

## **Municipal Utility Districts The Pros/Cons of a MUD as Your Neighbor**

**Texas City Attorneys Association  
2008 Summer Conference  
June 12, 2008**

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## **Banowsky & Levine, P.C.**

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Banowsky & Levine, PC is an AV rated law firm that has been representing, counseling and defending governmental entities since its inception in 1994. Through the simple mission of providing each of our clients easy access to cutting edge legal counsel, B&L has demonstrated its ability to achieve our clients' objectives in a cost effective manner. Our governmental services cross over the entire spectrum - - from defending against civil rights claims to consulting on zoning and contractual issues.

Scott D. Levine is one of the firm's founding members. Mr. Levine holds an undergraduate degree in business administration from the University of Arizona and a law degree from the University of California, Berkeley. Aside from representing various governmental entities in the north Texas region, Mr. Levine currently serves as councilmember for the City of Parker.



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## Municipal Utility District (MUD)

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MUDs engage in the supply, conservation, irrigation, and drainage of water, fire fighting, solid waste collection, disposal and recycling, wastewater treatment, and recreational facilities.

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## What Can a MUD Do?

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State law gives MUDs the power to establish the authority, rights, and duties necessary to accomplish the specific purposes for which they are created. The powers of MUDs created under general law are determined by the type of district. A "special law" MUD's powers are determined by its enabling legislation. Most MUDs have the power to:

- Incur debt and levy taxes
- Charge fees and set rules for its services
- Enter into contracts
- Obtain easements
- Condemn and annex property

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## Incurring Debt

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Many districts can issue bonds and other forms of debt. The Texas Constitution requires that all debt secured by tax revenues must be approved by district voters. Except for bonds issued by river authorities or bonds sold to a state or federal agency, the TCEQ must approve most district issued bonds.

This provision can be problematic for the cities that may be required to later annex the MUD, as the debt and its terms immediately become the obligations of the annexing city. In some cases, the remaining MUD debt is immediately due and payable by the annexing city.

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## Levying Taxes

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With voter approval, MUDs may levy a maintenance tax and tax increases to cover the costs of operating and maintaining the district's utility.

MUDs may also ask voters to authorize tax bonds. In authorizing these bonds, the voters also approve debt service tax to pay off the bonds as an annual property tax sufficient to cover the district's outstanding debt. This tax is levied on all property in the MUD based on appraised value.

It is possible for the MUD tax rate to far exceed the city's existing property tax rate, costing the resident more for fewer services than those provided for property within the city limits.

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## Charging for Services and Adopting Rules

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MUDs may adopt rules to govern their methods, terms, and conditions of service. These rules also may address water distribution, conservation, and the safety and sanitation of sewer systems.

Persons who violate a MUDs rules can be subject to penalties. Also, a MUD can stop providing its services for non-payment of an authorized charge. MUDs may employ peace officers who can arrest individuals whose actions violate MUD rules on land owned or controlled by the district. These peace officers can also enforce state laws.

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## Entering into Contracts

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A MUD has broad authority to contract for joint construction, financing, ownership, and operation of permitted projects. A MUD may also enter contracts with terms and conditions the board may consider "desirable, fair, and advantageous," for specified purposes. Contracts must be limited to a definite term.

A contract may specify the revenue source, or the combination of revenue sources, from which it is payable. If payments are to be made from taxes other than operations and maintenance taxes, a majority of voters must approve the contract in an election.

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## Obtaining Easements

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MUDs can obtain and use easements to access land owned by another person to install, inspect, repair, and maintain distribution and collection lines.

## Condemning Property

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MUDs have the right of eminent domain, which gives them the power to condemn property inside, and even in certain circumstances outside, the district's boundaries.

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## North Texas Study

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General facts about the districts in the North Texas study area:

- 29 of the districts have a boundary change date listed, which means the district boundary has changed at least once
- Included acres range from 145 acres to 132,300 acres (most are between 200 and 800 acres)
- Bonded amounts range from \$100,000 to \$240,000,000
- Tax rates range from .05 to 1.25 per \$100
- Average bonded amount: \$42.3 million

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## Some Key Players Impacted by MUDs

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- Land Owners and Professionals Initiating the MUD
- Land Developers in the MUD
- Homebuilders in the MUD
- Homebuyers in the MUD
- MUD Entity Itself
- Adjacent Land Owners
- Adjacent Homebuilders
- Home Rule Cities
- General Law Cities
- The County
- The School District

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## Land Owners and Professionals Initiating the MUD

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- **Benefits** – Ability to place public debt and repay themselves from the proceeds with very few restrictions
- **Liabilities** – Can be a high visibility, controversial and time consuming process

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## Land Developers in the MUD

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- **Benefits** – Likely to permit lower land costs, might have better or faster access to infrastructure
- **Liabilities** – Public service responsibilities are less defined

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## Homebuilders in the MUD

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- **Benefits** – Might have lower land costs, might have better or faster access to infrastructure, generally county not city building standards
- **Liabilities** – Public service responsibilities less defined, with fewer public services for the same or greater taxes than paid within city limits

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## Homebuyers in the MUD

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- **Benefits** – Possibly a lower priced home
- **Liabilities** – Less defined public services, possibly higher tax rate, county not city building standards

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## MUD Entity Itself

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- **Benefits** – Achieves all the powers granted by the statutes and is a separate governmental entity
- **Liabilities** – Incurs whatever debt and service area is voted in by the board, levies taxes based on the changing number of voters in the district, retains obligations and burdens of its governmental status until dissolved

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## Adjacent Land Owners

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- **Benefits** – Infrastructure may be more accessible
- **Liabilities** - MUD lowers land development costs, can frequently result in lower land, home and commercial construction values in the immediate market area

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## Adjacent Homebuilders

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- **Benefits** – None identified
- **Liabilities** - MUD lowers land development costs, increases profits to MUD district developers, and may make it difficult of cost prohibitive for nearby homebuilders

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## Neighboring Cities

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- **Benefits** – Might result in good development in the City's ETJ and increase consumer dollars for city commercial and retail
- **Liabilities**
  - Provides incentive and encouragement for "less than market rate" development
  - Receive no property tax unless and until MUD is annexed
  - Have essentially no ability to enforce land use standards
  - Assume the debt of the MUD with annexation
  - Increased burden on City infrastructure

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## The County

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- **Benefits** – Receives property taxes, perhaps sales taxes
- **Liabilities** – Likely to develop with lower home and commercial values than the market would have generated in the long run

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## The School District

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- **Benefits** – Receives property taxes
- **Liabilities**
  - May create growth faster than the ISD has planned, may generate lower home values than the market-based “going rate”
  - May create short term burden on local schools if growth was not anticipated

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## A MUD as a Good Neighbor

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## A Good Neighbor

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- Improves average housing value of the immediate area, bringing in development at or above market
- Accelerates funding for, and brings **new vital resources** of water, wastewater treatment and transportation capacity for its use and others
- Meets or exceeds City's planning standards
- Requires the development agreement to be part of any other required covenants for sales or development in the MUD

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## A Really Good Neighbor

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- Sets an operating and debt repayment schedule at a rate roughly equal to the property tax rate of the City
- Agrees to forgo its annexation and condemnation rights
- Presents a "defined cost" annexation strategy that the City can plan for in its future capital budget
- Merges police & fire at actual cost with the City that is likely to annex the MUD

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## But Even A Good Neighbor Presents These Unknowns . . .

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- Uses public funding for infrastructure, changing the market for other private property
- Ultimately lowers market values of adjacent private developable properties and the resulting tax base values applicable to every jurisdiction
- Accelerates area growth inside and outside of the City's land use plan
- Structures are usually not subject to the City's building permit process
- Can condemn and annex additional property, leaving the door open for a different footprint than that of the original development agreement
- Has the potential to become a separately incorporated city

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## A Bad Neighbor

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- Can force its way into a City's ETJ
- Can defy the comprehensive land use plan of the City
- Has strong financial incentives to ignore the City's zoning ordinances or densities
- Builds product of less value than adjacent properties
- Sets bond levies for residents at far higher than the City's tax rate
- Can negatively influence the property value of surrounding properties, and damage the tax base for all jurisdictions
- Financed with public dollars, which reimburses a developer who is "long gone"
- Leaves a fledgling community with a financial mountain to climb, or worse, MUD bankruptcy

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## How Do You Know if You Want a MUD for a Neighbor?

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- Determining whether a MUD is desirable is specific to each MUD and each city. Considerations including the following key factors, which are not all-inclusive:

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## Regional Economic Issues

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- Area population growth
- Development timing
- Market values of ETJ land
  - The stronger the real estate market and the faster the population growth, the less likely that a MUD is required to achieve optimum development.

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## Public Finance, Planning and Administration Issues

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- The City's ability to provide services to the proposed property in a non-MUD development scenario
- The City's capacity and willingness to provide discretionary police and/or fire protections under an agreement with the MUD
- The anticipated effect of a MUD on the City's long range plans for development in its ETJ
  - The more able a city is to handle the financial obligations of annexation, the less likely the MUD will be a long-term asset.

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## Intangibles

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- The viability of the site
- The experience, skills and financial depth of the proposed MUD's development team
  - The more comfortable the City and the MUD petitioner are with one another's track records, the more likely that a mutually beneficial development agreement can be successfully reached.

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## Key Questions for a City to Consider

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- How might the property develop “but for” the use of a MUD as a financing tool?
- Can the City serve the infrastructure needs of the proposed MUD within the legal timeframe of an annexation obligation?
- Is the City willing to delay annexation of this tract of land for an extended period of time, until development has reduced most if not all of the bonded indebtedness incurred for infrastructure development?
- Can the current owner/developer and the City be successful partners in crafting a development agreement, with the understanding that the provisions of the development agreement between them will survive with the land?
- What are the implications for the city if the MUD is approved and is a financial failure?

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## A Development Agreement Can Address Certain Issues

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- Water Conservation
- Planning Standards and Fees
- Building Codes and Controlling MUD expansion
- Police and Fire Services
- Sewer
- Roadways
- EMS
- Schools
- Parks
- Regulatory Issues
- Annexation

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