

Publications

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Texas HB 21 Reshapes the Requirements and Effects of Chapter 394 of the Texas Local Government Code

Texas House Bill 21 (HB 21), signed into law in May, has dramatically shifted affordable housing tax exemptions across the state. Specifically, HB 21's primary impact is on a housing finance corporation's area of operation and the applicable ad valorem tax exemption.

Below is a summary of the key changes that HB 21 makes to Chapter 394.

Area of Operation

A housing finance corporation (HFC) may own or engage in real property for residential development **only in** the following areas:

1. for an HFC sponsored by a municipality, the area of operation is limited to the boundaries of the municipality;
2. for an HFC sponsored by a county, the area of operation is limited to the boundaries of the sponsoring county; and
3. for an HFC sponsored by more than one local government, the HFC can operate within both the boundaries of the sponsoring municipality and the boundaries of the sponsoring county.

However, an HFC can operate outside of the areas defined above **only if** a resolution or order approving the activity is adopted by the governing bodies (municipality or county) of that particular outside area.

Additionally, HB 21 now permits HFC's to issue bonds to finance or support a residential development or a home that is located or will be constructed within the confines of the areas described above. This includes area(s) not described above so long as the issuance of the bonds is approved in the resolution or order of the governing municipality or county. The bonds will require the development to either: (i) have 50% of the units be reserved for occupancy by individuals earning less than 80% of the area's median family income; or (ii) meet the Occupancy Test (defined below).

Related People

- Nicholas L. Burkhart
- Ben Cleveland

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- Tax Credit Finance
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Ad Valorem Tax Exemption

For an HFC to qualify for an ad valorem tax exemption, multiple tests must be met:

1. **Occupancy Test** – either:
 1. 10% of units are reserved as **lower** income housing units with 40% of total units reserved for occupancy as **moderate** income housing units; or
 2. 10% of units are reserved as **very** low income housing units with 40% of total units reserved for occupancy as **middle** income housing units.
2. **Fifty Percent Test** – rent reduction at the development in the preceding tax year was (to be calculated starting in the first tax year after acquisition or first year of development):
 1. not less than 50% of the estimated ad valorem taxes that would have been imposed in the same preceding tax year if the property did not receive an exemption; or
 2. less than 50% of the amount of the estimated ad valorem taxes described in (a) beginning with the tax year specified above, but the project owner paid to each taxing unit for the applicable tax year an amount equal to that taxing unit's pro rata share of the rent reduction shortfall that exists based on the difference between the minimum rent reduction amount described by (a) and the amount of actual rent reduction at the development in the preceding tax year.
3. **Uniformity Test** – all units in the development, regardless of rent restriction, must have the same finishes, equipment and access to community amenities and programs.
4. **Percentage Test** – the percentage of very low, lower, moderate and middle income housing units reserved in a building must be the same as the percentage of each category of income-restricted residential units reserved in the development as a whole.
5. **Rent Test** – monthly rent charged per unit does not exceed:
 1. Very Low Income Housing Unit: 30% of 50% of the area's median income.
 2. Lower Income Housing Unit: 30% of 60% of the area's median income.
 3. Moderate Income Housing Unit: 30% of 80% of the area's median income.
 4. Middle Income Housing Unit: 30% of 100% of the area's median income.
6. **Disallowed Covenants Test** – HFC user and development **cannot**:
 1. refuse rental to an individual or family because they participate in the housing choice voucher program; or
 2. use a financial or minimum income standard that requires the renter to have a monthly income of more than 250% of the individual's or family's share of the total monthly rent payable for the unit.
7. **Requirements Disclosure Test** – project owner must publish on the development's website information about the development's policies regarding tenant participation in the housing choice voucher program.
8. **Marketing Test** – project owner must market units directly to participants in the housing choice voucher program and notify local housing authorities of the development's acceptance of tenants in the housing choice voucher program.
9. **Lease Agreement Test** – any lease agreement for an income-restricted residential unit must provide that:
 1. the landlord may not retaliate against the tenant or tenant guests because of participation in a tenant organization;
 2. the landlord may only choose to not renew the lease if landlord serves a written notice of proposed nonrenewal on the tenant not later than the 30th day before the effective date of nonrenewal and if the tenant:
 1. committed one or more substantial violations of the lease;
 2. failed to provide required information on the income, composition or

- eligibility of the tenant's household; or
3. committed repeated minor violations of the lease.

New Audit Requirements

An HFC or project owner that claims an ad valorem tax exemption for a multifamily residential development under Chapter 394 must annually submit (starting on June 1 of the subsequent date of completion or acquisition and each June 1 thereafter) to the department a compliance audit report that states: (i) whether the compliance with Chapter 394 has been maintained; and (ii) the difference in the rent charged for income-restricted units and the estimated maximum market rents that could be charged for those same units. The auditing department must conclude its audit within 60 days of receipt of the audit report and will publish a report summarizing its audit findings. Additionally, the auditing department will notify the submitter, within 120 days of receipt of the audit, any findings of noncompliance with such notice detailing the specifics of each noncompliance. Should the noncompliance not be remedied within 180 days of the initial submitter's receipt of the notice of noncompliance, the ad valorem tax exemption will be revoked.

Polsinelli's Tax Credit Finance Group continues to monitor the impact that HB 21 will have on Chapter 394. With extensive experience assisting developers with regulations surrounding Chapter 394, we are ready to assist with navigating the changes HB 21 imposes.