STRATEGIC ECONOMICS

MEMORANDUM

To: City of Las Cruces

From: Dena Belzer and Daniel Hernandez

Date: September 7, 2020

Subject: Royal Crossing TIDD Peer Review

Project Background

The former Las Cruces County Club (located generally at Main Street and N. Solano Drive) closed in 2011 after a prolonged financial decline. This site represents an important infill development opportunity for Las Cruces as expressed in multiple City policy documents, including the 2018 Apodaca Blueprint. In 2018, developers also began discussing the possibility of creating a Tax Increment Development District (TIDD) for a 91.27-acre area that would include a hospital and medical office building already under construction, as well as a mix of commercial and residential products that would create a new urban district in the City's inner core.

Following procedures mandated by the state of New Mexico's enabling legislation, City staff held a work session with the City Council to discuss the TIDD in September 2019. TIDD Guidelines were adopted in December 2019, and in January 2020 the developer filed a formal application to form the Royal Crossings TIDD with the goal of having an adopted formation resolution from the City Council in time to make a formal submission to the New Mexico Department of Tax and Revenue by September 1, 2020. Assuming the State approvals the District, this timeline would enable the TIDD to start collecting incremental tax revenues as of January 1, 2021. This timing is important because it would enable the district to set its base tax revenue year in 2019, allowing the first year that increment would be calculated to be 2020, when the hospital and medical office building will likely be completed. In other words, gross receipts and property tax revenues generated by these two new buildings would provide the initial revenue stream for the district. If the district were to be adopted in 2021, the tax revenues from these two buildings would become part of the base taxation levels and any incremental increases in gross receipts or property tax revenues above 2019 could not be captured by the district.

As part of the formal TIDD application, the developer was required to submit numerous technical documents, including, but not limited to, tax revenue projections tied to development phasing for a 25-year period and itemized public improvement costs the TIDD would cover. These revenue and cost assumptions were key inputs the legal documents necessary for the TIDD formation which include a financing plan, an operations and maintenance agreement, and a development agreement. The City and County jointly retained a financial advisor to review the developer's financing plan and determine if the projected revenues would be sufficient to cover the proposed costs the District would incur. The City also retained legal counsel to assist with preparing the development agreement and other necessary documents. The TIDD formation process is complex and this is the first developer-initiated TIDD for both the City of Las Cruces and for Dona Ana County, which has also been asked to contribute to the District a portion of its incremental tax increases from future development in the area. Therefore, the process of reviewing documents and engaging in negotiations with the developer has required staff to swiftly move up a steep learning curve.

It is also important to note that before any further development is built within the district, the developer would be required to have an approved planned unit development (PUD) plan for the entire site. The PUD would most likely represent a refinement of the site plan included in the Apodaca Blueprint with further modifications based on additional community input and any new proposals from the developer regarding the land use mix, site design, and potential development phasing.

In June 2020, City staff asked the City Council to consider adopting a TIDD Intent to Form Resolution as per the procedure specified in the State's TIDD enabling legislation. The next steps in the approvals process were to approve a formation resolution by late July 2020 and adopt an ordinance to dedicate the tax increments to the district in early August 2020. This timing was well within the September 1, 2020 deadline for submitting the proposed district to the state. However, at the June meeting, the City Council directed staff to make some changes to the allowable infrastructure costs and to respond to multiple questions and concerns raised by both the Council and community members. This required bringing the resolution of intent to form the TIDD back to the City Council on July 6th.

Based on further input from Council at the July 6th meeting, staff continued to negotiate changes in the District's details with the developer. At the same time, staff retained outside consultants, Proyecto LLC and Strategic Economics, to provide a peer review of the many TIDD related documents, review the questions being posed by Council and the community, and provide options for further adjusting the District's structure in response to this review. Proyecto LLC is a real estate advisory firm specializing in advising public agencies regarding development projects and in developing affordable housing. Mr. Daniel Hernandez leads the firm. Strategic Economics is an urban economics firm specializing in real estate and public finance related advisory services to public agencies. Among other specialties, Strategic Economics, led by Ms. Dena Belzer, has considerable experience with tax increment financing districts in many states around the country. Both firms are based in California but work nationally and are currently working together with the City of Santa Fe to redevelop the former Santa Fe College of Art and Design campus now owned by the City.

This memo presents the key findings from this peer review, as well as some possible lessons learned for any future efforts to form a developer-initiated TIDD in Las Cruces. These lessons reflect potential steps the City Council could have taken to address various concerns with the TIDD raised by both Council members and the community. Ms. Belzer and Mr. Hernandez were prepared to share this information with the City Council at their hearing regarding the Royal Crossing TIDD on August 11, 2020, but the developer withdrew their proposal to establish the district earlier that day, so the hearing was canceled. These findings are organized by the following topic areas:

- National Context for New Mexico's Tax Increment for Development Act
- Proposed TIDD costs
- TIDD annual revenue generation and development phasing assumptions
- The proposed district governance structure
- Potential lessons learned for Las Cruces

National Context for New Mexico's Tax Increment for Development Act

In every state, municipal or county taxes can only be levied based on authorization from the state legislature by what is called enabling legislation. New Mexico's state enabling legislation that establishes the policy objectives and specific mechanics for establishing tax increment development districts is the Tax Increment for Development Act (2006 as amended through 2019)[1]. Virtually every state in the U.S. had adopted some form of tax increment financing, except for Arizona.[2] While the specific mechanics for implementing these districts vary widely across states, there are some significant differences between New Mexico and other states regarding the legislative purpose for these districts.

Tax increment districts are primarily used to finance local infrastructure improvements and other public facilities that leverage private investment in development projects including new buildings or major building renovations. In the majority of states, the legislative rationale, or intended community benefit for enabling the public investments is to eliminate physical and visual blight caused by disinvestment in existing buildings within specified neighborhoods or districts. The longer-term public benefit is to increase property and/or sales tax revenues as well as create a funding stream to pay for necessary but expensive upgrades to aging or otherwise inadequate infrastructure systems. An economic development benefit, i.e., job creation may also be part of the legislative intent, but the job creation benefit is often based on new investments in the buildings that will house the new jobs. A few states use tax increment to fund affordable housing and a few other states require residential projects that are directly benefiting from tax increment financing to provide a certain number of affordable housing units within the project. benefiting from the district.[3]

State enabling legislation for tax increment districts typically evoke a "but for" rationale for tax increment financing districts, meaning that "but for" the tax increment financed investments in infrastructure or other allowable public improvements, the private investors would not invest their money in in this targeted location. However, because the "but for" argument can be hard to prove or measure, states do not require that local jurisdictions meet a specific "but for" performance standard as part of the district formation process. However, most states do require some form of "blight" finding as a proxy for the "but for" argument and to bolster the argument that targeting public investment to leverage private development is in the public's long-term interest.

Most states use incremental increases in either property or sales tax revenue to fund their tax increment districts. Therefore, to test the revenue generating potential for any given district requires projecting how much future development/property investment will occur and then projecting the real estate activity that will yield the incremental increases in tax revenues.

---

[1] https://casetext.com/statute/new-mexico-statutes-1978/chapter-5-municipalities-and-counties/article-15-tax-increment-for-development/section-5-15-2-findings-and-purpose

[2] https://www.nahb.org/-/media/NAHB/advocacy/docs/industry-issues/land-use-101/infrastructure/tax-increment-finance-by-state-report.pdf

[3] https://nhc.org/policy-guide/tax-increment-financing-the-basics/how-tifs-can-be-used-for-affordable-housing/

Because future real estate activity is a direct reflection of the real estate market and financial feasibility, district revenue projections are driven by market demand. In other words, for the tax increment district to work, it must have enough underlying market demand to support the projected future development. As result, some locations, such as downtowns or large shopping center sites, where demand is well understood and the public improvements funded by a tax increment district are only necessary to accelerate underlying market forces, are well-suited to tax increment districts. But districts with less development opportunity and lower overall market value tend to be poor candidates for tax increment financing.

New Mexico's TIDD enabling legislation is somewhat different than the national norm in several ways. First, the statue is "...for the purpose of supporting economic development and job creation."[4] As was discussed above, this primary focus on economic development, rather than on community development, is highly unusual.

Second, New Mexico's gross receipts tax (GRT) is arguably the most comprehensive tax of its kind in the country.[5] This makes the process of measuring the specific GRT tax revenues generated by any given development project or TIDD difficult. Therefore, the state has adopted a methodology for projecting GRT revenues based on land use, jobs by land use, and economic impact analysis using IMPLAN, which is a private proprietary economic model that measures how different sectors within an economy interact with each other. While IMPLAN is a highly regarded modeling tool, what it measures is not necessarily related to real estate market demand. Therefore, while IMPLAN generated GRT projections may show that a TIDD produces a positive net new GRT for the host community, there is no way to know if the project is actually generating new consumptive demand, which is where real GRT growth comes from, or if the demand is merely moving from one location to another within the community. Other states that use only property and/or sales tax revenues for tax increment districts tie revenue projections directly to potential real estate development-related property and retail sales activity. In these cases, real estate demand may provide a better, or at least more transparent, measure of potential revenues from a tax increment district than the methodology used for projecting TIDD revenues in New Mexico.

Third, the required content for the tax increment development plan (Section 5-15-1) focuses primarily on the district's boundaries, expected costs, projected revenues, and the estimated time required to pay back costs. There are other general requirements regarding land use, job creation, and other potential community benefits that could be incorporated into a plan but are not required. There are no specific performance requirements regarding job creation or other economic or community benefits; moreover, there are no standards for evaluating whether certain costs are appropriate for the district based on any specific community objectives for the district. In other states, plan documents required to form a tax increment district often include specific community goals associated with the district and demonstrate how the projects the district may finance will further these goals.

The focus on defining projects and their costs as key components to a TIDD development plan highlights another difference between New Mexico tax increment districts and those in other states. In New Mexico, the list of projects and project costs included in the development plans

[4] New Mexico Statue Section 5-15-2
[5] https://www.avalara.com/us/en/learn/whitepapers/service-taxability-by-state.html

establish a dollar amount that the district is expected to produce. In other states, districts can fund projects based on the revenue the tax increment produces, but there is no commitment to funding a certain level or cost of improvements. As a result, other states' districts may be more aspirational depending on revenues, whereas New Mexico TIDDs make a much firmer commitment to a total dollar amount that will be made available to the district. Of course, in New Mexico and other states, there is no legal requirement for local jurisdictions to backfill revenues from other sources if the tax increment districts do not perform as expected. Also, TIDDs in New Mexico, like in other states, do sunset after a specified term, usually 20 or 25 years, so if the districts do not produce the total expected revenue threshold set by the projected costs, there is no legal obligation to make up any revenue deficiencies.

New Mexico TIDDs also have much more governance autonomy than tax increment districts in other states. TIDDs are governed by a five-member governing body, which in the initial years is appointed by the local jurisdiction's governing body. But terms for these board members are relatively short, and after six years, qualified voters in the district start electing board members (§ 5-15-10). TIDDs can include residential neighborhoods, but because the tool is designed to foster economic development and job growth, in practice, most TIDDs do not include any residents who are registered voters, in which case, property owners vote in TIDD elections, with each owner's vote apportioned by the number of acres they own in the district(§ 5-15-8). This autonomy also has significant ramifications for how revenues allocated to the TIDD are spent. While the district cannot change the list of projects it plans to deliver without approval from the host jurisdiction's governing body, the TIDD board can have considerable discretion over when and how it spends this money, including deciding when to borrow money using bonds, or how to expend revenues for operation and maintenance expenditures, which are very broadly defined under the state statue (§ 5-15-12).

In practice, the net result of the TIDD project cost estimates set an upper limit on revenues the district can claim for its use, the long-term governance structure controlled by property owners, and the flexibility to use funds for a wide variety of operating and maintenance costs has two major implications. First, it appears that there is a possible incentive for developer initiated TIDDs to set their costs as high as possible in the initial district formation process, including extensive funds for operation and maintenance. And second, over time, there is little or no incentive for the district's board to work with the local jurisdiction's governing body to amend district plans as local conditions may change or priorities may shift. As a result, local jurisdictions may be giving up considerable annual tax revenues for an extended period of time without any way to change course. In effect, TIDDs become their own small enterprise districts with budgets, funding, and decision-making powers, whereas in most other states tax increment districts are primarily a funding and financing tool.

Royal Crossing Proposed TIDD Costs

Figure 1 shows the proposed public improvements and their associated costs included in the Royal Crossings Tax Increment Development Plan as of July 2020 which total $48,949,521. In reviewing these costs, the first step is to determine if they are all allowable under state statute (Section 5-15-3), which they appear to be given how vague the statue is about allowable costs. But this raises additional questions as to whether the district ***should*** cover these costs and what would be in the City of Las Cruces' best interests. As the discussion above points out, these costs can be construed as reflecting what's the developer's best interest.

FIGURE 1: TIDD COST SUMMARY

TABLE 2
TIDD COST SUMMARY
PUBLIC IMPROVEMENTS

	ESTIMATED COST		
IMPROVEMENT DESCRIPTION	HARD	SOFT	TOTAL
INITIAL INFRASTRUCTURE COSTS	2,970,857	742,714	3,713,571
SAMARITAN DRVE (MERCY STREET TO SOLANO DRIVE	699,600	174,900	874,500
PIONEER AVENUE (MERCY STREET TO MADRID AVENUE)	624,800	156,200	781,000
HEART AVENUE (SAMARITAN DRVE TO SAMARITAN DRVE)	899,800	224,950	1,124,750
MADRID AVENUE (BETWEEN N MAIN ST AND SOLANO DR)			2,300,000
LEGACY DRIVE (HEART AVENUE TO SAMARITAN DRVE)	1,117,600	279,400	1,397,000
SOLANO DRIVE INTERCHANGE	377,200	94,300	471,500
WATER RETENTION	1,393,920	348,480	1,742,400
SURFACE PARKING	5,328,000	1,332,000	6,660,000
STRUCTURED PARKING	17,280,000	4,320,000	21,600,000
PUBLIC COMMUNITY AREAS	7,587,840	696,960	8,284,800
GRAND TOTAL	**38,279,617**	**8,369,904**	**48,949,521**

Source: Tax Increment Development Plan: Royal Crossing Tax Increment Development District, May 26, 2020 updated July 14, 2020

To answer these questions, it is helpful to consider the Royal Crossing proposal in the context of a typical master planned development project. Master planned projects are generally initiated by a single master developer. Master developers buy or control sites large enough to support a significant amount of future development that would include a mix of land uses. The best sites for master development projects are typically greater than three to five acres lack certain prerequisites that would allow the envisioned development to occur. These could include the necessary planning approvals or entitlements from the local jurisdiction, and sufficient infrastructure on, and sometimes off, the site to support the anticipated amount of development. However, because there are costs and risks involved in providing these prerequisites, the land value is relatively low. The master developer then invests the necessary funds to provide the improvements necessary to enable the development to move forward, but these investments are also expected to increase the land value sufficiently to cover the developer's costs, provide a return on investment, and mitigate some risk for land buyers. Or some master developers do their own development projects as well as preparing the site for other developers. In any case, it's up to the master developer to determine what they think they can "afford" to invest in their site, given these costs weighted against potential future revenues, and then to determine if the project is feasible.

In the Royal Crossings TIDD project costs, the developer, who would act as both the master developer and may or may not do any actual development projects, appears to be shifting responsibility for some standard master developer costs on to the TIDD. By making this shift, the developer is asking the City to share the risk for developing the project, justifying this by claiming that development at the Royal Crossings site meets multiple public objectives including providing “high quality” development at this priority infill location, bring new investment into an area where very limited investment is occurring, generate as many as direct 1,500 jobs, and make certain roadway improvements that would benefit a larger area than just the district.

From the City’s perspective, achieving these policy objectives may provide sufficient rationale for agreeing to form a TIDD. However, it could also be in the City’s best interest to minimize the total cost of the TIDD as much as possible. This would enable the City to support the project, while also minimizing the TIDD’s impact to the City’s General Fund, and giving the City the ability to capture more “upside” from the project by committing fewer GRT and property tax dollars to the TIDD over all as well.

Figure 2 shows four illustrative scenarios that suggest how the City could have negotiated lower TIDD costs based on multiple considerations including: a) Which costs a master developer would normally bear; b) minimizing total size of the TIDD; and, c) assuming that the City could get more and better amenities for a lower cost by finding other ways than the district to pay for these improvements. These scenarios are presented as cumulative cost reductions and they are not necessarily the only way that costs could be eliminated from the district. But the intent is to illustrate a strategic approach to evaluating district costs while still meeting certain policy objectives. Each scenario and its rationale is explained below.

Scenario 1 eliminates all parking costs from the TIDD. Adequate parking is an essential element to any successful development project. This is especially true with retail projects which comprise a significant portion of the Royal Crossings development project. In addition, building values for new commercial buildings are predicated in part, on having adequate parking to serve the tenant or future user’s needs. Thus, it would seem critical for the private building owners to also control their required parking fields. While shopping centers often have complicated agreements around parking easements, these are all predicated on private ownership of the parking spaces. However, if the TIDD were to pay for any parking at the Royal Crossing site, when the district sunsets, the City would own the parking. While the City and the Royal Crossing developer had worked out a potential agreement on how a parking structure would be operated and maintained, should such a structure be built by the district, there did not appear to be a similar agreement for the surface parking lot. But, given that parking, especially surface parking is typically considered a standard development cost, there is no reason why the City should agree to pay for this cost with its tax revenues, and there is especially no reason why the City should own a surface parking field or a structured parking garage to support what is essentially a suburban style development project. Eliminating the surface parking cost ($6.6 million) and the structured parking garage (approximately $17 million) would reduce the TIDD cost by over $28 million to about $21 million.

Scenario 2 removes future parks that would be built within the master development. Figure 1 shows a total cost of approximately $8.2 million for public community areas. However, Figure 2 disaggregates these costs into three separate categories. The cost to develop future parks on the site has been shown as a $3.4 million dollar cost to the district. In this scenario, these future parks would be built by the master developer, not by the TIDD.

Because there is no adopted PUD plan for this site, it is not clear what the character of these “future parks” might be. if the park space is built with district money, then it will be publicly owned when the district sunsets. Therefore, the future use and users for this park should be well understood to justify this cost. If Royal Crossing was going to be a large new residential neighborhood then It might make sense for the City to add new park space in this area to accommodate future residents. But according to the TIDD Financing Plan Revised 7-14-20 FINAL, the project is expected to include only 513 housing units that could targeting potential households with children (337 multifamily units, 148 multifamily mixed-use units, and 28 townhomes), and 270 senior living units, for a total of 783 units. Although this many units will undoubtedly generate demand for park space is there enough demand to warrant building a new park in this location, and if so, then any such park should be sited and designed to also accommodate the general public for a larger area, not just to benefit residents and other users in the Royal Crossings area. Or it is possible that some of this new park demand could potentially be accommodated elsewhere in the City, including at Apodaca Park, thus eliminating, or greatly reducing the need for park space within the Royal Crossings area. On the other hand, plazas or open space amenities should be included in the overall Royal Crossings site plan. But these spaces would function as amenities primarily for use of district residents and other visitors. In this case, these spaces are value enhancements for the private development, not parks designed for the general public’s use. Therefore, these costs should be borne by the master developer, not the TIDD. It is very common for developers to be required to provide public open space amenities as a part of a PUD where the developer pays to build, operate, and maintain these spaces. Removing future would eliminate another $3.4 million from the TIDD, further reducing total costs to about $17 million.

Scenario 3 would remove Apodaca Park improvements from the district costs. In the revenue projections prepared by the developer, these improvements would not likely be made for at least ten years after district formation. However, by including this cost in the district, rather than finding another way to pay for them, the district is committed to potentially collecting an additional $2.8 million. As an alternative, the City could potentially use a city-wide parks bond or other funding sources to pay for these improvements. The cost to the City to issue this bond would be lower than the cost to borrow money through the TIDD; and the improvements could be delivered much sooner through a more transparent procurement process than if the district were responsible. This would result in a cumulative cost reduction amounting to approximately $14million.

Scenario 4 removes the proposed trail system costs. These costs could be paid for through some other mechanism, including a parks bond, as discussed above. Or these costs could be planned as active transportation improvements that would enable people to move around the City by walking or biking. Transportation improvements may be eligible for other sources of county, regional, state, or federal transportation grant funds, in which case, neither the City nor the district would need to pay for this additional $2 million.

FIGURE 2: TIDD COST SCENARIOS

	Proposed Developer Costs	Scenario 1: Cost without Parking	Scenario 2: Cost without Future Parks	Scenario 3: Costs without Apodaca Parks	Scenario 4: Costs without trails
Initial infrastructure costs	$3,713,571	$3,713,571	$3,713,571	$3,713,571	$3,713,571
Samaritan Drive	$874,500	$874,500	$874,500	$874,500	$874,500
Pioneer Avenue	$781,000	$781,000	$781,000	$781,000	$781,000
Heart Avenue	$1,124,750	$1,124,750	$1,124,750	$1,124,750	$1,124,750
Madrid Avenue	$2,300,000	$2,300,000	$2,300,000	$2,300,000	$2,300,000
Legacy Drive	$1,397,000	$1,397,000	$1,397,000	$1,397,000	$1,397,000
Solano Drive Interchange	$471,500	$500,214	$500,214	$500,214	$500,214
Water retention	$1,742,400	$1,742,400	$1,742,400	$1,742,400	$1,742,400
Trail system improvements	$2,000,000	$2,000,000	$2,000,000	$2,000,000	$0
Apodaca Park improvements	$2,800,000	$2,800,000	$2,800,000	$0	$0
Future Parks (within the development)	$3,400,000	$3,400,000	$0	$0	$0
Surface parking	$6,660,000	$0	$0	$0	$0
Structured parking garage	$21,600,000	$0	$0	$0	$0
Total Cost	**$48,864,721**	**$20,633,435**	**$17,233,435**	**$14,433,435**	**$12,433,435**

Source: Strategic Economics, 2020.

TIDD Annual Revenue generation and Development Phasing Assumptions

State statute (§ 5-15-5) requires that a TIDD tax increment development plan include an estimate of annual projected GRT and property tax revenues to be collected by the district. Projecting these revenues requires a series of assumptions including when development will occur/ be phased over time, the amount of tax revenues this development will generate each year reflecting incremental increases due to new development, and what tax rates will be applied to the gross revenue to determine how much money will go to the district and how much will be retained by the local jurisdiction. However, the Royal Crossing TIDD Financing Plan Revised 7-14-20 FINAL does not include any annual revenue projections. Tables 5A and 5B show the assumed tax rates for the GRT and property taxes for both the City and Dona Ana County. Tables 6A and 6B (page 19) show total cumulative GRT and Property revenues, and what annual recurring revenues will be after project build out. However, this information is insufficient on its own, to evaluate the district's potential revenues in relation to the proposed costs.

The Resolution No.20-176 packet given to the City Council for proposed adoption on July 6, 2020 includes a memo from Hilltop Securities dated April 7, 2020 that evaluates the district's proposed financing plan and points many deficiencies or inaccuracies included in the Plan, including the lack of annual projected gross receipts. Hilltop Securities was retained jointly by the City and Dona Ana County to evaluate the initial tax increment financing plan submitted by the developer. Also included in the packet was a response to the Hilltop Securities Memo prepared Goldenrod Companies (the developer) providing supplemental information to address the many issues and concerns raised by Hilltop Securities in the April 7 memo. In a follow-up memo dated May 8, 2020, Hilltop Securities evaluated the additional information provided by Goldenrod, although this second memo was not included in the July resolution.

In its May 8 memo, Hilltop Securities acknowledges that the supplemental information from Goldenrod did provide both an annual cash flow projection for the district, and an annual estimate of sources and uses showing how the projected annual revenues compared to projected costs incurred by the district. However, in this memo, as in the earlier memo from April, Hilltop Securities raised concerns over the costs included in the district, pointing out that some costs, like land acquisition, are not typically included in TIDD costs, and questioning the operation and maintenance costs. However, the memo also suggests that the developer's cash flow, which estimates total cumulative revenues of $243 million be further investigated to evaluate what minimum annual revenue would be required by the district to support its financing needs, and that based on this, that the City then lower the percentage of revenues it would contribute to the district, along with several other recommendations regarding the district's potential financing structure.

Since Hilltop Securities provided the City and County with these memos, the Company also provided staff with a copy of a sources and uses financial model which could be used to test the sensitivity to the financing plan if the City and County tax rate contributions to the district were reduced. One outcome of this was that the City reduced its share of GRT from 75 to 70 percent and operating and maintenance costs were removed from the district costs.

However, in reviewing the sources and uses model, shared with the City, there seem to be two issues. The first is that the annual development phasing, which represents the annual revenue sources, does not reflect the most current development phasing assumptions in the proposed final Financing Plan. This means that the sources and uses analysis conducted in May has not be updated and retested based on subsequent changes in the sources (land use mix and phasing for the Royal Crossings project) that are reflected in the most recent Financing Plan. Second, the project costs, or uses, were not be modified to reflect any potential cost reductions suggested by Hilltop Securities. As a result, the City has very imprecise information about how well the Financing Plan will perform and whether further negotiation could have been conducted that would have enabled the developer to move forward with the Royal Crossings project, while further minimizing the City's revenue exposure.

The Proposed District Governance Structure

According to state statute (§ 5-15-10), the governing body from the jurisdiction creating the TIDD has the option to serve as the district board, or to appoint a five-member board as specified in § 5-15-10 (D). However, developer initiated TIDDs in New Mexico appear to always have an appointed district board, rather than having the governing body serve in this capacity. From the developer's perspective, this makes sense. But as with establishing the district's initial costs, this governance structure could create a misalignment between the developer's and the public's interest, especially if the district does not generate the level of anticipated revenues and can not deliver the proposed public improvements.

In most other states, elected district boards may be more common where district members are voting to tax themselves. But in the case where a district is using a local jurisdiction's revenues, i.e., basic tax revenues, the governing body could make a case appointing itself as the district board. This would serve to make the district more directly accountable to larger community and create an opportunity for greater flexibility with managing district funds over time.

Potential Lessons Learned for Las Cruces

Although the Royal Crossings TIDD proposal was withdrawn, it is possible that at some point in the future, Las Cruces will receive another request for a developer initiated TIID. Therefore, the following lessons learned reflect findings from this review and offers possible future approaches the City could take in if and when another such proposal come forward.

1. **Seek outside assistance with evaluating and negotiating a TIDD**. Establishing a developer-initiated TIDD is a complicated process and takes very specific experience and expertise. Also, because this is not necessarily a commonly used tool in New Mexico, many cities have long-term highly qualified staff people, but these staff may still lack any exposure to the TIDD process and the detailed analyses required to establish the district's revenue projections. In addition, the because of the way New Mexico's enabling legislation is written, the developer has an incentive to make district costs as high as possible. Developing a good strategy for evaluating the key relationship between costs and potential revenues should be at the heart of a TIDD formation process. But if staff does not have the right inputs, it is not easy to understand this process. City staff did, very appropriately, rely heavily on legal counsel and Hilltop Securities for some

technical analyses. But the results did not necessarily deliver the most strategic TIDD Financing Plan that could both meet the City's policy larger objectives and provide some incentive to the developer.

2. **Require the annual cash flow and sources and uses analysis as the main building block for evaluating a TIDD.** The developer appears to have omitted this information, which is required by state statue, from their initial Financing Plan. As a result, Hilltop Securities was not able to evaluate the district's efficacy until relatively late in the process. Also, the recommendations made by Hilltop Securities regarding both cost and revenue assumptions were not necessarily tested and used to recalibrate the District Financing Plan. Instead negotiations with the developer focused primarily on cost reduction, which is critical, but not enough on revenue projections and financing options. As a result, the final Financing Plan did not include any annual revenue projections, as mandated by the state, and the revenue projections that had been provided in late April did not match the final proposed development program/phasing, and were therefore technically, incorrect.
3. **Establish clear policy objectives for undertaking a TIDD that can also be used to evaluate the project costs.** Staff did present the Governing Body with general policy objectives to justify the TIDD. But it is not clear how early in the TIDD formation process these objectives were vetted, and whether these were considered against the policy trade-offs required when deciding to use tax increment financing. As was discussed above, using tax increment revenues to fund capital projects requires making trade-offs regarding how General Fund revenues get uses. TIDDs can be powerful tools for incentivizing economic development, but not every district will deliver powerful results. Therefore, it is important for the Governing Body and community members to fully understand and agree to these trade-offs before moving into the process of evaluating and negotiating a district financing plan.
4. **Evaluate the option to have the governing body serve as the district board.** Apparently, the City's legal counsel strongly advised against this option. But the rationale for this was never fully clear. Also, because this was a developer-initiated TIDD, the developer may not have agreed to this governance structure. But, given the issues identified above regarding the challenges with developers having long-term control over TIDDs, the City may want to explore and better understand this option prior to, or early in the process of evaluating another TIDD proposal.