



THE WOODLANDS TOWNSHIP

The Woodlands, TX

BUDGET PLANNING INITIATIVE SUMMARY

DATE: August 3, 2015

SUBJECT MATTER: Review of Incorporation Cost and Issues

STRATEGIC PLAN REFERENCE:

- 4.4. Continue to explore changes and enhancements to the current governance structure and clearly quantify and communicate potential impacts

SUMMARY ANALYSIS/CONSIDERATIONS:

In 2007, The Woodlands Township entered into a Regional Participation Agreement with the City of Houston. This RPA agreement allows the Township to continue current operations as a special purpose district without risk of annexation until at least 2057. The Woodlands has the ability to incorporate or adopt an alternate form of local government any time after May, 2014 and for a period of 50 years from the effective date of the agreement (2057).

In 2011, the Township initiated a study to examine all aspects of the Incorporation option. The Township Board retained the services of independent consultants to assist with this effort. The Board then approved a project plan for the consultant and also reviewed and approved the financial assumptions that the consultant would use in the development of The Woodlands Incorporation Financial Model and Results.

Examined Current Structure to Determine Deficiencies or Gaps – The consulting team initiated a number of evaluations. They evaluated how the current system is working and examined its structure to determine deficiencies or gaps. The team conducted extensive focus group meetings with residents, business groups, elected officials, service organizations and other public entities. Based on this focus group process, the consultant determined that, while the Township government was viewed very positively, the following new abilities would be viewed as benefits associated with The Woodlands incorporation.

- Ordinance making ability
- Local control of services/functions
- More consolidated service delivery/MUDs become part of city structure

Development of a Financial Model – EPS, the consultant used to develop the financial modeling, has extensive background in modeling various types of projects for local governments throughout the nation. EPS was charged with developing a financial model to illustrate the ongoing operating and capital costs if the Township changed from its current form

of government to one of incorporation as a municipal entity. To develop this model, EPS used financial data gathered from a number of government entities.

- The Woodlands Township
- Montgomery and Harris Counties
- Texas peer communities (Sugarland, Frisco, McKinney, Round Rock)
- Woodlands MUDs in Harris and Montgomery Counties

In developing this model, the consultants attempted to define the projected service levels associated with incorporation using cost data and service levels provided in the four comparable Texas cities. These comparison communities were selected based on size, location, socioeconomic factors, tax structures and overall reputation for high levels of service, which made them most similar to The Woodlands community.

The consultants found that there are some unique cost differences (and service expectations) between certain services provided by the Township as compared to services provided in the comparable communities.

When comparing simple tax rates, there is sometimes a rush to judgment to assert that all communities provide the same services that can be compared easily through a tax rate comparison. There are certainly some similar cost elements in communities but there are a number of cost elements and procedures that are very different.

Some of these differences involve a higher level of service provided currently by the Township when compared to some of the comparable communities. Specifically in areas such as parks, aquatics, fire service and waste management, the Township's service levels and staffing exceed the services provided in some of the comparable communities.

The following examples are used to detail some of these major cost differences when comparing current operations to other communities:

1. **Law Enforcement** – The current budget cost for contract law enforcement in The Woodlands is considerably less than what is paid in comparable communities. Although the Township contracts for most of the direct patrol services provided within The Woodlands, many additional law enforcement costs such as detectives, special services, training, administration and other policing costs are presently borne by the Counties through their budgets. If incorporated, The Woodlands would incur all police support service costs presently funded by the county as well as debt service for new police and courts facilities, and initial start-up costs associated with the developing, equipping and training a new police department. Even if The Woodlands were able to continue to contract with the County, by law The Woodlands would be responsible for 100% of costs related to services rendered, including those services currently funded through the County tax levy. The proposed department size for a Woodlands Police Department reflected in the incorporation cost report is very comparable to the staffing and costs for other similar cities.

2. **Parks, Pathways and Aquatics** –The costs of operating the parks, pathways and aquatics programs are shown at existing service and cost levels. (As noted in the study, while the Township’s Parks Department performs or coordinates some community maintenance, the parks department is not a public works department.) Some of the comparable cities may have much lower costs for parks services because of reduced service offerings (fewer parks, miles of pathways and pools) or parks maintenance costs that are funded by homeowner associations, as occurs in Sugar Land through the First Colony HOA. First Colony was a master planned community that was annexed to the City of Sugar Land in the 1990’s and continues to provide park maintenance, pathway maintenance, pools, covenant enforcement and other amenities through its Community Association assessment rather than through the city’s property tax levy.
3. **Fire Services** – The current fire department staffing in The Woodlands Township provides for fire and EMS first responder service with eight fire stations and four firefighters assigned to each engine company. Some of the comparable cities have fewer fire stations and choose to assign only three firefighters to an engine company. This higher level of service has been implemented by the Township and is projected to continue if incorporation occurs.
4. **Waste and Recycling** – The Township currently provides garbage and recycling service as part of its basic service and the cost of this service is paid through the tax levy. Most comparable cities provide this service as a separate fee-based service rather than as part of their basic tax supported services.
5. **Debt Service** – Projected debt service costs for The Woodlands to assume roadway reconstruction and provide for other needed city infrastructure will require a substantial bonding commitment and increase existing debt service requirements. Most of the comparable cities have been funding this type of city roadway infrastructure for years and do not have the “built up” demand that will be experienced in The Woodlands should incorporation occur. Montgomery County has not been able to secure the needed level of funding to keep up with road restoration / capacity projects.
6. **RPA Debt and RPA Payments** – Per the terms of the Regional Participation Agreement with the Cities of Houston and Conroe, The Woodlands Township is required to make annual payments to support regional projects. The net impact of the required payments is \$2.4 million annually and these payments are unique to The Woodlands situation. These payments will continue if The Woodlands incorporates. The other cities in this model do not make RPA payments to other entities.

Findings of Financial Model – The compilation of the data model indicated that additional costs and additional revenues associated with incorporation could increase the Township tax rate from 32.5 cents (the Township’s tax rate at the time of the study) to 55.49 cents per \$100 to taxable value. Please keep in mind that these are estimated cost numbers and the numbers are based on additional services The Woodlands would have to assume upon incorporation. These

numbers were developed using four peer cities as examples. These peer cities had the following tax rates at the time of analysis:

- City of Round Rock 42.32 cents per \$100
- City of Frisco 46.19 cents per \$100
- City of McKinney 58.55 cents per \$100
- City of Sugarland 30.00 cents per \$100

This projected increase in the Township tax rate is primarily due to new responsibilities that The Woodlands would be required to assume under incorporation. Incorporation would shift the responsibility for providing a number of basic services from the counties to the new city. Some of the major service costs and responsibilities to shift to the city at the time of Incorporation would include:

- Law enforcement – change from enhanced county services by contract to a municipal police department
- Assume maintenance and roadway replacement responsibility
- Assume public works functions (including water, wastewater and drainage financing and local operations)
- Assume traffic management responsibility
- Municipal court operation and ordinance enforcement
- Planning / zoning
- Private utility oversight and regulation
- Facility costs for police, courts and city maintenance

If incorporated, The Woodlands would have to assume the full cost of the above services. Although these service costs are currently provided by the county government, the Township should not expect its residents to see any significant decrease in the county tax rates if The Woodlands incorporates and assumes these additional service costs.

Some of these new services and statutory regulations are expected to generate new revenue sources upon incorporation (such as court fees, building inspection and franchise fees), however, the net impact is that The Woodlands will likely see a tax increase because newly assumed costs are projected to exceed new revenues.

Changes in MUDs as a Result of Incorporation – The Municipal Utility Districts within The Woodlands Township would be assumed as part of the city’s operations upon incorporation. The study found that the 12 active MUDs in the Township had property tax rates that ranged from 4 cents per \$100 of taxable value to 99 cents at the time of the study (these numbers have changed since the 2012 study.) The average of all MUD property tax rates within the Township was 26.3 cents per \$100.

Based on consolidating all of these MUD operations into an incorporated city operation, the average weighted tax rate impact would have eight MUDs paying more in property taxes while residents in four MUDs would pay less.

As learned from prior work on governance for The Woodlands community, one very sensitive aspect of incorporation would be the dissolution of existing Municipal Utility Districts with the city assuming MUD liabilities and assets. Because The Woodlands was developed over decades, each MUD is in a different state of development (and associated tax levy to property owners). Older Villages of the Township have essentially completed initial development and bond debt has been paid down, resulting in a lower debt obligation for those MUDs translating to a “low” MUD tax property rate. Newer parts of The Woodlands have more recent investment in water, wastewater and drainage facilities, resulting in “higher” MUD tax rates. Upon incorporation, the city would assume all MUD debt responsibility and fund the debt through a uniform tax rate, or user fees applied to all users. This could mean an increase in taxes for many property owners in older portions of The Woodlands (those that have, in their view, already paid for the infrastructure investment), and incorporation could be seen as an inequitable option for certain taxpayers regarding these costs. In contrast, residents in the newer portions of The Woodlands may believe that there is no inequity because they will be contributing to the cost of rehabilitation and repair of older facilities, as is now beginning to be incurred in older sections of the Township. This element of costs that didn’t exist for prior studies, the escalating costs of delivery of water, wastewater and drainage services, will likely result in significant cost escalation in the price of water and wastewater services to users. The mandated move from ground water to surface water is a regional phenomenon in the Houston area and has been accomplished at a lower cost than other regional areas. As a result, the competitive position of Montgomery County has not been adversely impacted but the increased cost of water leaves less flexibility to increase wastewater rates to address rehabilitation and repair costs. How potential additional costs could be added to either taxes or water and sewer bills to cover these costs would have to be considered.

Mobility and Road Maintenance – One area of significant future cost in the Township surrounds the growing resident issue of mobility. Who makes improvements, and when, will impact a city tax rate either favorably or negatively.

If Montgomery and Harris County make needed investments in road infrastructure to enhance mobility in the Township prior to incorporation, the city would be relieved from having to make those same expenditures, which would favorably impact the tax rate. While the cost of construction or redevelopment of roads and infrastructure in the Township is known to be a large cost, removing some of that cost by delaying incorporation could advantage city taxpayers. However, if needed mobility improvements were delayed until incorporation, all or a greater portion of the costs of making those mobility improvements would shift to the city and would likely increase the tax rate for Township property owners.

Earlier this year, a Montgomery County road bond referendum to repair and build county roads to resolve mobility issues failed. While the county has stated it plans to hold a future bond referendum, the timing and proposed projects are unknown.

Depending on the timing of issuance of road contracts for road repair/enhancement, an inflation factor has also become a real issue. The cost of road improvements (especially new projects) has grown significantly over the past couple of years. It is unknown if this trend will continue or if costs will moderate; however, these costs will impact the city tax rate in maintaining the road infrastructure.

Community Findings Regarding Incorporation – In 2012, the results of feedback from residents, businesses, elected officials and others provided the following advice to The Woodlands Township Board of Directors:

- 11% Don't rush to a decision (on incorporation); take time to thoroughly consider options
- 16% Defer an incorporation election
- 36% Do not incorporate; continue as the Township
- 19% Continue to analyze and research options; improve the Township (through ordinance-making authority, improved law enforcement, etc.)
- 6% Incorporate; hold an election
- 12% I don't know; I need more information; continue to listen to community

Continue to Analyze and Research Options

While the Township reviews an annual governance assessment report each year, it has been three years since the completion of the last financial analysis. As the Township approaches residential build-out and growth in the area progresses, the Board may desire to revisit governance issues and the related review of costs related to incorporation. While previous studies have addressed costs associated with incorporation, the growth of the Township, recent community indicators and relationships with current service providers would need to be revisited because of the ever changing fiscal and political environment that impacts the Township.

Major decisions would have to be made regarding contracting out of services, versus developing the capability to provide the services directly by the city. Whether a decision is made to develop an in-house city capability to provide a service, or contract with a third party to deliver that service, timing of necessary actions becomes extremely important. In order to accomplish the necessary actions in a timely manner, third party consulting advice would likely be necessary to ensure all issues are addressed and nothing falls through the cracks in start up and delivery of services by the city. Until substantial discussions are held with existing service providers, it shouldn't be assumed that any existing way of delivering services to the community could be contracted, and as importantly, if contracted... at what cost?

Decisions regarding amounts and issuance of municipal bonds must be addressed with a strategy developed to accomplish the objective of timely funding as required to provide city services.

Ultimately, some decisions could be driven by Texas law and an appropriate strategy would have to be developed to address funding of those city services.

The final financial model from the 2012 study and the final July 2012 Governance Strategy and Assessment Report are attached for reference.

If the Board is interested in pursuing an updated financial analysis, the Board should establish the assumptions to be used in the study or affirm the initial assumptions from the 2012 study.

Preparation for Future Governance Needs

The 2012 study noted several facilities that would be needed by the Township once incorporated, including court, public safety and public works facilities. In an effort to accommodate future needs, the Board approved the purchase of an 11.6 acre tract of land in the Town Center area (see separate budget initiative).

In the planning process for the 2015 budget, the Township Board discussed establishment of an incorporation reserve as a budget initiative, but no action was taken to implement such a fund.