

HARRIS COUNTY MUNICIPAL UTILITY DISTRICT NO. 82

**INFORMATION KIT**

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The content contained in this Information Kit is provided by the Harris County Municipal Utility District 82 Board of Directors as a service to our residents. This Information Kit and the information contained within should ***NOT*** be relied upon or used in any manner as an information source when considering whether to buy, sell, or hold any financial instruments issued by the District. Harris County MUD No. 82 files official continuing disclosure statements each year as required by the Securities and Exchange Commission.

**FACT SHEET: DISTRICT OVERVIEW**

**District Mailing Address and Telephone Number**

Harris County Municipal Utility District No. 82  
c/o Allen Boone Humphries Robinson LLP  
3200 Southwest Freeway, Suite 2600  
Houston, Texas 77027  
(713) 860-6400

**Public Information Officer/Media Contact**

Lynne B. Humphries  
Allen Boone Humphries Robinson LLP  
3200 Southwest Freeway, Suite 2600  
Houston, Texas 77027  
(713) 860-6400

**Emergency Contact**

Lynne B. Humphries  
Allen Boone Humphries Robinson LLP  
3200 Southwest Freeway, Suite 2600  
Houston, Texas 77027  
(713) 860-6400

**For Security Emergencies Contact:**

Precinct 4, Harris County Constable  
(281) 376-3472

**For water and sewer emergencies contact:**

TNG Utility Corp.  
2815 Spring Cypress Road, Suite 3  
Spring, Texas 77388  
(281) 350-0895

**Size of District and Annexations**

- Original size of District at creation: 802.528 acres
- Annexations added 1,044.0702 acres
- Current size of District: 1,846.6982
- 2,477 active residential connections as of September 25, 2006
- Projected number of residential connections at completion of development: 5,900.

### **Date of Creation**

May 30, 1973

### **Bond History**

\$125,270,000 in bonds have been authorized by the voters and, as of November 1, 2006, \$33,375,000 have been issued and sold. \$12,513,000 in refunding bonds has been authorized and, as of November 1, 2006, \$800,000 have been issued and sold. For additional information, please see separate section entitled, "How does the District fund its projects?" and separate fact sheet entitled, "District Bond Issuance History."

### **Tax Rate**

The tax rate has declined from a rate of \$.979/\$100 in assessed value in 1998 to \$0.79/\$100 in assessed value for 2006. For additional information, please see separate section entitled, "How does the District fund its projects?"

### **Current Rate Order**

The District's current Rate Order is available by contacting Sharon Covan of Allen Boone Humphries Robinson LLP at (713) 860-6429 or by accessing the District's web site at [www.hcmud82.com](http://www.hcmud82.com)

### **Subdivisions and Developers/Builders**

Subdivisions in the District are: Bradbury Forest, Breckenridge Forest, Forest Point, Tiffany Meadows, North Spring, and Spring Ridge

Builders of homes in the District include Ryland Homes, Supreme Builders, Supreme Builders, Lennar Homes, Centex Homes, D. R. Horton, and Bradbury Development.

### **Notable District Projects and Accomplishments**

The District's internal facilities, owned and operated by Harris County Municipal Utility District No. 82, provide a public water supply and distribution system, sanitary sewage collection system and treatment plant, and storm water collection and transmission, storm water pollution prevention and detention for the subdivisions in the District. For more complete information, please see separate sections entitled "What services does the District provide other than utilities?" and "What emergency plans does the District have?"

FACT SHEET: DISTRICT BOND ISSUANCE HISTORY

District voters have authorized a total of \$125,270,000 of bonds for the purpose of acquiring, constructing, repairing, improving and expanding waterworks, wastewater treatment and storm drainage in the District. Thus far, the following bonds have been issued:

1974 Waterworks and Sewer System Combination Unlimited Tax Bonds - \$1,935,000  
1976 Waterworks and Sewer System Combination Unlimited Tax Bonds - \$ 435,000  
1978 Waterworks and Sewer System Combination Unlimited Tax Bonds - \$1,245,000  
1982 Waterworks and Sewer System Combination Unlimited Tax Bonds - \$1,950,000  
1984 Waterworks and Sewer System Combination Unlimited Tax Bonds - \$3,300,000

The 1974, 1976, 1978, 1982 and 1984 Waterworks and Sewer System Combination Unlimited Tax Bonds are paid in full.

2001 Unlimited Tax Bonds - \$1,580,000  
2002 Unlimited Tax Bonds - \$6,950,000  
2005 Unlimited Tax Bonds - \$4,900,000  
2006 Unlimited Tax Bonds - \$11,080,000

District voters have authorized a total of \$12,513,000 of refunding bonds. Thus far, the following refunding bonds have been issued:

1993 Unlimited Tax Refunding Bonds - \$4,015,000  
1996 Unlimited Tax Refunding Bonds - \$2,065,000

## WHAT IS A MUNICIPAL UTILITY DISTRICT OR MUD?

Municipal utility districts, or "MUDs," are created to bring public water, sewer, drainage and other basic services to residents who are not served by a city. To accomplish the purposes for which they are created, MUDs are authorized by law to purchase, construct, own, operate and maintain all facilities necessary to supply water to, to collect and treat wastewater from, and to collect, store, and drain stormwater from the land within their boundaries. In addition to providing water, sewer and drainage services, MUDs may provide trash collection, fire service and supplemental security patrol services, and may generally enhance communities by building parks and recreational facilities. In connection with providing services, a MUD adopts rules and charges for the services it provides, enters into contracts for goods and services, incurs debt, and levies taxes.

MUDs are authorized by Article XVI, Section 59 of the Texas Constitution and by Chapters 49 and 54 of the Texas Water Code. MUDs (also called "Districts") are political subdivisions of the State of Texas. They can perhaps best be described as the most fundamental form of local government because they provide municipal level services, have elected officials, and are authorized to assess and collect taxes and sell bonds in order to pay off the debt incurred in providing their services. Because it is a political subdivision, the District's meetings and files, including the meeting minutes, are open to the public. Unless it is financially dormant or otherwise exempt, each District also has an annual standardized independent audit. The audit results are filed with the TCEQ and are open to the public.

## HOW AND WHEN WAS THE DISTRICT CREATED?

Harris County Municipal Utility District No. 82 was created by the Texas Water Commission, now known as the Texas Commission on Environmental Quality (the "TCEQ") on May 30, 1973, with the idea that providing water, drainage, sewer and other services to our communities was a job best done by a group of citizens who are residents of the District and who are elected by their neighbors. Operating as a MUD also allows broader latitude to customize services, promote community benefits and respond to opportunities that benefit our customers.

## WHO ARE OUR CUSTOMERS AND WHAT AREA DO WE SERVE?

Harris County Municipal Utility District No. 82 is comprised of approximately 1,847 acres of land located approximately twenty-three miles from downtown Houston, two miles east of I-45 and two miles southeast of Spring, Texas. The District is primarily residential in nature, but has retail and other commercial establishments sufficient to support our residents' needs. As of November 1, 2006, the District includes the following subdivisions: Bradbury Forest, Breckenridge Forest, Forest Point, Tiffany Meadows, North Spring and Spring Ridge.

As of September 1, 2006, the District had 2,477 single family residences, twelve commercial enterprises, four churches and four schools within its boundaries, and the certified valuation for all residential and commercial properties in the District was \$252,034,900 as of January 1, 2006.

A current map is available on the District's web site at [www.hcmud82.com](http://www.hcmud82.com)

#### WHAT UTILITY SERVICES DOES THE DISTRICT PROVIDE FOR ITS RESIDENTS?

Harris County Municipal Utility District No. 82 is within the extraterritorial jurisdiction of the City of Houston. Therefore, its utility systems have been designed and constructed to meet the standards of the City of Houston as well as all applicable state standards.

#### WATER

The District has the capacity to supply 3,000,000 gallons per day of potable water to its residents. The District currently has two water plants and a third under construction. The District also has an emergency water interconnect with Timber Lane Utility District.

The District tests its water supply disinfection levels on a daily basis. Bacteriological tests are performed throughout the distribution system each month. The TCEQ periodically collects and analyzes drinking water samples for chemicals, compounds and a spectrum of contaminants commonly found in ground water. A copy of the most recent report may be obtained from David Wright of TNG Utility Corp. at (281) 350-0895. The District also annually publishes a consolidated water quality report, the Consumer Confidence Report. A copy of the entire TCEQ drinking water report may be obtained from David Wright of TNG Utility Corp. at (281) 350-0895.

Harris County Municipal Utility District No. 82 is within the boundaries of the Harris-Galveston Subsidence District ("Subsidence District") which regulates groundwater withdrawal. The District's authority to pump groundwater is subject to an annual permit issued by the Subsidence District. The Subsidence District has adopted regulations requiring the reduction of groundwater withdrawals through a conversion to alternate source water such as surface water. The Texas legislature created the North Harris County Regional Water Authority (the "Authority") in 1999 to reduce groundwater usage and provide surface water to the northern portion of Harris County. The Authority has developed a ground water reduction plan ("GRP") and obtained Subsidence District approval of its GRP. Harris County Municipal Utility District No. 82 is included within the Authority's GRP.

The Authority has the power to issue debt for the payment of its obligations and has established fees necessary to accomplish its purposes. The Authority currently charges

the District a fee of \$0.84 per 1,000 gallons of groundwater pumped. This rate is effective through September 30, 2007.

#### WASTEWATER/SEWER

The District owns and operates a 1.1 million gallon per day wastewater treatment plant. The District treats and processes approximately 450,000 gallons of wastewater every day.

#### DRAINAGE

The District is located within the Harris County Flood Control District. The District has two detention ponds as of November 1, 2006. The District has one drainage channel - the Breckenridge Forest Drainage Channel and there are three drainage channels within the District maintained by the Harris County Flood Control District.

## WHAT SERVICES DOES THE DISTRICT PROVIDE OTHER THAN UTILITIES?

### LAW ENFORCEMENT

State law allows MUDs to contract with city and county law enforcement to provide security services. Harris County Municipal Utility District No. 82 contracts with Precinct 4 of the Harris County Constable's office for law enforcement services and currently provides three deputy patrols in the District's boundaries. The Harris County Constable's office can be contacted at:

Harris County Constable, Precinct 4  
6831 Cypresswood Drive  
Spring, Texas 77379  
(281) 376-3472

### TRASH COLLECTION

State law authorizes MUDs to provide solid waste collection and removal services. Harris County Municipal Utility District has contracted with Republic Waste Services to provide trash collection services to the MUD's residents. Republic Waste can be contacted at (281) 540-0522.

### FIRE PROTECTION SERVICE

Fire protection service is provided by the Spring Volunteer Fire Department, which operates a station within the boundaries of the District. The Spring Volunteer Fire Department can be reached at (281) 355-1266.

## WHAT EMERGENCY PLANS DOES THE DISTRICT HAVE?

### DROUGHT CONTINGENCY PLAN

The State of Texas requires all MUDs to have a Drought Contingency Plan that sets forth the procedures to be used during drought conditions. The District adopted an Amended Drought Contingency Plan in 2005. A copy of the District's Drought Contingency Plan can be found in the District's public records located at the offices of Allen Boone Humphries Robinson LLP, 3200 Southwest Freeway, Suite 2600, Houston, Texas 77027, or by calling Sharon Covan of Allen Boone Humphries Robinson LLP at (713) 860-6429).

### POWER OUTAGES

In the event of a power failure, the District has generators that are equipped to run 72 hours based on 100% usage.

## VULNERABILITY ASSESSMENT

Pursuant to the Bioterrorism Preparedness and Response Act of 2002, the District performed a Vulnerability Assessment in May of 2004 and prepared an Emergency Response Plan filed with the U.S. Environmental Protection Agency in November of 2004.

### HOW DOES THE DISTRICT FUND ITS PROJECTS?

#### TAXES

The Texas Constitution allows the District, if authorized by its voters, to levy *ad valorem* taxes. Taxes are used to maintain and improve the District's systems and to pay off any bond debt. The District's tax rate is set annually by its Board of Directors after consultation with its independent financial advisor, and the rate is the same for all properties within the District. The District's 2006 tax rate is \$0.79 per \$100 in assessed value. The tax rate is set annually in September or October. For complete and updated information regarding the District's tax rate (current and historical), you may consult the District's monthly meeting minutes, which are available by accessing the District's web site at [www.hcmud82.com](http://www.hcmud82.com)

#### BONDS

The laws creating the District allow it to finance, subject to voter authorization, various acquisition, construction, maintenance and capital improvement projects by issuing and selling bonds. A District may also issue park bonds, fire protection bonds, and road bonds. The District repays the principal and interest on its bonds through *ad valorem* taxes and/or net operating revenues.

In the typical situation, the developer advances the money necessary to design and construct the District's initial water, sewer, and drainage infrastructure. This advance is conditioned on the District's promise to repay the developer a portion of the expense to the extent approved by the Texas Commission on Environmental Quality if and when property value increases to an amount sufficient to allow the District to sell bonds. In addition to selling bonds to repay the developer for the initial design and installation of the infrastructure system, a District may sell bonds (1) to install its own initial system; (2) to repair, upgrade, maintain or enhance existing systems; (3) to refund existing bonds in order to lower debt service costs; and/or (4) to fund fire service, parks and roads.

At an election, voters within the District must authorize the issuance of bonds prior to the District being able to issue bonds. Also, the TCEQ (except for refunding bonds)

must review and approve the projects to be funded with bond proceeds and Texas Attorney General must approve the District's authority to sell the bonds and levy the taxes to repay them. Thus, a District cannot and does not incur debt without both voter approval and proper governmental safeguards. Moreover, no bond funds are paid to a developer until there has been a reimbursement audit by an independent auditor.

Harris County Municipal Utility District No. 82 directors work to balance the need to minimize taxes with the need to provide consistent, quality services. As of September 1, 2006, the voters in MUD 82 have authorized the issuance of \$125,270,000 in bonds and the District has issued \$33,375,000.

WHO MANAGES THE DISTRICT?

MUD 82 is administered by a Board of Directors with five members who all either own property or are residents within the District. The District's Board has financial and operational authority for the District, but retains consultants and contractors who, among other things, operate, maintain, improve and repair the water, sewer and drainage systems and plants, bill and collect for water and sewer services the District provides, and provide the District with financial and legal advice.

Board members are elected for four year staggered terms, with elections held every two years in May of even-numbered years.

The current directors of MUD 82 are:

		<u>Term</u>
Gary Sundstrom	President	5/04 - 5/08
Rick Gable	Vice President	5/04 - 5/08
Don Hays	Secretary	5/04 - 5/08
Matthew Hoffpauir	Assistant Vice President	5/06 - 5/10
Jerry Chesnutt	Assistant Secretary	5/06 - 5/10

## WHO ASSISTS IN THE OPERATION OF THE DISTRICT?

### Auditor

The auditor conducts an independent annual audit that is filed with the TCEQ.

### Bond Counsel

The District retains attorneys to act as bond counsel, who assist in the District's issuance of bonds by providing a legal opinion that the bonds are valid and binding obligations of the District payable from a continuing ad valorem tax. The firm selected by the District is nationally recognized in this area. The bond counsel for the District is Allen Boone Humphries Robinson LLP.

### Bookkeeper

The bookkeeper maintains the general ledger, reconciles bank and other financial statements, invests funds in accordance with the Texas Public Funds Investment Act and with the District's Investment Policy, and prepares monthly activity and budget reports.

### Engineer

The engineer oversees the design, construction and installation of the water, sewer and drainage systems.

### Financial Advisor

The financial advisor advises the District on issuing bonds and on adopting the annual tax rate.

### General Counsel

The District retains attorneys to act as general counsel, advising the Board of Directors on any matters that are presented. The firm selected by the Board is principally engaged in representing municipal utility districts in all aspects of their operations. The general counsel for the District is Allen Boone Humphries Robinson LLP.

### Investment Officer

The Investment Officer oversees the District's investments.

*Tax Assessor/Collector*

The tax assessor/collector for a taxing unit collects the property taxes and accounts to the governing body for the revenues the taxing unit collects.

*Tax Counsel*

When the District issues bonds, it also engages tax counsel to provide a written legal opinion to the effect that interest income on the bonds is tax-exempt to the bondholders, subject to certain conditions, under existing provisions of the federal Internal Revenue Code.

## HOW CAN I CONTACT THE DISTRICT?

The District's Board of Directors meets every fourth Monday at 12:00 p.m. at Allen Boone Humphries Robinson LLP, 3200 Southwest Freeway, Suite 2600, Houston, Texas 77027. Allen Boone Humphries Robinson LLP is located at the corner of the Southwest Freeway (Highway 59) and Buffalo Speedway. Agendas for each meeting are posted at 2308 North Spring in the District and on the District's web site at [www.hcmud82.com](http://www.hcmud82.com) at least 72 hours before every meeting, and the Board of Directors invites all members of the public to attend its meetings.

The District's consultants and contractors may be contacted as follows:

### **For emergencies, contact:**

Lynne B. Humphries  
Allen Boone Humphries Robinson LLP  
3200 Southwest Freeway, Suite 2600  
Houston, Texas 77027  
(713) 860-6400

### **For water and sewer emergencies contact:**

TNG Utility Corp.  
2815 Spring Cypress Road, Suite 3  
Spring, Texas 77388  
(281) 350-0895

### **For security emergencies contact:**

Precinct 4, Harris County Constable  
(281) 376-3472

### **Auditor**

Patsy Waldrop  
BKD, LLP  
2800 Post Oak Blvd, Suite 3200  
Houston, Texas 77056  
(713) 499-4600  
[pwaldrop@bkd.com](mailto:pwaldrop@bkd.com)

### **Bookkeeper**

Linda Canik  
ETI Accounting Services  
P.O. Box 73109  
Houston, Texas 77273  
(281) 444-4866  
[linda@equitaxinc.com](mailto:linda@equitaxinc.com)

**Engineer**

Eric Spencer  
Van De Wiele Engineering, Inc.  
2925 Briar Park, Suite 275  
Houston, Texas 77042  
(713) 782-0042

**Financial Advisor**

Cliff Kavanaugh  
First Southwest Company  
1021 Main Street, Suite 2200  
Houston, Texas 77002  
(713) 651-9850  
[ckavanaugh@firstsw.com](mailto:ckavanaugh@firstsw.com)

**Garbage Services**

Republic Waste Services of Texas, Ltd.  
2010 Wilson Road  
Humble, Texas 77396  
(281) 540-0522

**Operator**

David Wright  
TNG Utility Corp.  
2815 Spring Cypress Rd., #3  
Spring, Texas 77388  
(281) 350-0895

**Tax Assessor/Collector**

Vickey Sullivan  
Equi-Tax, Inc.  
P.O. Box 73109  
Houston, Texas 77273  
[Vickey@equitaxinc.com](mailto:Vickey@equitaxinc.com)

MEMORANDUM:

IMPACT OF MUNICIPAL UTILITY DISTRICTS  
ON THE GREATER HOUSTON AREA <sup>1</sup>

- ▶ There are more than 511 active municipal utility districts in the Greater Houston area
- ▶ The active Houston area Districts cover a total of 550 square miles, including 52,000 acres of commercial property
- ▶ The active Houston area Districts serve 470,000 single family residences, 107,500 apartment units and approximately 1.9 million residents
- ▶ In total, Houston's active Districts contain \$9.2 billion in commercial improvements

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<sup>1</sup> As of November 1, 2006.

MEMORANDUM:  
TEXAS MUNICIPAL UTILITY DISTRICTS:  
AN INFRASTRUCTURE FINANCING SYSTEM

**I. The History of Special Districts**

**A. Overview**

Large population growth requires the development of new communities. Massive capital outlays must be made in order to provide quality water, sewer, drainage, and other municipal services to these new communities. General units of government (e.g., states, counties, and cities) historically have been unwilling or unable to finance these large capital outlays. In Texas, this inability has been due to legal restrictions in the Constitution on municipal debt and taxing authority, combined with the unwillingness of one constituency to incur debt for the benefit of another, especially when risks associated with new development are involved.

Private financing of these capital outlays failed in Texas because the infrastructure costs were recovered through the sale of land, resulting in higher lot prices and unaffordable housing. Attempts at private ownership of the needed facilities led to the construction of substandard systems because the fees required to recover the capital costs were excessive. In addition, because there are no periodic charges associated with drainage facilities, the cost of such facilities could not be recovered through user fees.

States like Texas, Florida, and California that have experienced rapid growth have addressed the shortcomings described above by using special district governments to finance all or part of the required utility and community support facilities. Special districts are local governmental entities that can be endowed with special powers to provide one or more specific services when general purpose governments cannot or will not provide a necessary service to an area. This flexibility makes special districts efficient tools for the stimulation of urban growth and enables them to function in the development of commercial, industrial, and residential properties, and in projects ranging from small subdivisions to large master-planned communities. Among the types of special districts widely used in the United States are hospital, school, water, irrigation, drainage and flood control, urban renewal districts, river authorities, and developmental districts.

**B. Texas Constitutional and Legislative Background**

Texas recognized the need for special districts as early as 1904 when it adopted Article III, Section 52, of the Texas Constitution, authorizing the Texas Legislature to pass laws permitting special districts. After struggling with the limits on indebtedness and other shortcomings in the 1904 amendment, Texas adopted Article XVI, Section 59, of the Texas Constitution in 1917, allowing water districts to operate with unlimited tax

authority and bond indebtedness. Since 1917, the Legislature has authorized numerous types of special districts. Water districts were initially used to develop the state's agricultural lands and later to service small communities. After the use of water districts for urban residential development increased significantly in the 1950s and 1960s, Texas adopted Chapter 54 of the Texas Water Code in 1971 authorizing the creation of Municipal Utility Districts ("MUDs") to streamline the process. In 1995, Chapter 49 was added to standardize the administrative provisions for the numerous types of districts. Today, MUDs are the primary financing tool used by developers in Texas for new development.

### **C. City Involvement**

Texas cities are granted a sphere of influence outside their boundaries known as extraterritorial jurisdiction ("ETJ"). A city must consent to the creation of a MUD within its ETJ or its corporate limits. In its consent, the city may require the MUD to submit all plans for its infrastructure for approval and limit the length of maturity and interest rate of the MUD bonds. The city bears no risk for the development or the MUD, while controlling the quality of the infrastructure. The city has the legal option to annex the MUD, acquire all the assets and assume the debt, subject to certain procedural steps.

### **D. Special Districts in Texas Today**

A majority of the approximately 1100 special districts in Texas today were created over vacant land owned by the developer outside of city limits. Even after significant annexation by cities, over 2 million people populate these special districts, and it is estimated that there is in excess of \$6 billion in outstanding special district bonds. There is significant use of special districts in Austin and rapidly growing use in the Dallas metropolitan area. Most of the special districts in Texas, however, are located in the Houston metropolitan area. It is estimated that the approximately 500 special districts located in the Houston metropolitan area have in excess of \$4.5 billion in outstanding bonds. All of the major community developments in the Houston metropolitan area over the past thirty years have been developed using special districts. Some of these communities and their approximate acreage include The Woodlands (27,000 acres), Clear Lake City/NASA (15,000 acres), First Colony (10,000 acres), Sienna Plantation (10,000 acres), and Cinco Ranch (5,400 acres). The use of special districts has enabled Houston to sustain quality growth while retaining the lowest home prices of any major metropolitan area in the United States. Houston has acquired a major portion of its land and population through annexation.

The development of the city of Sugar Land, Texas provides a compelling example of the benefits of using special districts. Sugar Land was a company town (sugar cane processing) on the Southwest side of Houston until the 1960's. Its population in 1970 was approximately 5,000 people. In the 1970's, the sugar cane fields surrounding the town were sold to developers who utilized special districts to develop the area. After the build-out of these communities was completed, the City of Sugar Land annexed all of the property by dissolving the special districts and assuming their debt. Today, Sugar Land has a

population of approximately 70,000 people, has a low ad valorem tax rate, and is viewed as one of the most prosperous, high-quality communities in Texas.

## II. Municipal Utility Districts

### A. Overview

The objective of a MUD is to provide various services such as water, sewer, and drainage (including detention ponds) to certain areas where municipal services are not available. A MUD also has the ability to construct parks, street lighting, fire prevention facilities, and certain types of roads. The funds used to construct the MUD's facilities are obtained through the public sale of tax-exempt municipal bonds. The MUD provides for the payment of the principal and interest on the bonds through its unlimited power to levy and collect ad valorem taxes on all taxable property in the MUD. The taxes are then paid by homeowners and landowners in the MUD. In addition, homeowners and other users pay monthly water and sewer fees to pay for the costs of operating and maintaining the system.

### B. MUD Benefits

MUDs have been a highly effective and well accepted development tool in Texas because they benefit all of the represented interests: (i) bond investors, (ii) developers, (iii) consumers, and (iv) good public policy. In fact, the only current opposition to the use of MUDs comes from those opposed to the promotion of growth and the creation of affordable housing.

**1. Bond Markets.** The combination of several features has developed investor confidence in, and a ready market for, bonds issued by Texas MUDs. The most important of these features include (i) a MUD's ability to impose an unlimited ad valorem tax rate to support its bonds and (ii) the regulatory requirements imposed on MUD bond issues.

Although there are no constitutional or statutory limits on the amount of bonds that it may issue, a MUD must satisfy strict financial feasibility rules issued by the Texas Commission on Environmental Quality (the "TCEQ"). Before a MUD can issue any debt the TCEQ rules require (i) the completion of all water, sewer, and drainage facilities to be financed with the proposed bond issue, (ii) the completion of all streets and roads that provide access to the areas served by the utility improvements, (iii) the completion of at least 25 percent of the projected value of houses, buildings and/or other improvements shown in the projected tax rate calculations used to support the bond issue, and (iv) a showing that the land values, existing improvements, and projected improvements will be sufficient to support a reasonable tax rate for debt service payments for existing and proposed bond indebtedness while maintaining competitive utility rates. More than just a legalized disclosure of the risks, these standards are designed to protect the consumer against

excessive tax rates and maintain the integrity of MUD bonds, resulting in better interest rates for future MUD projects.

Although the TCEQ limits the amount of bonds it may issue, a MUD is authorized to levy an unlimited annual ad valorem tax against all property in the MUD to pay the interest and principal on the bonds. A MUD's tax lien has first priority over mortgages and assessments, and has the same priority as county, city, and school district taxes. This priority is of great significance when considered in conjunction with the fact that only in extreme situations will a borrower or mortgage lender who has foreclosed forfeit property in order to satisfy taxes due on the property.

All MUD bonds must also be approved by the Attorney General of Texas.

The interest payments made by a MUD to a purchaser of its bonds are generally exempt from federal income taxation.

**2. Developer.** MUD financing of such infrastructure enables the developer to recover infrastructure costs that would otherwise be recovered by raising the selling price of subdivided units. During the first phase of a typical 500 acre development using a MUD, the developer finances the build out of infrastructure for the first 100 acres. After construction of the first phase is complete and the TCEQ feasibility standards are met, the MUD issues bonds to pay for the constructed facilities and reimburses the developer with the bond proceeds. The MUD levies an ad valorem tax on all taxable land, houses and other improvements in the District to support the bond issue. The developer uses the reimbursed funds to build out the second phase of development. This cycle is repeated until the entire development has been built out.

MUD financing of utility improvements enables developer capital to be redeployed more quickly and less expensively than other methods, resulting in a higher quality development over a shorter development period. A MUD's cyclical reimbursement feature also lowers the barrier to entry for developers by reducing the amount of required capital necessary to begin development of new communities, thereby creating a more competitive housing market.

Developers choosing non-MUD financing will be subjected to higher private interest rates and longer reimbursement periods. Thus, if a developer privately finances infrastructure costs, the cost of the subdivided units will be inflated by the pro rata cost of the utility system and extra borrowing costs, resulting in significantly higher lot prices and higher housing costs. Moreover, private financing can slow the rate of development because traditional lenders will not finance a new development phase until the loans for the prior phase have been repaid.

**3. Consumers.** The costs of all MUD utility systems are ultimately paid by the consumer. As was discussed above, the use of MUDs allows the cost of site

improvements to be paid for through public financing, thereby lowering lot costs and reducing the price of homes. The tax-exempt interest rates on the MUD bonds are lower than mortgage rates. In addition, payments of taxes to the MUD are frequently deducted by homeowners on their federal income taxes. Thus, the buyer's payments to the MUD are significantly lower than if the cost of improvements were included in the purchase price. The MUD's periodic water and sewer charges cover the operation and maintenance of the district's utility systems.

Sellers are required to have purchasers of land and houses within the MUD execute a "Notice to Purchaser" informing purchasers of the existence of the MUD, its tax rate and the amount of authorized bonds. MUDs are also required to file that same information in the real property records.

**4. Good Public Policy.** Several good public policy goals are achieved through the use of MUDs, including the development of quality infrastructure, the creation of affordable housing, and the creation of a governmental entity elected by MUD residents to provide for the long term management and financing of a community's infrastructure needs.