

GOVERNMENT & REGULATIONS

DEVELOPERS PLAN TO PUSH BACK AGAINST REGULATION

A NEW LAW PASSED BY THE TEXAS LEGISLATURE MAY CHANGE DEVELOPMENT IN THE ETJ

By Ramzi Abou Ghalioum and Justin Sayers – San Antonio Business Journal
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In 2021, Meritage Homes (NYSE: MTH), a homebuilder out of Scottsdale, Arizona, filed a lawsuit against the city of Cibolo when it couldn't get the paperwork it needed pushed through City Council to begin work on a project into which it had invested millions of dollars.

The denial, the council claimed, was rooted in the fact that Meritage had violated the city's development code by not adequately planning how it would deal with the wastewater produced at its planned Legacy Trails subdivision.

Meritage, on the other hand, disagreed. In its lawsuit, it argued that it had made the necessary arrangements to have its homes be on septic tanks until such a time as they could be connected to a main sewer line.

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In March 2022, another lawsuit was filed against the city of Cibolo under the same auspices by Miami-based homebuilder Lennar (NYSE: LEN). It claimed that Green Valley Special Utility District, the wastewater utility provider in the area, had committed to a December 2022 deadline for completing extensions to its sewage infrastructure, but that obtaining preliminary plats was necessary to keep development of a project it was calling Cibolo Farms moving at a pace that would not compromise the project's economic viability.

City Council once again voted to deny the plat, despite the city’s planning and zoning department recommending approval. In its filing, Lennar notes that the Texas Local Government Code “provides that the municipal authority responsible for approving plats ‘must approve’ a plat that satisfies all applicable technical requirements.” Essentially, it contended that the denial of the plat application was without merit.



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The city of Cibolo, due east of San Antonio, was involved in lawsuits with two different homebuilders over plat applications.

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Art Anderson, the attorney with Dallas-based Winstead PC who is representing both builders in the Cibolo lawsuits, denied a request for comment “due to client conflicts.” The lawsuits, however, are proof of the friction burns felt between cities and developers within the unincorporated areas of the Texas hinterlands known as the extraterritorial jurisdiction, or ETJ.

In fact the University of Texas published a paper authored by Anderson in 2021 detailing how the Legislature and the courts in Texas have spent half a century fine-tuning regulation in the ETJ.

But even now, the issue is far from airtight.

Governance in the ETJ was once again a focal point of this year's legislative session. In May, Gov. Greg Abbott signed Senate Bill 2038 into law, which will allow landowners in the ETJ to petition for release from oversight by the municipality to which that ETJ belongs beginning in September. Instead, those property owners would now be regulated by the county.

Cities abusing the power they wielded over properties in their ETJ was the impetus for the bill, said its author, State Senator Paul Bettencourt, a Houston Republican.

"Residents would have to follow the rules and regulations of that municipality without the ability to vote on the rules, regulations or elected officials making them," he said.

Approval for removal from the ETJ is subject to a vote during that year's general election, although cities can expedite the process by simply agreeing to the request for removal from the ETJ.

San Antonio developer Blake Yantis, co-founder of Mosaic Land Development — the same developer which sold the Legacy Trails subdivision to Meritage — said that coming to a consensus over design with the municipality whose ETJ he's developing in is the more favorable approach. In reality, he said that doesn't always pan out.

"We've got a project in Williamson County where we have plans to de-annex," Yantis said. "We had some limits tied into [that city's] ETJ. It's really just sort of a disagreement as to what the city thinks they can do versus what we think is clear they can't do."



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Blake Yantis, partner at Mosaic Land Development, said he plans to use SB 2038 to remove one of his properties from the ETJ of a city in Williamson County.

MOSAIC LAND DEVELOPMENT

He didn't want to name the specific municipality from whose ETJ they were considering leaving for fear of reprisal.

"Whether it's through access to utilities or processing plats, there are any number of things these cities will impose to slow down a development," Yantis explained.

SB 2038 is a step in the right direction for developers, giving them a tool to fight back against municipalities putting up barriers to development, he said.

"Rather than spending time and effort getting them to understand, we can just remove ourselves from the ETJ."

For Austin-based MileStone Community Builders, the passing of SB 2038 was a watershed moment in a years-long debate over a 775-acre tract of land between San Antonio and Austin.

A house of cards

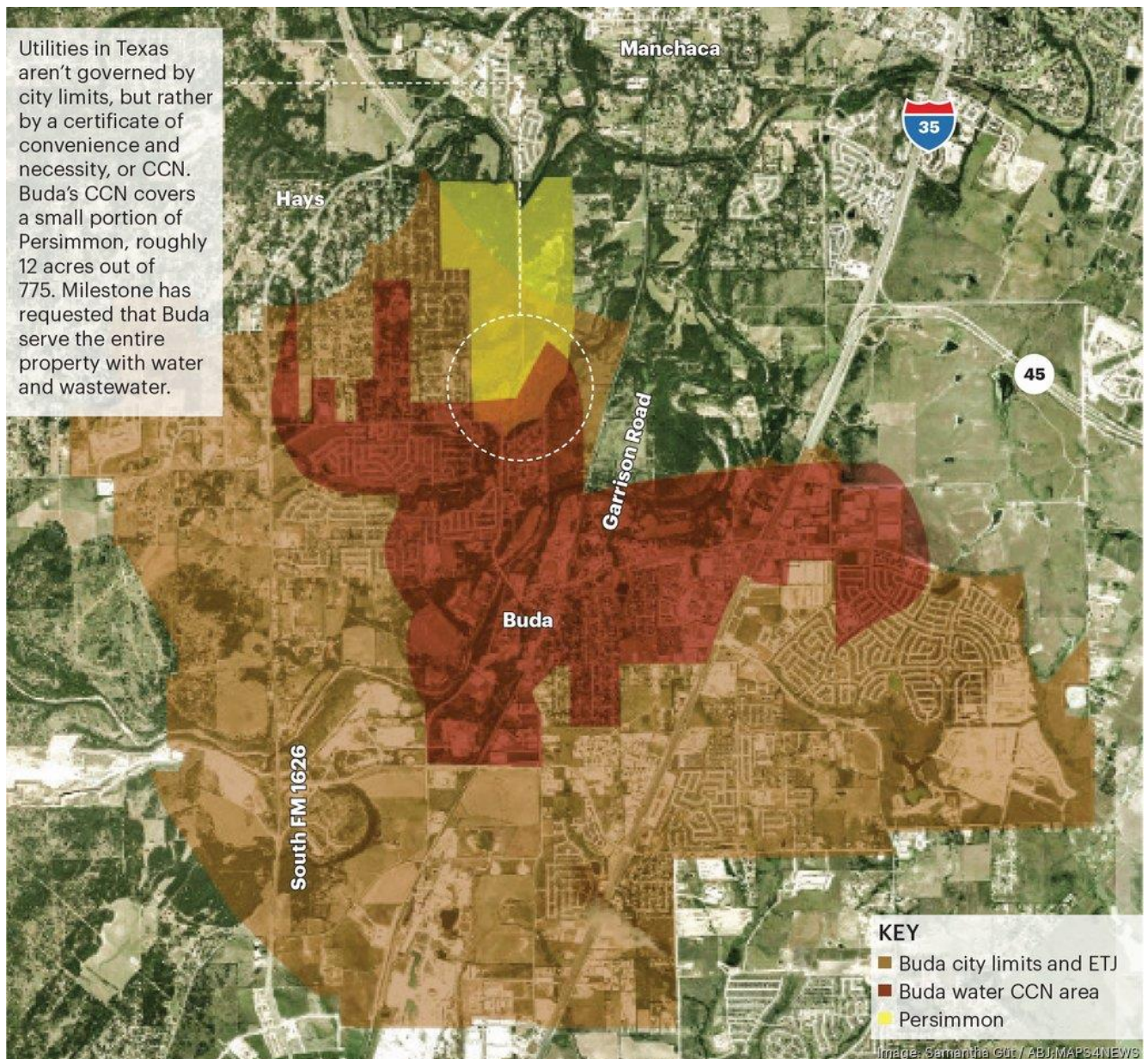
Since 2018, the developer has been trying to turn a sprawling tract of land in the extraterritorial jurisdiction near Buda into a subdivision with thousands of homes. It attempted to strike a deal with the city which included access to water and sewer services. The deal was necessary because although utilities in Texas aren't governed by a city's limits, but rather by a certificate of convenience and necessity or CCN, the development — called Persimmon — is both outside Buda's city limits as well as most of its CCN, which means the city is not legally obligated to provide it with water.

In exchange for utilities, city officials sought concessions from the developer to quell neighbors' concerns and "create a project that preserves the best interests of Buda." Those concessions included commitments from MileStone that 30% of the residential lots at Persimmon be 60 feet wide and another 30% be 80 feet wide, which would dramatically slash the number of lots it intended to develop, rendering the project not economically viable.

The problem highlights the reason for bills like SB 2038.

"I think for a long time, municipalities have taken for granted their ability to pretty much do whatever they want from a regulatory perspective," said

Garrett Martin, MileStone president and CEO. "I think really that the pendulum has swung too far in the direction of those municipalities."



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Proposed Persimmon neighborhood crosses ETJs for Buda, Austin

The bill, which Martin called a "game-changer for how projects get developed," gives landowners more control over what they can and can't do. It's a handy tool for developers to have in their back pocket, especially within the emerging metroplex of San Antonio and Austin. As the inner core of those cities become increasingly landlocked, more developers are venturing out into

the ETJ. An overwhelming number of applications for new residential subdivisions in San Antonio are in the city's ETJ.



Garrett Martin, president and CEO of Austin-based MileStone Community Builders, called SB 2038 "a game-changer for how projects get developed."
ARNOLD WELLS

"Our approach to development is one focused on collaboration with all the stakeholders and by virtue of that, we spent a lot of effort, energy and resources investing in building consensus around our projects," Martin said. "But when one party becomes entrenched in their position and you can't get past that, or one party is not doing their job and not reviewing the project as they should, or something along those lines, then you need the ability to continue to use your land, develop your land."

A light touch

On the other side of the argument, many cities with developments in the ETJ believe they will one day voluntarily annex themselves into that city, and development agreements like the one tied to Persimmon will allow the development to be more harmonious with that city's land use regulations.

Because cities have limited control over their fringes — for instance, they cannot enforce zoning codes — they believe it makes sense to try and be consistent.

"You can have development that is disjointed from the city. Because counties don't have zoning regulations, you can have undesirable uses right next to a residential area," said Buda City Manager Micah Grau. "It really strips away a city's ability to zone and control the built environment of what happens around a community."

With regards to Persimmon, Grau said Buda is "most-prepared and best-suited" to provide utilities to the development, but acknowledged the possibility of MileStone — and potentially other developers — taking advantage of SB 2038.

"I imagine we're going to see similar requests over the next few months and years related to this," he said.

Patchwork cities

City of Taylor assistant city manager Tom Yantis said he was concerned that SB 2038 would create "patch-work quilt areas" around cities.

"For any city, I think the most difficult issue that this is going to arise is how to plan for the future extension of public infrastructure into the ETJ because we don't know whether the area is going to be in the ETJ or not," Yantis said.

"When you're trying to plan for growth of a city, you need to understand how you're going to serve the area that you grow into with streets and water and sewer and drainage projects. If you don't know whether that area is going to be part of the future city boundary, it's hard to plan for how you are going to grow."

He thinks cities might now focus more on providing services to the areas they already have.

"There will be less long-range planning for areas in the ETJ, which will maybe refocus some of the resources to just the areas that are already in the city limits. That could help maybe with not getting cities stretched too thinly from a financial standpoint on infrastructure extensions in the ETJ. I can see that as a potential advantage where it just kind-of refocuses your attention to the area in the city limits," Yantis said.



Tom Yantis is assistant city manager for the city of Taylor, outside Austin.

CITY OF TAYLOR

But Chris Johns, an Austin-based land use attorney at Johns & Counsel PLLC said there have already been signs that the bill has done its job.

“The market has started to change because developers saw there was a path out of the city of Taylor,” he said. “If you look at what happened before this legislation, the market had totally frozen up. Now everybody sees that there is a potential path forward here – that things have started to sell and things are starting to go under contract.”

The elephant in the room

In Persimmon’s case, leaving the negotiating table with the city of Buda means it has to get utilities elsewhere — and that isn’t always an easy problem to fix.

“Generally, you’re looking at 4.2 to 5 lots per acre in a very customary development, maybe at 3 to 3.5 per acre, so if you tell me I need 80-foot lots, I’ve lost 30-40% of my revenue,” said Tom Staub, founder of master-planned

developer Red Oak Development, which is based in Austin. “But you still need to get your water and sewer from somewhere.”

He explained that in the ETJ, setting up municipal utility districts, or MUDs, is one of the only means to feasibly get those utilities while still allowing a project to pencil. Established in 1971, MUDs allowed large-scale development to occur in the ETJ despite a lack of infrastructure, at the developer’s cost. Residents in a MUD are subject to property taxes levied to help finance the infrastructure and facilities put in place.

While they’re a viable solution for sourcing that infrastructure, however, there are significant obstacles to setting up a MUD. They require approval from the Texas legislature, or special dispensation from the Texas Commission on Environmental Quality, and they also require the endorsement of the municipality in whose ETJ or city limits they reside.

Outside of the regulatory hurdles, they can also add an immense upfront capital cost to a project.

“When the average sewer plan is going to cost you somewhere in the range of \$8 million and \$20 million, and a water tower will cost you \$8 million and \$15 million, there’s still economic hurdles you have to overcome,” Staub said.

He explained that’s why annexing into a city can be desirable for a development. While there are still fees associated with connecting to a city’s utilities, those can be better-managed than resorting to a MUD.

Grau, the Buda city manager, said they have demonstrated the ability to work with landowners on MUDs in the past. But still some issues remain.

"MUDs provide a funding source for creating infrastructure but it doesn’t create water," he said. "So, you have to still have to have an adequate water supply for a development to occur."

MileStone’s Martin said water challenges depend on the tract of land. Some parcels are in areas with companies who have exclusive rights to provide utilities, making it easier to figure out who to contract with. The ones that aren’t will likely need to turn to other alternatives, whether it’s municipal utility districts, temporary fixes like package plants or pumping groundwater.

Residential Builders

2021 local sales volume

Rank	Prior Rank	Business name
1	1	Chesmar Homes
2	2	David Weekley Homes
3	3	Monticello Homes

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