The fee schedule most frequently used is the one recommended by the *Manual of Professional Practice of the Texas Society of Professional Engineers*. Fees are proportional with construction cost, and the paradox thus created is that the better the engineer performs his service, the smaller his fee becomes. As the developer pays none of the water district costs, the original developer oriented board of directors is not particularly motivated by the circumstances to exercise watchfulness in this regard.

Although lawyers serving the water district are not bound by a schedule of fixed fees, the water district has easy recourse to others if the fees of one lawyer should appear exorbitant.

High engineering and legal fees would increase the bonded debt that a district must incur and reduce the salability of the bonds by raising the ratio of bond indebtedness per resident. From this point of view, developers and bond underwriters do have reason to keep engineering and legal fees at reasonable levels.

Although it is undeniable that excessive fees have occasionally been paid to consultants, it should be noted that criticisms of an equally serious nature are frequently made about other governmental agencies. From time to time, city, county, and national officials, both elective and appointive,
come in for criticism on the grounds of bad judgement or illegal al acts. So long as the governmental units of any nature are operated by i individuals there will be abuses of power.\textsuperscript{14}

**Proposal:**
Requiring the levy of a reasonable tax from the first day of operation would offer an incentive to the developer to minimize district expenditures generally and specifically to curtail excessive consulting:ing fees. A statutory requirement for disclosure of the amount of water district debt related to any property offered for sale within a district wct would constitute an additional strong incentive.

2430 LAND VALUE TAXATION

Many of the results sought in the foregoing proposals for improvement could be realized by the use of *land value taxation*.\textsuperscript{15} This method of taxation practiced in varying degrees in other countries and recently initiated in Hawaii, places substantially heavier tax rates on lar land than on building, thus placing a greater share of the tax burden on our owners of undeveloped land. By use of this device, the problems of risk to to early residents and payment of interest from principal could be directly remedied. The use of land value taxation has several beneficial effects in that it discourages the holding of land speculatively and removes the penalty for improvement that exists under the standard ad valorem practice. Unfortunately, Article III, Section 48 of the Texas Constitution con contains a requirement that taxation be "equal and uniform" and consequently, a constitutional amendment would probably be required to allow the use of this method of taxation.
The use of special districts clearly has relevance to new areas of urbanized territory just developing their own governmental structure. A careful examination of the Texas version of promotional special districts has indicated that they are particularly well suited for use in a variety of developmental situations. Because of their somewhat restrained powers, by comparison, Texas districts have managed to avoid certain pitfalls and problems experienced in California.

Because of certain abuses in California, the use of promotional special districts in that state has been regulated to such an extent that its potentiality for functioning as an efficient land development vehicle has been greatly impaired. In curing the several shortcomings in Texas law, as it relates to water districts, caution must be exercised to avoid a similar outcome.
2400 FOOTNOTES

1. Robert W. Travis, "Use of Water Districts in the Development of Land" (San Jose State College, Business School, 1963), page 1.


3. Chatters, "Is Authority Financing the Answer?", The American City, (1955), page 70.


12. Alan D. Carey and John P. Owen, "Water Districts; An Asset or a Liability?" (Houston Homebuilders Association, March, 1959) page 57.

13. Ibid. page 57.


3000
Urban Growth and Regionalism
The list of urban problems in America seems limitless and it is impossible to determine with precision each link in the chain of reactions caused by the rapid increase of urban population. The growth of the national population itself and the extent to which it is urbanized are perhaps the only phenomena that can safely be identified as the central cause of the problem. In spite of the fact that urban growth is often characterized as a particularly problematic phenomenon, it seems safe to predict that it will continue well into the future.

The primary factor influencing the continuance of urban growth is the existence of a correlation between population growth and median family income. The greatly enhanced economic vigor and level of personal opportunity that results, at least in part from the process of urban growth, encourages the further concentration of economic activity in given areas creating what has been termed a "herd effect". The ability of a community to grow depends on its ability to attract additional spending. Every dollar attracted has a "multiplier" effect on community income. This means that for every dollar of spending in a particular community, the income of the area will eventually increase by a multiple which is determined by the portion of additional income generated that is resident in the same community. The multiplier effect is likely to be greater in large, industrially diversified and relatively self-contained communities than in smaller areas. Population growth
leads to increased demands for goods and services thus raising the level of spending within a community.4

Although economic growth per se has been generally considered to be desirable, it may be argued that there are certain undesirable side effects. Commuting time to work is lengthened, pollution levels rise and a heavier burden of traffic is placed upon the city streets requiring widening of arterial routes, construction of interchanges, and installation of more expensive systems of traffic control. Older residential areas are sometimes left to wither away by the exodus of population to suburbia. The per capita cost of extending certain municipal services to outlying areas tends to rise as the limits of the urbanized area are extended. In spite of these factors, a desire on the part of individuals to experience conditions of economic growth appears to be basic.

Economic growth is associated with a number of other phenomena. Among these are longer life expectancy and higher levels of education attained.5 Regardless of what evil side effects are attributed to economic growth, it is difficult to persuade individuals to give up such basically desirable benefits. Because economic growth is related to urban growth, there is a built in tendency for further concentration of economic activity in given areas. As evidence of this tendency, many agencies exist to stimulate regional economic development. Federal departments and agencies,6 state and local governments, foundations, industries and utilities, chambers of commerce and many others are involved.

In many ways, arguments about the desirability of urban growth are academic because it is clear that substantial growth, in one form or another, will continue for some time. As an indicator, it is estimated by the
Congress that this nation is likely to experience a population increase of about seventy-five million persons during the remaining years of this century. Even under conditions of "zero population growth", it seems reasonable to presume that rural/urban, intraurban and interurban migration would continue to occur thereby creating a demand for growth and development in some areas. The problem, then, is to accommodate the growth that will occur as gracefully as possible.

3120 FACILITATION AND STIMULATION OF GROWTH

The importance of promotional special district use in Texas and in other states has been their ability to facilitate development. Special districts are capable of financing many of the needed improvements and community services thus enabling development to occur. Without their availability, the necessity for the developer to finance these improvements would be regarded as an impediment.

Because the financial burden is borne by those directly benefitted and not by the developer, special districts have the ability to construct the needed improvements in accordance with closely regulated design criteria thus contributing to the health, safety and welfare of the community at large. Because the resulting system is publicly owned, it can be more closely regulated and controlled in terms of technical standards than can private systems. If private systems were relied upon, it could be expected that systems barely adequate to meet immediate demands would be provided. As further development occurred, the original system would have to be modified or replaced. This would be done at a cost many times greater than the additional cost to install a system of ample capacity before development occurred.
There are indications that the use of special districts in the development of land has a stimulating as well as an enabling effect. Certainly, the availability of the district mechanism alone will not cause growth to occur. A certain "critical mass" in terms of developmental momentum is required to even support a bond debt and to justify the risks inherent in development. As an element in an economic development program, special district use is limited to a "balance tipping" effort to activate growth opportunities which already lie just beneath the surface. The stimulation offered by the use of special districts stems from its ability to tap the international bond market as a vast source of credit not otherwise available for assisting urban development.

Most residential development in the Houston area is assisted by water districts whereas districts are not permitted in the Dallas area. Although the comparison of housing starts and the per cent of change from the previous year in these two cities is not offered as proof positive that the use of water districts has a stimulative effect on housing production, the comparison is illuminating.8

<table>
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<th></th>
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</tr>
<tr>
<td>Dallas</td>
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</table>

THE FORM OF FUTURE GROWTH

Much of the body of planning literature is vague on the definition, causes and effects of urban sprawl. The term has been used to describe several phenomena including the general low density extension of the urban fringe, strip or ribbon development along transportation routes and discontinuous or "leap frog" development. By use of this term, peripheral growth
is often incorrectly described and implicitly classed as a detriment to society. Upon closer investigation, sprawl development appears to have a much more complex and dynamic nature than the usual characterizations would lead one to believe. After careful analysis, it seems inconclusive that the pattern of development characterized as sprawl is socially un-economic or undesirable in the long run.9 There appear to be some aspects of sprawl which are beneficial. Among them are these:

1. Sprawl development may be an efficient mechanism for "banking" land for future development at a higher order of use.

2. Discontinuous development insures that improvements over a vast area do not become obsolete at one point in time.

In spite of these long range considerations, there are undesirable effects on the central city jurisdiction which is partly responsible for promulgating the pattern:10

1. Development of vacant land within the city and in its immediate fringe area is discouraged.
   a) As property taxes on undeveloped land are low, vacant tracts within a city are to be looked upon as tax liabilities. Though they consume few city services, they consume space and require greater effort in delivering services to other users.
   b) The tax liability exists in relative as well as absolute terms because the opportunity cost of retaining vacant land is the exclusion of a potential tax generating development.

2. Annexation of substantial developed areas provides for a healthy urban tax base.11 As annexation of vacant land is undesirable, a continuing program of annexing fringe areas is made more difficult by encouraging the dispersion of development.

3. As buildings become older, they develop into fiscal deficits while new investment in land improvements tend to be fiscal surplus generators. By failing to structure incentives to promote development of vacant land in town or close in, the central city loses fiscal surplus generators and inherits the fiscal deficits.12

4. As residential development is pushed outward, it is followed by the manufacturing and commercial construction which represents a much more significant loss in tax base.13

Inasmuch as sprawl might be considered an apparition of a "normal" or "desirable" response to municipal needs, it is appropriate to identify factors
which contribute to its development.

**CONCENTRATION AND DISPERSION**

Public regulation contributes to sprawl by imbalancing the attractiveness of competing areas. This imbalance often evolves through parochial political considerations with little thought to the patterns of urban growth that are encouraged. If the most attractive method for financing improvements is restricted from use in a controlled area and stringent standards and regulations apply only within the controlled area, development may be impelled outside the controlled area thus contributing to sprawl. 14

In the Houston example, the use of water districts is a primary incentive to development. City policy limits the use of water districts to the area beyond the city limits. At the same time, subdivision controls and other restrictions apply which tend to inhibit development within the city and (since the 1963 Municipal Annexation Act) in the extraterritorial jurisdiction. An inordinate amount of vacant yet buildable land is included in the Houston city limits. Figures from the 1970 census show that 47% of the total area is vacant and it is estimated that 95% of the vacant land is buildable. The amount of land involved is nearly two hundred square miles. 15 Though many factors have contributed to this pattern of urban development, the existence of disproportionate incentives for development as illustrated in figure 3100-1 are partially responsible.

Correcting the disproportionate incentives would tend to remove the dispersing effect on development and would encourage a more natural functioning of the free market mechanism in the selection of sites to be developed.
Development Incentives

LEGEND:

<table>
<thead>
<tr>
<th>WATER DISTRICT USE ALLOWED</th>
<th>WITHIN CITY LIMITS</th>
</tr>
</thead>
<tbody>
<tr>
<td>YES</td>
<td>+</td>
</tr>
<tr>
<td>NO</td>
<td>-</td>
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<table>
<thead>
<tr>
<th>SUBDIVISION REGULATIONS APPLY</th>
<th>INSIDE EXTRATERRITORIAL JURISDICTION</th>
</tr>
</thead>
<tbody>
<tr>
<td>YES</td>
<td>-</td>
</tr>
<tr>
<td>NO</td>
<td>+</td>
</tr>
</tbody>
</table>

OUTSIDE CITY LIMITS
This might occur by uniform exercise of building regulations at the regional level and by a city decision to allow the formation and operation of water districts within the city limits.

The policy of Houston and most other Texas cities not to allow the use of water districts within their boundaries appears to be based on concern that inequitable, though not illegal, double taxation will result. In contrast to this practice, at least one smaller municipality in the Houston metropolitan area, Missouri City, has allowed the formation of districts within its city limits. In addition to increasing the city tax base by converting low tax base vacant land to improved property, the practice has mollified any sprawl or dispersal effect that district use might have when such use is disallowed for improvement of "in town" or "near in" properties.

It is recognized that the magnitude of the double taxation problem generally increases as city size increases. In order to allow water districts to function inside larger cities, a system of partial city tax relief for land owners subject to district taxes could be instituted. Though this concept has not been used, it would seem to present no great problem as the city would be furnishing only limited service to these owners. As with fringe districts, the city could simply wait for the bonded debt of the "in town" water district to dwindle to an appropriate level before dissolving that entity and replacing it in the operation of water related utility services. If statutory revisions or constitutional problems delay implementation of this provision, liberal use of refund contracts would partially offset the incentive to develop outlying land.
In addition to disproportionate development incentives, the nearly unlimited availability of sub-surface water has contributed to the pattern of urban development in the Houston area. This phenomenon gives developers freedom from dependency on extension of city water lines for service to new subdivisions. Although water districts have been a primary vehicle for the development of outlying water systems, it is the availability of water and not the developmental vehicle which contributes to the resulting "leap frog" pattern of development.

On the other hand, the established units of general local government have an effective monopoly over the water supply in many conventional developmental situations. This is the case particularly in water short areas because the established government has invested in the construction of some type of elaborate reservoir and watershed system for an uninterrupted supply in times of shortage. Duplication of these facilities is not economically feasible, so developers are forced to rely on the city for extension of service.

In this situation, the developer is not only dependent on extension of the established water system, but he is commonly required to pay a large part of the extension cost as well. Obviously if the developer must finance the provision of utility improvements, a cost he may avoid by forming a special district, this increased demand for capital investment will be passed on to the purchaser of subdivided units in order for the developer to recover from his financial burden. It should be pointed out, however,
that there are several additional inflationary effects which result from
dependence upon a municipal water and sewer system:

a) As in an area subject to zoning, the supply of developable land
is synthetically limited. Assuming that demand for new units
remains constant, the cost of available undeveloped land is
increased. This increase in land cost is also reflected in the
cost of subdivided units. Conversely, the ready availability
of waste disposal and water supply capability on a regional basis
has the opposite effect and makes commuting distance the only real
limitation on the extent of potentially developable land.

b) Fewer developers can be expected to be active under conditions
requiring heavy capital outlay for both land and improvements.
This further limits the supply, thereby influencing the price of
available units even higher. In addition, decreased competition
enhances the opportunity for price fixing or monopoly.

Figure 3200-2 illustrates the limiting effect on the supply of developable
land available in water short areas. It should be noted that the water
district concept as a financing mechanism may function by purchasing water
supply or sewage treatment from another unit of government. Its use is
precluded only by city refusal to contract the needed service.

3160 EFFECT ON HOUSING COSTS AND LOCATIONAL TENDENCIES

It has been shown that special district financing of development costs has
a decreasing effect on the initial price of housing. An interesting aspect
of this effect is that the proportional diminution of unit selling price
is greatest for lower income housing. The phenomenon encourages developer
interest in lower income housing, thus enhancing the supply. As a result,
approximately 75% of all housing units built in Texas water districts over
the past ten years have been sold through either FHA or VA insured mort­
gages. Illustration 3100-3 shows the operation of this phenomenon in
simplified terms.

Reference to the example for a development in the $20,000 price range
MUNICIPAL CONTROLLED WATER SUPPLY

UNLIMITED AVAILABILITY OF WATER SUPPLY

3100-2

Influence of Water Access

LAND WITHIN THE MUNICIPALITY

LAND WITH ACCESS TO WATER SOURCE
## 3100-3

### Per Lot Costs

**Utilities by Special District**

**Utilities by Developer**

**$20,000 Price Range**

<table>
<thead>
<tr>
<th>Item</th>
<th>Special District</th>
<th>Developer</th>
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</thead>
<tbody>
<tr>
<td>Raw Land</td>
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<td>$1,500</td>
</tr>
<tr>
<td>Water Utility</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Improvements</td>
<td>------</td>
<td>1,800</td>
</tr>
<tr>
<td>Other Utility and</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nonutility Improvements</td>
<td>1,000</td>
<td>1,000</td>
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<tr>
<td>Total Cost</td>
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<tr>
<td>10% Developer Profit</td>
<td>250</td>
<td>430</td>
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<tr>
<td>Sale to Builder</td>
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<tr>
<td>Construction</td>
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<tr>
<td>Sale to Home Buyer</td>
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<td>21,230</td>
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</table>

Difference in price: $21,230 - $19,250 = $1,980  
% Difference: $1,980 / $19,250 = 10.2%

### $40,000 Price Range

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</thead>
<tbody>
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<td>$2,500</td>
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<tr>
<td>Water Utility</td>
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<td></td>
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<tr>
<td>Improvements</td>
<td>------</td>
<td>1,800</td>
</tr>
<tr>
<td>Other Utility and</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nonutility Improvements</td>
<td>1,200</td>
<td>1,200</td>
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<td>Total Cost</td>
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<td>10% Developer Profit</td>
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<tr>
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<td>39,050</td>
</tr>
</tbody>
</table>

Difference in price: $39,050 - $37,070 = $1,980  
% Difference: $1,980 / $37,070 = 5.3%
shows that with special district financing of water utility improvements on a 1500 unit project, the total cost to the developer is $2500 per unit X 1500 units or $3,750,000. If the developer is required to finance these improvements he must have access to $4300 per unit X 1500 units or $6,450,000. The difference of $2,700,000 represents about 72% more investment required in the latter situation. As more development activity is likely under lower cost conditions, the supply of subdivided, buildable lots is increased, thereby enhancing the likelihood of "buyers market" conditions prevailing.

A secondary, but important aspect of encouraging developer interest in lower cost units may relate district use to a sprawling pattern of growth. With the cost of water utility improvements removed from the initial cost of the unit, the cost of raw land takes on added importance as the major item of development expense. In order to keep the cost of raw land within required limits, the developer is forced to select land at some distance farther beyond the urban center than he might otherwise choose to do, thereby contributing to a discontinuous, sprawling form of urban growth.
3100 FOOTNOTES


2. Ibid. page 44.

3. Ibid. page 37.

4. Ibid. page 40.

5. Ibid. page 31.


10. Ibid.


16. Ron Heiser, Assistant Director, Houston City Planning Department, personal interview, 2/2/72.

Development of a Regional Urban Growth Policy

REGIONAL NATURE OF THE PROBLEM

The 1970 census showed that America, after growing from a nation of farms to a nation of cities, had become a nation of suburbs. In the decade of the 1960's, the census reflects an increase of 12% in the national population of which fully 75% was absorbed in suburbs. One startling conclusion from the census data is that most of the nation's cities are actually losing population with the exceptions of the Sun Belt cities of Florida, California, Arizona and the Gulf Coast of Mississippi and Texas. Even in the exceptions, the absence of a real decline was often due to a liberal annexation policy. In light of this information, it appears that general units of local government are becoming obsolete as the cognizant authority to plan and co-ordinate urban growth on a regional scale because of their established nature, archaic structure, and, in the case of county government, predominantly rural background.

The United States began to develop an awareness of growing urban problems and the inability of local governments to handle them only recently. The first concerted response to the problem was "creative federalism". This concept prevailed through the Kennedy and Johnson administrations. The programs that were initiated circumvented the states and resulted in direct federal-local compacts. Federal aid to cities came to be regarded in the same way as foreign aid. It was designed to relieve overload on city governments, but failed to confront the problem of poor system design, i.e. that the municipality is not co-extensive with the community. The Demonstration Cities and Metropolitan Development Act of 1966 required
that most applications for federal assistance within a metropolitan area be submitted for review by the state designated regional planning agency or council of government (COG). The states thus regained the prerogative of control. The revesting of this prerogative seems appropriate as only the states can preside over the reorganization of their agencies, the municipalities, counties, authorities and special districts, which administer local government in this country.5

Long before the advent of the COG concept, there was a recognition in Texas that few urban problems could be solved by the individual cities and counties acting alone. As a result, a tradition of reliance on regional special purpose agencies such as river authorities developed. These agencies were created to perform the role of operating "line" programs in specified areas. In addition to these agencies, twenty-three COGs have been established in Texas which now serve 90% of the state's population, according to the 1970 census.6 COGs have been designated as "planning and development clearinghouses," but with voluntary membership and no authority to carry out plans themselves, they are relegated to serving as a planning and co-ordination forum for other established governments.

3220 REGIONAL HOLDING COMPANIES

Walter A. Scheiber, Executive Director of the Metropolitan Washington Council of Governments, recently prepared a position paper entitled, "Regional Holding Company: Next Step for Texas?"7 The paper, which was delivered to a seminar convened by the Texas Governor's Office of Planning Co-ordination, suggests that a working relationship should be established between the COGs, special districts and authorities to capitalize on the strengths of each. COGs are responsive to the local political process and are
concerned with the entire range of problems facing their region while special purpose agencies have the skill, experience and authority to finance and operate individual region wide programs. The purpose of the arrangement would be to create an interlocking directorate within the governing bodies of the COG and each operational agency, thus tying all regional service agencies together and giving the regions' local elected officials the major policy voice in both types of organizations. The "Regional Holding Company" would be our ideal agency for implementing policy on a regional basis because it would have the capability to implement as well as plan.

The huge scale of the urban/regional government contemplated might threaten its constituents with a loss in real representation and government responsiveness. Under this proposal, there would be two units of local government; the regional holding company and the individual local service units such as cities, counties and special districts. The local service units would function as precincts of the regional holding company and would be operated by directly elected officials. These jurisdictions would, in turn, have membership in the regional holding company and a vote proportional to the number of their constituents.

The proposal is for a federal system on a micro level. It would divide responsibility for services between the regional and local service unit. Responsibility for those functions such as police and fire protection, planning, regulation and approval of new local service units would rest with the regional holding company, and all other responsibilities would be reserved for the local service units.

Because of natural economies of scale, it could be anticipated that
actual performance of many local service functions would be accomplished by the regional holding company through intergovernmental contracts. Two examples of the trend toward the use of intergovernmental contracts as a means of handling common functions in metropolitan areas are the Lakewood Plan in California and the Cypress Creek Plan in Texas.

Lakewood, California, upon becoming incorporated, contracted with Los Angeles County for the performance of practically all its governmental services. Similarly, a plan discussed in section 2360 was recently adopted in Texas whereby the individual water districts in the Cypress Creek Watershed contracted with the San Jacinto River Authority for the execution of sewage and waste water related functions. Nassau Bay, a suburban Houston community, contracts for police service from the county sheriff's department.

Under existing conditions, councils of government could perform services in addition to those presently being performed. As a suggestion, COGS could take a more active part in arbitrating and mediating between local units of government and special districts which might mutually benefit through cooperation. In a sense, the COGS could serve as regional referee for intergovernmental contracting and for mergers and consolidations.

3230 DEVELOPMENT OF NEW COMMUNITIES

There is a growing national consensus that incentives should be devised to encourage larger, more comprehensive and consequently better ordered development of additions to our urbanized territory. Title VII of the Housing and Urban Development Act of 1970 lists as a finding that:

"...the national welfare requires (financial and other) encouragement
of well-planned, diversified, and economically sound new communities, including major additions to existing communities, as one of several essential elements of a consistent national program for bettering patterns of development renewal.13

Though many of the provisions of the act were based upon findings and recommendations of the 1969 report of the National Committee on Urban Growth Policy, there are two significant differences in these documents. These differences serve to point up the continuing American tradition of belief, not only in functional appropriateness, but in the exhaustion of remedies at the lowest level before seeking intervention by a higher level of government. The differences are:

1. While the committee report proposed that major emphasis for implementation of policy be placed on public corporations, the Congress wrote into Title VII a declaration that the policy of the Department of Housing and Urban Development would be to rely to the maximum extent possible on private enterprise for the accomplishment of the purposes of the act.14

2. While the committee report recommends that "new community programs assisted under this program should not encourage the proliferation of special service districts, and should, to the maximum extent possible, build upon the powers of general purpose state, county and local governments", the legislation is conspicuously devoid of any such pronouncement.15

Several states have experimented with the use of special improvement districts to facilitate larger and more comprehensive development. A recent analysis of alternative approaches indicates that special districts are particularly well suited to overcome the problems encountered by developers in implementing projects of a "new community" scale.16 Described below are three applications of the special improvement district concept to facilitate large scale, privately sponsored urban development.

a) Estero Municipal Improvement District was created by an act of the California legislature in 1960. The project involved 2600 acres of San Francisco Bay Tidelands on which the developer and petitioner for the district had obtained a purchase option. The Estero district was formed to enable the development of Foster City, California, and was authorized to incur a bonded debt of $72,000,000.17
b) Reedy Creek Improvement District in Oceola and Orange Counties, Florida was created to assist the development of Disney World by special act of the state legislature in 1967. The stated purpose is "to undertake improvements in order to promote favorable conditions for the development of a recreation-based community".18

c) A series of water districts for a new community in Texas is the most recently publicized large scale project to be partially financed through the use of special districts. Woodlands, which is a "new community" venture of George Mitchell, a Houston developer, is proposed for Montgomery County. The community, which includes nearly 17,000 acres and has a projected population of 150,000, is to operate as a satellite community, eventually to be annexed by Houston.19 Woodlands is to be developed with a series of water districts identical to the districts used in Texas for subdivision development.

Both Estero and Reedy Creek are single large districts. The powers conferred on the Estero district are broad, but the powers of Reedy Creek Improvement District include all municipal powers except police and protection and are the broadest ever conferred on a special district. Its powers may be exercised within the entire district even if portions overlap municipalities and other political subdivisions. It is exempt from county and municipal zoning laws and building controls, and may exercise eminent domain authority outside as well as inside the confines of the district.20 It is paradoxical that the district was created as a recreational area and Florida presently has no general statute under which a developer's district can be created.21

Developer control of the district in these two single large districts is accomplished by an allocation of voting power based on property ownership within the district. Since the developer will be the major landowner until the development is nearly complete, he can "control" the election of the district board of directors as long as necessary.

The Woodlands example is cited to illustrate the flexibility that can be
achieved through use of the smaller, general law type of district with standard, utility related powers. From the earlier description, it will be recalled that Texas water districts have several distinguishing features which are significant to large scale or "new community" development:

a) Because developer control is maintained only by virtue of the incumbancy of the original board of directors, it must be anticipated that control will shift to the new residents in a short period of time. As the development is projected to span twenty years, a series of small districts are to be formed to accommodate development in two to three year phases. A master district in which control will vest with the developer until after the last phase, will co-ordinate the functioning of the smaller districts through intergovernmental contracts. An effect of this arrangement benefits the new residents in that representation and control comes much quicker than if the developer had to maintain control of the municipal services for twenty years.22

b) Texas water districts are restricted to financing of water, sewer and drainage improvements. This leaves a number of other services such as fire protection, police protection, community recreational facilities, streets, parks, etc. to be financed otherwise. To fill these gaps, Woodlands' developer will use an automatic community association. HUD guaranteed loans will finance improvements made by the community association and these loans will be amortized by the regular ad valorem assessments on the property of the association's members. It is possible to use the homeowners association in this way only because the HUD guarantee removes the necessity for lenders to require a first lien as collateral. In a smaller, subdivision scale development, the nonutility improvements would be financed by the developer and recouped with the sale of subdivided parcels. This feature is important because it provides a common sense safeguard to keep the developer from promoting overly speculative projects.23

Although there are some ways in which the planned use of a series of special districts to develop Woodlands is weaker than the single district plan executed in Foster City, California, or Disney World, Florida, there are compensating advantages which make the plan for Woodlands appropriate to serve as the basis for a model of special district financing. When compared to the single district option, the series of smaller districts has these advantages:

1. Each district becomes democratically representational in a short
period of time relieving the developer of a major source of malcontent among the new citizens.

2. Enfranchisement by property ownership has been challenged on the basis of the "one man one vote" principle established in Avery v. Midland County. Even though the challenge was unsuccessful in that instance, plans to determine voting power on the basis of land ownership are clearly contrary to the Avery principle which is firmly established in the law. Control of water districts in Texas is achieved by popular vote and the system is therefore legally conventional and without fault.

3. Flexibility in financing is enhanced because early districts become economically viable long before the total package would do so. As an example, 30% completion of a project divided into ten districts represents three viable districts and seven that are likely to have issued no bonds. On the other hand, 30% completion of a one district project represents a single non-viable entity.

3240 CONCLUSION

Texas water districts were shown in section 2000 to be an extremely advantageous method of facilitating urban growth. Because they have exercised under only one set of conditions, they have become identified by association with the creation of a discontinuous and unplanned pattern of urban growth. Analysis of water district use in the Woodlands example, and of similar special districts used to promote "new community" development, suggests that special districts may be used to facilitate the development of alternate patterns of growth. The analysis further implies that Texas water districts are the most nearly ideal type of promotional special district because they are most easily adapted as a tool in the context of any urban growth policy that may evolve.
3200 FOOTNOTES


2. Ibid.

3. Ibid.


5. Ibid. page 37.


7. Ibid. IV-1 thru IV-9.

8. Ibid. IV-2.

9. Ibid. IV-3.


11. Ibid. page 13.


15. Ibid. page 173.


21. Laura Gasaway, "New Community Development Districts", pages 41-44.


Summary and Conclusions
The primary financial obstacle in the development of land is the cost of procuring basic water related utility improvements. Investment required in other site improvements is slight by comparison. The only other major item of expense is the cost of land which is less problematic because land provides its own loan collateral.

The current political situation leads to anticipation of no major change in the system of reliance on private entrepreneurship in the development of additions to our urbanized area. Consequently, this study was predicated on the assumption that none would occur and that initial analysis of the alternatives from the developers point of view was appropriate. This analysis led to an immediate identification of several realistic and several unrealistic options with one, the use of promotional special districts, clearly superior to all others. The decision process is approximately represented by figure 4000-1.

The use of water districts in Texas for the development of metropolitan additions has evolved over a period of some twenty-five years and appears to have reached a level of refinement and sophistication greater than that of special districts operating in other areas. Texas water districts have the following characteristics:

1. They have no limit on their ability to tax which makes the "full faith and credit" of the district substantial backing for bond holders.

2. They have no limit on their ability to incur debt and are therefore singularly qualified to finance the installation of systems that meet high standards of planning and engineering.
Criteria

- EQUITY INVESTMENT
- UNDUE COMPLICATIONS
- CONTROL
- MARKETING EFFECT
- LONG TERM EFFECT

Alternatives

- INCORPORATION
- ANNEXATION
- DEVELOPER FINANCED
- PRIVATE UTILITY COMPANY
- SPECIAL DISTRICT

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4000-1
Comparison of Alternatives for Financing Water Utility Improvements

Values represent the approximate ability of each option to satisfy a private developer's criteria.
3. As developer control is limited to the term of office of the original board of directors, water districts are conventionally small in size.

4. Because representation is based on the "one man, one vote" principle, they become democratically representational in a short time.

5. Control passes easily from developer to homeowners and from homeowners to annexing city.

6. District powers are limited to water related functions. This forces the developer to finance the remaining improvements otherwise.

7. They serve as sub-municipal entities before an area is sufficiently developed to warrant or afford the full range of municipal services.

The major areas of difficulty are these:

1. Because of a constitutional requirement that any debt to be repaid through taxation be submitted to the resident electors of the jurisdiction incurring the debt, developers must build several houses and sell them to individuals favorably disposed to vote the regional debt.

2. Because early residents move in at a time when the bonded debt is highest and tax base is lowest, they risk being responsible for more than their "normal" share of the debt if further development fails to occur.

3. The Texas Constitution is not sufficiently broad to permit the district's involvement in fire protection - a necessary and water related function.

4. Deceptive market practices are possible relative to taxes because there is no requirement for the levy of any tax in the early years of development.

5. The early directors have little incentive for frugality in causing district expenditures to be made.

Proposals made to correct these weaknesses consist of two constitutional amendments and various legislative actions. A constitutional amendment is needed to remove the necessity for resident electors voting the issuance of bonds. An amendment is also required to broaden the constitutional grant of power thus enabling water districts to engage in fire fighting activity and to clarify the questionable constitutionality.
of other powers contained in the statutes.

The TWRC should be given a sufficient state appropriation to enable them to properly and aggressively pursue their regulating business. At the same time, the Legislature should require that the Texas Water Rights Commission establish a policy requiring a uniform accounting system, and the levy of a reasonable tax from the first year.

Section 3000 relates the use of promotional special districts to the phenomenon of urban growth. There are indications that urban growth will continue to occur in some form and special districts will therefore continue to have importance as a viable means of facilitating this growth. Beyond this facilitating function, the unique ability of the special district to attract long term capital investment from "municipal bond" investors appears to have a stimulating effect on development.

The Houston metropolitan area, which served as a base for evaluation of Texas water districts, is characterized by a particularly low density, discontinuous pattern of growth. Because much of the growth of Houston was facilitated by the use of water districts, it is frequently assumed that the pattern of growth in Houston has been caused or at least strongly influenced by their use. Contrary to this belief, there are indications that the pattern of regulation over water district use rather than the use of districts per se is significant as a determinant of urban form.

Similarly, the availability of subsurface water has influenced the random pattern of development in the Houston area rather than the use of districts as the vehicle for development of the water utility systems.

One relationship between water district use and a dispersed areal pattern of development appears to be inherent but is indirect. As the proportional
reduction of initial housing cost achieved by district use is greatest for lower cost units, developer interest in less expensive units is encouraged. The search for land reasonably priced for lower cost units is likely to result in the selection of remote and scattered sites.

Most major urban areas in the United States have outgrown the political jurisdictions vested with authority to govern their growth. The vast urban regions which are emerging require innovation in terms of government capable of regional jurisdiction. Because of the functional problems that exist in an agency of regional size, a division of responsibilities between the regional agency and constituent local service units seems appropriate. An example of this kind of relationship is the cooperation between the San Jacinto River Authority (a regional authority) and the individual water districts (local service units) within its jurisdictions.

There is evidence that a national policy is evolving to encourage the development of larger and more comprehensive urban additions. Several developments of this type have been assisted by special districts. These examples show that promotional special districts may be used in a variety of developmental situations indicating that the urban form that they produce is determined primarily by the parameters established for their operation rather than as a direct effect of their use.

4020 CONCLUSION

Policy to direct urban growth can be implemented in several ways. It can be accomplished by strong government interference in what is now the almost exclusive domain of private enterprise, or by structuring incentives or subsidies to influence the decisions of the private developer.
Of the two options to influence private decisions, the incentive certainly represents less cost to society and an action of a lower magnitude than a subsidy. The use of promotional special districts may be considered an incentive to development.

The use of special districts has the advantage of placing the burden of risk on the developers and bond investors who voluntarily sustain the risk for the hope of reasonable compensation. It is an equitable device because it assesses the cost of improvements directly against those benefited.

With no conscious intent to promote any particular pattern of growth, the regulated use of water districts as an incentive to development has contributed to the determination of urban form in Houston. By recognizing special district use and regulation as one determinant of urban form, it becomes possible to consciously influence the urban pattern by adjustment of special district powers and regulations.

Because it is a solution which does not interfere with the existence and territorial integrity of other governments and disturbs their functional integrity only slightly, the special district is politically feasible and commends itself to all vested interests.
4000 FOOTNOTES

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