

DOWNTOWN TUCSON INITIATIVE PROPOSED REFORM AND STANDARDIZATION ACT

I. GENERAL HISTORY

In 1999, Arizona adopted A.R.S. Section 48-4201 et seq. (together with certain related taxation statutes, “the Act”) for the purpose of encouraging job and revenue growth in Tucson. In Proposition 400, Tucson took advantage of the authority granted to it in the Act and established the Rio Nuevo Multipurpose Facilities District (“the District”). The District was intended to promote job creation and enhanced development, pursuant to the Act, in a geographical area that includes most of downtown Tucson and extends east along the Broadway corridor (“the Rio Nuevo Area”). The Act also established a Board of Directors (“the Board”) for the District. The Act funded the District by allocating to the District, through 2025, part of the State’s portion of the sales taxes (“TIF Monies”) generated within the District. The Act authorized the District to direct TIF Monies to certain projects, though from the beginning there was disagreement over exactly what projects and types of projects were eligible to receive TIF Monies from the District: some argued that the District was authorized to direct TIF Monies only to the development of the Tucson Convention Center, an adjacent hotel, and related projects (“Primary Projects”), while others argued that the District was authorized to direct TIF Monies to Primary Projects as well as to other projects owned by the District (“Owned Projects”), and yet others argued that the District was authorized to direct TIF Monies to the above and also to privately owned site-specific projects (“Private Projects”). This disagreement over the District’s authority caused (and continues to cause) significant confusion among interested parties and the community at large over the questions of exactly when, how, and at what locations TIF Monies can be spent. What is clear is that, prior to 2010, the Board (working with the City) spent \$230 million on all of the above, and in a very broad area, with very little result.

In 2010 the Act was revised by the Legislature in the hope that the missteps and errors of the past would not be repeated, and that the original purposes of the Act would be accomplished. Pursuant to that revision, the District was made largely into a State-run entity, the duration of its existence was extended, and the Board was reconstituted. Our goal at this time is to clarify and resolve the issues now facing the District and the Rio Nuevo Area, and to develop the Rio Nuevo Area rapidly and in a manner that, consistent with the revised Act and its purposes, will create jobs and generate increased revenues, which in turn will allow and fund even better and greater enhancements to the Rio Nuevo Area.

II. ISSUES

As noted above, certain issues have arisen that need to be clarified and resolved in order to achieve the goals of the Act. In particular, the District faces financial limitations, continuing questions over its authority to act, regulatory impediments to the development of the Rio Nuevo Area, and complications arising from longstanding disputes with the City of Tucson:

A. Financial Limitations of the District. For various reasons, sufficient TIF Monies do not currently exist to complete the Primary Projects, and, in turn, the Owned Projects. Those shortages also have resulted in the inability of the District to give financial assistance to Private Projects in the Rio Nuevo Area. The problem of these financial shortages and limitations must be solved in order to move forward in achieving the goals of the Act and the District.

B. Authority of the District to Act. Further, as indicated above, there is considerable dispute as to whether (and how) TIF Monies can be spent -- that is, whether TIF Monies can be spent only for Primary Projects, or whether they also can be spent on Owned Projects and/or Private Projects. The Act specifically provides that TIF Monies may be spent on “multipurpose facilities.” (See A.R.S. Sections 48-4204(B) and 48-4237.) “Multipurpose facilities” are defined to include two components:

1. the “**primary component**,” which must be located within the District and on the particular site depicted on the publicity pamphlet circulated prior to the passage of Proposition 400, and must be “used to accommodate sporting, entertainment, cultural, civic, meeting, trade show or convention events or activities, fire, police or other public safety facilities and tourism offices” (see A.R.S. Section 48-4201(4)(a)), and
2. “**secondary components**,” which are those projects determined by the Board to be “necessary or beneficial to the primary component, [but] limited to on-site infrastructure, artistic components, parking garages and lots, and public parks and plazas” (see A.R.S. Section 48-4201(4)(b)). In addition, secondary components may include “related commercial facilities that are located within the multipurpose facility site.”

It is not clear that the past activities of the District have conformed to these statutes. Likewise, it is not clear that similar FUTURE activities of the District would be consistent with the statutes. Specifically, prior to 2010, the pre-2010 Board invested TIF Monies in a wide variety of projects throughout downtown and the west side (not just on “multipurpose facilities”). Further, the pre-2010 Board provided financial assistance to private developers. Given the above provisions of the Act, it is not clear that those expenditures were made in a manner that conformed to the definitions of either a primary or a secondary component of a multipurpose facility as defined above. Various legal opinion letters have been written to address some of these issues, but these are just opinion letters and are not the law. Thus, continued investment by the Board in such a range of projects, particularly including Private Projects, is (in our opinion) subject to the risk of challenge through litigation or otherwise on the grounds that it is improper either to make investments beyond multipurpose facilities or to provide financial assistance to private investors. To eliminate these risks of challenge and litigation against both the District and potential investors in the Rio Nuevo Area, and also to ensure that the anti-corruption and remediation purposes behind the Legislature’s recent revisions to the Act are realized, the Act

must be clarified to authorize District investment in areas beyond multipurpose facilities AND ALSO to permit the District to provide financial assistance to qualified Private Projects as well.

C. Regulatory, Procedural, and Other Structural Impediments.

1. City of Tucson Issues. Other problems also have become apparent and need to be solved in order to achieve rapid and efficient development, the creation of jobs, and the generation of increased revenues within the Rio Nuevo Area. Specifically, the Act does not adequately provide for coordination between the City of Tucson (which controls the regulatory bureaucracy governing development within the city, including in the Rio Nuevo Area) and the District (which, theoretically, has the money and plans for development in the Area). It is a common assumption that the District controls all development within the Rio Nuevo Area. But it does not. City ordinances and regulations still govern development in the Area. Thus, investors and job creators continue to encounter difficulties in moving forward with Private Projects in the Rio Nuevo Area due to City regulations and bureaucratic issues, even when it is the desire of the District to move those Private Projects forward. In turn, this has frustrated both the District and the Private-Project investors who are eager to move forward rapidly. The Act must be clarified to resolve these inconsistencies and to allow efficient regulation by the City as well as a degree of regulatory input by the District to assure such efficient regulation.

2. Development Fees and Other Disincentives. Currently, costs imposed upon developers through impact fees, utility-connection fees, and related charges increase the up-front expenses for any project, increase the developers' speculative risk, and therefore discourage investment in such development. In an area such as the Rio Nuevo Area, where reinvestment and revitalization are needed, the negative effect of these disincentives is magnified. Similarly, the increased property taxes assessed against properties after they are renovated acts as a disincentive to redevelopment.

3. Rio Nuevo Issues. In addition to the procedural and regulatory impediments at the City level, similar issues exist at the Rio Nuevo District level. In particular, the District has not standardized its guidelines and procedures for granting assistance and offering incentives to Private Projects within the District. This has caused confusion among developers and potential developers of Private Projects. This confusion discourages the desired progress within the District.

D. Disputes with the City of Tucson. Since 2010, the District has been involved in various disputes with the City of Tucson regarding the Primary Projects and the Owned Projects. These disputes involve hundreds of millions of dollars. Justifiably, this requires the current Board to focus on resolving these

past disputes, which, in turn, substantially reduces the ability of the Board to focus on future development and improvements within the Rio Nuevo Area. These disputes must be resolved in order to allow the Board to devote its time and energy to achieving the goals of the Act -- to create jobs and generate revenue within the Area.

III. SOLUTIONS

To assist in addressing the above issues, various parties have formed the Downtown Tucson Initiative, Inc., a 501(c)(6) non-profit corporation ("DTI"). The goal of DTI is to seek solutions to the above problems, generate a consensus for such solutions, and to effectuate and institutionalize such solutions by obtaining amendments to the Act and/or to the operating procedures of the City and the District.

Having studied these issues, DTI proposes the following modifications to the Act and/or to the procedures of the City and the District. Each of the above "Issues" can be resolved by the following proposed solutions:

A. Financial Limitations of the District. As noted above, the District does not have sufficient funds to undertake further projects in the Rio Nuevo Area. All TIF Monies have been committed by the pre-2010 Board. The post-2010 Board currently is working hard to resolve some of these problems by undertaking audits to see exactly where TIF Monies were spent previously. In turn, this will allow the post-2010 Board to begin to define where TIF Monies *might* have been misspent, and perhaps to recoup some of those monies. But this will be a long-term process that will likely involve major litigation. And in the meantime, the Board will continue to be unable to proceed for lack of funds.

Currently, pursuant to A.R.S. Sections 48-4203(B)(1) and 42-5031, the District is funded by incremental increases in sales-tax proceeds generated in the Rio Nuevo Area as follows: **The amount of the TIF is equal to THE LESSER OF (1) one-half of all the state sales taxes collected within the District, OR (2) the difference between all the state sales taxes collected within the District LESS (minus) the amount of state sales taxes generated within the District during 1999.**

In order to allow the District to move forward we recommend the following change be made to the Act in order to increase current funding available to the District immediately: **The Act should be amended to provide that, commencing immediately, the District shall begin to receive the lesser of (1) one-half of all the state sales taxes collected within the District, or (2) the difference between all the state sales taxes collected within the District LESS (minus) seventy-five percent of the amount of state sales taxes generated within the District during 1999.** This will result in an annual increase in TIF revenues to the District in an amount equal to twenty-five percent of the amount of state sales taxes generated within the District during 1999 (that is, \$ (25% of

the 1999 Base)) to allow it to recommence projects consistent with its status as a State-controlled entity.

We further recommend that **A.R.S. section 42-5031(B) should be amended to remove the language which restricts payments of TIF monies to the District in excess of “the amount required to service the debts and obligations of the district.”** Given the debt incurred by the previous Rio Nuevo Board, the current statute severely restricts the current Board’s ability to plan and engage in new projects, while this change would remove that restriction and give the Board more predictability and freedom to act.

Finally, we recommend that **A.R.S. section 42-5031(D) should be clarified, making clear that the City’s “matching” obligation can be satisfied only through direct cash payments to the Board, not by other expenditures, by the provision of services in kind, or otherwise.**

B. Authority of the District to Act. As noted above, A.R.S. Sections 48-4204(B) and 48-4237 limit the use of TIF Monies to “multipurpose facilities,” which are comprised of the “primary component” and the “secondary components.” Though various opinions have been offered about the extent to which these statutes, in practice, restrict the District’s participation in the development of projects within the Rio Nuevo Area, including the District’s authority to assist or participate in Private Projects, there still is concern that these statutes can be seen to authorize District action and expenditures only within a limited area near the Tucson Convention Center. Certainly, the performance audit conducted by Crowe Horwath raised concern over these issues. To remove any doubt and allow the District to proceed with development throughout the Rio Nuevo Area, including providing financial assistance to Private Projects, as it deems appropriate, the Act should be amended as follows:

1. The Act should be amended, as necessary, to provide for a “third component,” which would include projects anywhere within or immediately contiguous to the Rio Nuevo Area, not just closely adjacent to the TCC, so long as those projects benefit the District and are likely to increase employment and sales-tax generation within the District.

2. The Act should be amended to provide that ALL components allow the District to participate in, or financially assist, Private Projects in the following circumstances:

a. The Private Project meets City Codes (to be discussed below).

b. In the Board’s judgment, the Private Project will substantially increase sales-tax revenues, employment, and/or consumer and public traffic at the Project Site, and/or that the

Project presents a likelihood of creating an extraordinary increase in sales-tax revenues, employment, and/or consumer traffic generally in the District or portions thereof.

c. Any financial assistance will not violate the “Gift Clause” of the Arizona Constitution. In this regard, the Act should be amended in such a way as to specify that the Rio Nuevo District is a “tax levying public improvement district” that is exempt from the Gift Clause and thus may provide direct assistance to Private Projects pursuant to Article XIII, Section 7 of the Arizona Constitution. Moreover, the Act should make clear that developers of Private Projects may give the District conservation easements over such Private Projects in return for such financial assistance, and that the District may make loans to Private Projects, including but not limited to loans that are repaid by crediting the Private Projects with as much as the full value of any incremental increase in sales-tax revenues generated from a particular site over the amount of such revenues generated from the site at the time of the loan.

3. Section 42-5031(C), A.R.S., should be deleted by the Legislature. That provision of the Act currently provides that the “primary component” must be “constructed during the first phase of the project.” Since there exists substantial dispute over the timing and nature of the “primary component,” and this dispute may not be resolved for an unknown period of time, this provision must be removed in order to allow the Board to move forward in a manner consistent with the purposes of the Act.

4. The Act should be amended as necessary to clarify that the Board has authority to enter into transactions that might survive the termination of the District’s existence.

The District should agree to adopt clear, standardized procedures and policies for Private Projects to follow in seeking Board approval or assistance. (See Paragraph III(C)(3)(a), below.)

C. Regulatory, Procedural, and Other Structural Impediments.

1. City of Tucson Issues. As noted above, nothing in the Act gives the District the right to override or supercede the regulatory requirements (e.g., zoning, design approvals, construction permitting, safety-code permitting, occupancy permitting) imposed by the City for any project in the Rio Nuevo Area. Any attempt to transfer said regulatory powers to the District from the City likely would result in lengthy litigation, which would have questionable chances of success. Moreover, and in any case,

the District does not have the bureaucratic infrastructure necessary to regulate such matters. In addition, if the District were to attempt to develop its own staffing, rules, and infrastructure for these purposes, the costs would be prohibitive.

Rather than enter into a major dispute with the City in an attempt to preempt the City on these matters, we recommend instead that the provisions of existing legislation be utilized or adapted to resolve these issues. In particular, in 2011, the Arizona Legislature adopted SB 1598, which was called the Regulatory Reform Act (“RRA”). The RRA adopted a “Regulatory Bill of Rights” (“RBR”), as codified in new statutory provisions in A.R.S. Sections 9-831 to 9-837. The RBR requires the simplification of regulatory processes and seeks to assure foreseeability and certainty, and to reduce risk for private development projects throughout the state. The RBR will become effective on December 31, 2011, and applies to City regulations. Certain provisions of the RBR give significant new benefits and advantages to developers of Private Projects in dealing with the City. In particular, A.R.S. Section 9-835 of the RBR provides that by December 31, 2012, “[a] Municipality that issues licenses . . . shall have in place an overall time frame during which the Municipality will either grant or deny each type of license it issues.” Thus, the RBR should be used as a basis for assuring an efficient and reasonable City regulatory process for Private Projects in the Rio Nuevo Area. This could be achieved either by negotiations with the City or by amending the RBR to clarify that **all City licenses (which includes all permits, applications, licenses, etc.) shall be granted or denied in not more than thirty days.**

2. Development Fees and Other Disincentives.

a. In order to eliminate the disincentives imposed upon developers through impact fees, utility-connection fees, and related charges, we recommend that **any city, county, or other local jurisdiction or subdivision thereof waive any impact or connection fees imposed within the District for connection to any utility or similar service provided by that jurisdiction or subdivision.**

b. **Appropriate language should be added to the Act by the Legislature to provide that any Private Project within the District shall, upon any upgrade, improvement, or change of use in a particular property, have its property taxes frozen for up to ten years at pre-development levels.** This provision would allow the local property-taxing authorities to continue to tax such projects according to their use and value prior to the development, and also allow for such increases in the amount of taxes collected as may have applied to the property without the development.

After the expiration of the abatement period, property taxes on any such project would increase gradually over a period of years until they match the post-development condition, use, and valuation of the project.

c. Similarly, any Private Project within the District should, upon any upgrade, improvement, or change of use in a particular property, receive an abatement in the site-specific (that is, site-generated) sales taxes. Again, after the expiration of the abatement period, such sales taxes would increase gradually over a period of years until they match the generally-applicable level of taxation.

3. Rio Nuevo Issues. In order to eliminate confusion concerning the procedures and guidelines by which developers of Private Projects can apply for, and participate in, incentives and other Rio Nuevo benefits, we recommend the following:

a. Clarify the Financial Programs and Incentives Available to Private Projects. The Board should immediately adopt a clear statement outlining an incentive program for Private Projects, so that potential developers of Private Projects know exactly what benefits are available from the District. This program should include (but not be limited to) the following financial programs for Private Projects in the Rio Nuevo Area:

i. Loans, at low interest rates, should be made available to Private Projects, with the Private Project credited for repayment with the full value of any incremental increases in sales tax revenues generated from that particular site over the amount of such revenues generated from the site at the time of the loan. The amount and terms of said loans must be left to negotiation between the Board and the developer of the Private Project, so long as the loan is to be repaid in full on commercially reasonable terms.

ii. The District should offer direct financial assistance to appropriate Private Projects in return for conservation easements in favor of the District. Such conservation easements could protect a wide variety of District interests, including but not limited to maintaining the ambiance or aesthetics of the District, and encouraging projects that directly benefit the District generally and/or other projects in the District (such as public parking, advertising space, open space,

cultural or sports usages that will draw large numbers of people to the entire area, etc.).

iii. **The District should adopt a program providing payment by the District of any un-waived impact and connection fees assessed by the City or County, as well as utility hookup fees assessed by various utility companies on Private Projects within the Rio Nuevo Area. The Board then should leverage its market position to negotiate reduced rates for these items with the relevant governments and utilities.**

b. **Adopt Clear Guidelines for Private-Project Participation.** The Board should immediately establish a clear set of guidelines for evaluating any applications for assistance to Private Projects. In particular, in order to participate in the above financial programs, developers of Private Projects should be required to show only that:

i. **The Private Project will be located in or immediately contiguous to the District.**

ii. **There is a substantial likelihood in the Board's opinion that the Private Project will generate a substantial increase in sales-tax revenues, employment, and/or consumer and public traffic within the District or portions thereof.**

iii. **The Project is feasible (financially and otherwise), creditworthy, and has a substantial likelihood of coming to substantial completion in a reasonable time period under the circumstances.**

iv. **The Project is in compliance with City codes.**

D. Disputes with the City of Tucson. As noted above, the District is involved in various disputes with the City of Tucson, which disputes involve hundreds of millions of dollars. While this is a major focus of the Board, it also represents an enormous potential liability to the City. Conversely, receiving cooperation (as opposed to opposition) from the City would greatly enhance the probability of effectuating the required legislative changes set forth above, as well as improve the District's ability to achieve the goals of the Act -- to create jobs and generate revenue within the Area. Thus, we propose that the Board should consider resolving the disputes with the City, perhaps by relinquishing some or all of its claims against the City in exchange for the following:

1. Legislative Cooperation. The Board should demand that the City provide affirmative, active, and vigorous support to the Board and DTI in lobbying the Legislature to make the statutory changes and amendments set forth above.

2. Regulatory Cooperation. The Board should demand that the City agree to and cooperate in making the regulatory changes set forth in Paragraph III(C), above.

3. Contractual Cooperation. The Board should demand that the City agree to the termination, renegotiation, and/or formation of intergovernmental agreements as is necessary to effectuate all of the above.