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June 28, 2007

Internal Revenue Service
CC:PA:LPD:PR (REG-136806-06)
PO Box 7604
Ben Franklin Station
Washington, DC 20044

RE: REG-136806-06: Payments in Lieu of Taxes (PILOTs)

Ladies and Gentlemen:

The National Association of Bond Lawyers (NABL) respectfully submits the attached comments in response to the Notice of Proposed Rulemaking in the Federal Register on October 19, 2006 (REG-136806-06), relating to payments in lieu of taxes (PILOTs).

NABL appreciates the effort of the Department of the Treasury and the Internal Revenue Service in addressing these issues as well as the request for and consideration of NABL's submission.

The comments were prepared by a NABL Task Force on PILOTs identified in Exhibit A to this letter.

NABL believes that participating in the guidance process supports clarification of and facilitates compliance with the tax law and regulations. Accordingly, NABL members would welcome the opportunity to discuss these recommendations to achieve clarity, certainty and administrability in this area of the law.

NABL exists to promote the integrity of the municipal market by advancing the understanding of and compliance with the law affecting public finance. A professional association incorporated in 1979, NABL has approximately 3,000 members and is headquartered in Chicago.

If you have any questions, please contact me at 949/725-4237 or through email at clew@sycr.com or Elizabeth Wagner, Director of Governmental Affairs at 202/682-1498 or through email at ewagner@nabl.org.

Thank you again for the opportunity to submit NABL's comments.

Sincerely,

Carol L. Lew

Carol L. Lew

Enclosures

Cc: Eric Solomon
Donald L. Korb
Michael J. Desmond
Lon B. Smith
John J. Cross III
Rebecca L. Harrigal
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NABL Task Force on PILOTs (Exhibit A)

National Association *of* Bond Lawyers

RECOMMENDATIONS
BY THE
NATIONAL ASSOCIATION OF BOND LAWYERS
TO THE DEPARTMENT OF THE TREASURY
AND THE
INTERNAL REVENUE SERVICE
RELATING TO THE TREATMENT OF PAYMENTS IN LIEU OF TAXES
UNDER SECTION 141 OF THE INTERNAL REVENUE CODE

I. Introduction

The National Association of Bond Lawyers ("NABL") submits the following comments in response to the Internal Revenue Service's solicitation for public comments on proposed regulations (the "Proposed Regulations") published in the Federal Register on October 19, 2006 (Reg-136806-06), relating to the treatment of a payment in lieu of taxes ("PILOT") under Section 141 of the Internal Revenue Code of 1986, as amended (the "Code"). Various people contributed to the preparation of these comments, including a task force formed by NABL. (*See* Exhibit A for a list of members.)

NABL welcomes the opportunity to comment on the Proposed Regulations following two recent private letter rulings ("PLRs") addressing PILOTs as taxes of general application. While NABL appreciates guidance regarding the interpretation of the Code, NABL has both substantive and procedural concerns with respect to certain aspects of the Proposed Regulations. These recommendations address the conformity of federal tax restrictions in the Proposed Regulations to PILOT arrangements under current State and local laws.

Under Section 141 of the Code, a tax-exempt bond will constitute a private activity bond if the issue of which the bond is a part satisfies both the private business use test of Section 141(b)(1) of the Code and the private security or payment test of Section 141(b)(2) of the Code. "Generally applicable taxes," as defined in Treas. Reg. §1.141-4(e), are not considered "private security" or "private payments" for purposes of satisfaction of the private security or payment test.

Treas. Reg. §1.141-4(e)(2) defines a "generally applicable tax" as an enforced contribution exacted pursuant to legislative authority in the exercise of the taxing power that is imposed and collected for the purpose of raising revenue to be used for governmental purposes. Such a tax must have a uniform rate that is applied to all persons of the same classification in the appropriate jurisdiction, and the tax must have a generally applicable manner of determination and collection.

Pursuant to Treas. Reg. §1.141-4(e)(3), a payment does not qualify as a generally applicable tax if it is a special charge for a special privilege granted or a service rendered. The Treasury Regulations further set forth certain permissible and impermissible agreements that signify whether or not a tax has a generally applicable manner of determination and collection, and provide that an agreement to reduce or limit the amount of taxes collected in furtherance of a *bona fide* governmental purpose is a permissible agreement. Thus, an agreement between a governmental entity and a taxpayer to subsidize a portion of the tax payments due does not alter the character of tax payments as taxes. Further, outright grants to a taxpayer do not alter the character of tax payments as taxes (*see* Treas. Reg. §1.141-4(e)(4)) nor do improvements that benefit a taxpayer (*see*, *e.g*., PLR 8945032).

Treas. Reg. §1.141-4(e)(5) (the "PILOT Regulation") treats PILOTs as generally applicable taxes for purposes of the private security and payment test, only if --

> (i) The payment is *commensurate with* and *not greater than* the amounts imposed by a statute for a tax of general application; and
>
> (ii) The payment is designated for a public purpose and is not a special charge (as described in paragraph (e)(3) of this section). For example, a payment in lieu of taxes made in consideration for the use of property financed with tax-exempt bonds is treated as a special charge. [*Emphasis added.*]

The PILOT Regulation was adopted after a narrower rule for PILOTs was initially put forward in 1994 proposed regulations. Those proposed rules were then expanded in 1997 final regulations in response to comments from a number of political subdivisions that the 1994

proposed rules did not conform to the practices used in various communities with respect to PILOTs.

Until 2006, there was little guidance interpreting the PILOT Regulation. In July 2006, the IRS released PLR 200641001 and PLR 200641002 (the "Stadium Rulings"), where the IRS addressed whether certain PILOTs securing bonds to finance stadiums (and certain other property) constituted private payments or security for purposes of the private security or payment test under Section 141 of the Code. In both Stadium Rulings, the financed stadium (and certain other property) was subject to private business use, for purposes of Section 141 of the Code, because of a leasing arrangement between the issuer and a private company ("Company") affiliated with a sports team ("Team"); the stadium was subleased to the Team. In both Stadium Rulings, the financed stadium property and site would generally be subject to generally applicable real property taxes unless an exemption was available; however, under State law, an exemption existed for real property owned by certain State and local governmental units. State law permitted certain State and local governmental units to enter into PILOT agreements, requiring PILOTs equal to all or a portion of real property taxes that would otherwise be payable with respect to the property.

In the Stadium Rulings, Company agreed to pay a fixed amount of PILOTs to the bond issuer each year that would be in excess of the debt service on the bonds but would not exceed the real property taxes that would have been levied on the property absent the PILOT agreement. The PILOTs to be paid reflected the issuer's judgment as to the amount of real property tax abatement necessary to induce the Team to remain within the issuer's jurisdiction.

The IRS analyzed whether the PILOTs were "commensurate" with respect to the real property taxes otherwise payable. Noting that the preamble to the PILOT Regulation indicated that the PILOT rules were to be flexible, the IRS stated that, in the context of the stadium project, commensurate should mean "corresponding or proportionate in measure." In the Stadium Rulings, the PILOTs formula had a reduction based on the deemed benefits associated with the stadium project and inducements sufficient for the Company and the Team to go forward with the project. Noting that the PILOTs were the same magnitude as the initial projected property taxes and that the PILOT Regulation did not require the proportion to be

consistent, the IRS determined that the PILOTs were commensurate. The IRS also determined that the PILOTs were: (i) intended to be used for a public purpose (debt service on bonds furthering economic development and recreational opportunities); and (ii) not intended to be a "special charge" as the PILOTs were a reduced version of the real property taxes otherwise payable.

Shortly after the public release of the Stadium Rulings, the IRS released the Proposed Regulations altering the restrictions relating to the treatment of PILOTs under the private security or payment test of Section 141 of the Code.

The Proposed Regulations amend existing Treas. Reg. §1.141-4(e)(5) by setting forth standards defining what is meant by a payment "commensurate with" and not greater than the amounts imposed by a statute for a generally applicable tax in each year. This proposed definition, in its entirety, reads as follows --

> (ii) Commensurate standard. For purposes of this paragraph (e)(5), a payment is "commensurate" with generally applicable taxes only if the amount of such payment represents *a fixed percentage of*, or reflects *a fixed adjustment to*, the amount of generally applicable taxes that otherwise would apply to the property in each year if the property were subject to tax. For example, a payment is commensurate with generally applicable taxes if *it is equal to the amount of generally applicable taxes in each year, less a fixed dollar amount or a fixed adjustment determined by reference to characteristics of the property, such as size or employment.* A payment does not fail to be a fixed percentage or adjustment as a result of a *single change* in the level of percentage or adjustment following completion of development of the subject property. The payment must be based on the *current assessed value* of the property for property tax purposes for each year in which the PILOTs are paid and that assessed value must be determined *in the same manner and with the same frequency* as property subject to generally applicable taxes. A payment is not commensurate if it is *based in any way on debt service on an issue or is otherwise set at a fixed dollar amount that cannot*

> *vary with the assessed value of the property* determined in the manner described in this paragraph (e)(5)(ii). [*Emphasis added.*]

II. Executive Summary

Certain States permit PILOT arrangements. The method of calculating PILOTs varies with the jurisdiction and is far broader than the methodology permitted under the Proposed Regulations. NABL recommends that any alteration to the PILOT Regulation provide flexibility for State and local governments in conforming tax-exempt financing of publicly-supported facilities to State and local law. NABL is concerned about the rapid shift in tax policy regarding PILOTs from the thoroughly considered interpretation of the PILOT Regulation in the Stadium Rulings to the treatment in the Proposed Regulations, issued shortly after public release of the Stadium Rulings.

Regardless of the political, legal, or other reason that a PILOT financing structure is utilized, if that financing could be accomplished on a tax-exempt basis when supported by *ad valorem* or sales-and-use taxes themselves, that same financing should be permitted when supported by PILOTs, if those PILOTs do not exceed the taxes otherwise payable. Public support by a State or local government through the use of tax reductions (through abatements, PILOTs, or grants) should be irrelevant to that jurisdiction's ability to access tax-exempt bond financing. The tax rules should not dictate the structure of the transaction when valid governmental purposes or State or local laws exist dictating the selection from alternative taxing structures. Reductions of tax payments by agreement or grant do not alter the characterization of taxes (and no special rules restrict the flexibility of the governmental unit in tailoring the subsidy); PILOTs should be treated in a similar manner.

Further, NABL applauds the provision in the Proposed Regulations that eliminates the "special charge" example in the PILOT Regulation as such example is ambiguous and unclear; however, NABL does provide certain suggestions for clarity with respect to the prohibition on special charges. Lastly, NABL strongly recommends that any final regulations have a prospective effective date.

III. Background on Tax-Incentivized Municipal Financing

A. In General

Depending on the State constitution, State law, or local law, a municipality or other political subdivision undertaking to subsidize a project (typically for economic development purposes) may adopt any of several structures with substantially identical economic consequences. For example, among other possibilities, a political subdivision may: (i) provide direct cash subsidies to the private owner or lessee of the project, while maintaining the project on the tax rolls and fully subjecting it to *ad valorem*, sales, and other excise taxes; (ii) maintain the project on the tax rolls, but provide for partial abatement of *ad valorem* or other taxes; (iii) take actions (*e.g.,* through an acquisition/leaseback of private property) to remove the project from the tax rolls, but require that the private lessee make payments in lieu of taxes in accordance with a schedule that is either negotiated or determined in some other manner; or (iv) negotiate with a private lessee (*e.g*., in the context of total or partial privatization of military facilities) for reduced payments in lieu of taxes as an incentive for the development of an otherwise exempt property.[1] In each case, the private owner, lessor, or lessee, as the case may be, is incentivized to undertake the project by reason of the resulting reduced net tax burden (*i.e.,* the taxes reduced by continuing grants or abatement, or the taxes eliminated by governmental action and replaced by PILOTs). As noted, each of these structures can be employed to produce the same economic consequences; the choice from these (or other) structures is a function of State or local law and politics, not (typically) a function of federal income tax considerations.[2] As an additional incentive for economic development, a political subdivision may also subsidize all or a portion of the capital cost of the project by making a direct grant or making available the proceeds of its debt obligations.

B. Overview of PILOT Agreements

Certain States authorize local governments to negotiate, under particular circumstances, PILOTs to be paid by private parties. Some State and local governments have

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[1] While this discussion refers to an abatement or credit to *ad valorem* tax, abatement or credit is equally applicable to sales-and-use taxes.

[2] Certain State law structures involving bonds supported by *ad valorem* real property taxes can be economically similar to PILOTs. *See* Exhibit B.

enacted their own laws and guidelines with respect to PILOTs, particularly with respect to *ad valorem* property taxes. Certain laws authorizing PILOTs used in twelve States are briefly summarized in Exhibit C; however, these States are only a representative sample of the States that permit the negotiation of some form of PILOTs.[3] Because the laws of each State or local government are unique with respect to the implementation of PILOTs, PILOTs that occur in these various jurisdictions are difficult to categorize; generally, however, PILOTs take one of three forms.

The first and most straightforward form of PILOTs is an agreement directly between a taxing authority and a private party to make PILOTs in lieu of the tax payment that the private party would otherwise be required to make. In most cases, the PILOTs payable by the private party are less than the taxes that otherwise would have been payable, and these reduced payments are an incentive to the private party to locate or expand a business in the taxing jurisdiction. Most States that permit the direct negotiation of such a PILOT agreement between the taxing authority and the private party limit the type of business or transaction in which a PILOT agreement is permitted. For example, State law may permit a taxing authority to negotiate PILOT agreements only with respect to projects that are located in a redevelopment area.

Many States have constitutional provisions that do not permit the first form of PILOTs, and, therefore, a second form of PILOTs has developed. A common constitutional provision in many States is a requirement that all property be taxed equally. Such a constitutional requirement is sometimes explicit or is sometimes implicit in the equal protection clause of the State constitution. This type of constitutional provision frequently prevents local taxing authorities from negotiating PILOT agreements directly with a private party because taxing the private party less than a similarly situated taxpayer would be constitutionally impermissible. These same constitutional provisions that require the equal taxation of property usually exclude from this limitation governmentally-owned property and property owned by certain types of charitable entities, *e.g.*, non-profit hospitals and schools. In an effort to promote economic development by offering tax abatement to prospective businesses, many jurisdictions have created a structure to avoid these constitutional limitations, particularly the requirement that

[3] NABL has not performed a comprehensive survey of all States.

properties be taxed equally. Under this structure, the property that is the subject of tax abatement is conveyed to a governmental entity, usually a political subdivision or an industrial development authority established by the political subdivision, and leased back to the private party. Because title to the property is held by a political subdivision, the property becomes exempt from taxation. In most cases, the local taxing authority does not want the property to be totally exempt from taxation, and the local taxing authority (or the industrial development authority, as the case may be) requires that the lease or other separate agreement provides for PILOTs made by the private party as long as the property is governmentally owned. These payments will generally be less than the taxes that otherwise would be payable with respect to the property, as the primary goal of this structure is usually to provide tax abatement. Since many of these transactions involve industrial development authorities, many of these PILOT transactions are structured as an issuance of bonds the proceeds of which are used to construct the facility leased to the private party.

A third form of PILOTs can best be characterized as voluntary PILOTs. As referenced above, property owned by certain types of charitable entities is exempt from property taxation in many States. Property owned by the federal government is also generally exempt from property taxation. In some cases, a charitable entity, (*e.g.*, a college), or the federal government, may be the largest property holder in a taxing jurisdiction. Although the charitable entity- or the federally-owned facility is exempt from taxation, the charitable entity or the federal agency that operates the facility may choose to make PILOTs because the political subdivision cannot provide adequate essential governmental services without PILOTs. In these situations, the PILOT transaction is implemented for a reason completely opposite from the PILOTs described above: instead of the political subdivision subsidizing the private party, the private party is subsidizing the political subdivision. Depending on local law, these PILOTs may be used for debt service on bonds issued for a wide variety of purposes.

In each of these three forms, the amount of the PILOTs is usually negotiated directly between the taxing authority or taxing authorities[4] and the private party. In some cases,

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[4] In situations where State and local taxation is structured to provide for taxation by multiple authorities (*e.g.*, a county, a municipal corporation, and a school district each imposing *ad valorem* property taxes at its own millage rate), a separate PILOT agreement may be executed with each separate governmental entity.

State or local laws impose constraints on the amount that can be negotiated. For example, in some jurisdictions, PILOTs must be in an amount that is not less than the taxes that would otherwise be payable by the private party to support the local school system. Generally, however, local taxing authorities have discretion to determine the amount and term of PILOTs. In addition, NABL is aware of payments characterized by nonprofit payors as PILOTs that relate to usage, (*e.g.*, "per 911 call" charges) or percentage of income (*e.g.*, multifamily housing projects); many of these arrangements provide for PILOTs with respect to some taxing districts and not others (*e.g.,* retirement communities not paying PILOTs for school districts). Even for those payments that are characterized as property taxes, it is often very difficult to estimate with any degree of accuracy the valuation of the property owned by a nonprofit entity. (*See* Exhibit C for descriptions of various State PILOTs.)

IV. Comments with Respect to the Proposed Regulations

A. Substance of the Proposed Regulations

The Proposed Regulations provide a definition of the meaning of "commensurate with" under Treas. Reg. §1.141-4(e)(5). This proposed definition of "commensurate with" contains the following requirements: (i) that the PILOTs be a fixed percentage of or reflect a fixed adjustment to the otherwise applicable tax of general application; (ii) that the PILOTs be subject to no more than a single change in the level of percentage or adjustment; (iii) that the PILOTs be based on the current assessed value of the property for property-tax purposes for each year paid (and, in doing so, precludes sales-tax PILOTs); (iv) that the assessed value of the PILOTs be determined in the same manner and with the same frequency as occurs with other property subject to this generally applicable tax; and (v) that the PILOTs not be based in any way on debt service on a bond issue or otherwise be set at a fixed dollar amount that cannot vary with the assessed value of the property.

B. General Comments

Given that structures with similar economic consequences should generally be treated consistently and that differing forms of PILOTs should be taken into account, NABL recommends that the IRS adopt rules relating to PILOTs that are more flexible than those under

the Proposed Regulations. In particular, if a State or local government chooses to assess PILOTs equal to 100% of taxes, 0% of taxes, or anything in between, the federal tax law should not discriminate. Under State or local law, PILOTs often are intended to be used as an additional technique for promoting economic development and may permit greater flexibility than that allowed with tax abatements and grants. This fact should have no impact on whether PILOTs are treated in the same manner as are generally applicable taxes.

NABL believes that a central premise of the PILOT Regulation should be that economically equivalent financing structures be treated identically for purposes of tax-exempt bond financing. If a project may be financed on a tax-exempt basis through bonds supported by partially abated incremental taxes (or by incremental taxes notwithstanding continuing grants back to the taxpayer by the taxing jurisdiction), then that project should also be eligible for financing on a tax-exempt basis through bonds supported by payments in lieu of, but equal to, such partially abated incremental taxes.[5] That Treas. Reg. §1.141-4(e)(5) accomplishes this result of equivalency has been made clear in the Stadium Rulings, although NABL agrees with the treatment in the Proposed Regulations that this equivalency should be clarified by the deletion of the last sentence in Treas. Reg. §1.141-4(e)(5). Moreover, NABL recommends that this equivalency be preserved in any other revisions to the PILOT Regulation, as political subdivisions should be able to choose whether and how much to tax their constituents without running afoul of the PILOT Regulation. If flexible rules exist to provide grants and abatements with respect to taxes of general application (*see* Treas. Reg. §1.141-4(e)(4)), similar flexible rules should exist for PILOTs.

C. Specific Comments

As previously stated, in certain States, PILOTs may be implemented only by a governmental unit, often a conduit bond issuer (*e.g.*, an industrial development authority), by taking title to the property that is the subject of the PILOTs, and leasing the property back to the private user. Pursuant to the lease, or in a separate agreement with one or more taxing authorities, the private user agrees to make PILOTs as part of its rent or to make PILOTs to the

[5] *See* Rev. Rul. 71-49, 1971-1 C.B. 103, where tax equivalency payments made to the New York City Educational Construction Fund were treated as taxes for purposes of determining whether such amounts were deductible.

relevant taxing authorities. Because the legal title to the property is vested in a governmental unit, the property is exempt from property taxation, and the PILOTs are usually negotiated amounts that are lower than the property taxes that would otherwise have been payable. If the PILOTs are payable to a taxing authority, they are typically (although not always) paid to the taxing authorities that otherwise would have received taxes with respect to the property, even though those taxing authorities may not be party to the acquisition/lease-back or revenue bond structure that permits the PILOTs.

1. Designation of Public Purpose. Certain provisions of the Proposed Regulations, including certain carryover provisions from the PILOT Regulation, are difficult to apply in the context of the PILOTs described above. For example, both the Proposed Regulations and the PILOT Regulation provide that any permissible PILOTs must be "designated" for a public purpose. No guidance is provided with respect to what entity is required to make such a designation or how such designation is to be made. Many PILOTs are paid directly to the applicable taxing authorities pursuant to acquisition/lease-back or revenue bond structures to which the taxing authorities may not even be parties. The degree of involvement of the various taxing authorities in the structure and approval of PILOT agreements varies from State to State and locality to locality. Therefore, each relevant taxing authority may not have the opportunity in the applicable documents to designate that the PILOTs would be applied to a specific public purpose. From a local-government procedural standpoint, an additional complication arises when multiple taxing authorities are involved, depending on the structure of State and local taxation in the relevant area. The governmental unit that serves as lessor under the acquisition/lease-back structure establishing entitlement to the PILOTs can designate that the PILOTs be used for a public purpose; but because such governmental unit is frequently not the actual recipient of all or a portion of the PILOTs, such a designation may not be meaningful. NABL recommends that this language be clarified to provide that any PILOTs must be *applied* for a public purpose and not *designated* for a public purpose, or that an agreement between or among governmental units satisfies this requirement.

In this regard, NABL observes that, with perhaps the notable exception of PILOTs structured in contemplation of a particular bond issue (*e.g.*, the Stadium Rulings), most governmental units that receive payments under PILOT agreements treat the revenues received

under these agreements as tax revenues, not separating them on financial statements nor depositing them into separate accounts. NABL does not believe further designation is required if the PILOT revenues are commingled with other tax revenues, as such commingled monies are inherently applied for public purposes. Further, in other situations (*e.g.,* the treatment of commingled investment earnings on bond proceeds under Treas. Reg. §1.148-6(d)(6)), deference has been given to the widespread practice of commingling funds from multiple sources by States and local governments. Therefore, NABL recommends that commingling of such PILOTs by a State or local government with substantial tax and other revenues effectively indicates that the PILOTs are being treated by that governmental unit as general governmental revenues and, thus, applied for a public purpose. In addition, to accommodate State and local governmental structures where multiple PILOTs are commingled and used in substitution for incremental taxes in the context of infrastructure financings described above, NABL recommends that these commingled PILOTs be treated as applied for a public purpose. Possible language for this provision is as follows:

> A PILOT is treated as applied for a public purpose when it is deposited into a commingled fund with substantial tax or other revenues from governmental operations (treating for these purposes other PILOTs deposited into the fund as tax revenues) of the issuer.

NABL believes that such deference to State and local treatment of PILOTs is appropriate.

2. Special Charges. Because of potential confusion as to the meaning of the last sentence of Treas. Reg. §1.141-4(e)(5)(ii), which provides that PILOTs paid in consideration for the use of property financed with tax-exempt bonds are treated as special charges, the Proposed Regulations would delete such last sentence. While NABL supports the deletion of the last sentence because its scope of application is unclear, the PILOT Regulation will still restrict special charges, and the application of such restriction will remain unclear with respect to PILOTs. Specifically, Treas. Reg. §1.141-4(e)(3) will continue to provide that "a payment in lieu of tax that is limited to the property or persons benefited by an improvement is not a generally applicable tax." As discussed above, many PILOTs are structured in connection with acquisition/lease-backs for property and, as a result, are payments for what is arguably the special privilege of occupying the property. In addition, when a political subdivision develops

an incentive package to attract business to a community, that package will often include a commitment to extend roads and/or public utilities to the site at which the business will be located. These improvements may be financed by an issue of tax-exempt bonds, whether tax increment, special assessment, or general obligation bonds. As a result, the business will "benefit" from an improvement. Treas. Reg. §1.141-4(e)(3) is currently unclear and difficult to apply with respect to PILOTs. If Treas. Reg. §1.141-4(e)(3) is read broadly, a majority of PILOT arrangements (which arguably involve some sort of benefit to the payor) may be considered to involve "special charges." Consequently, to ensure that a relevant PILOTs exception is available to State and local governmental units and to simplify and clarify the PILOT Regulation, NABL recommends that Treas. Reg. §1.141-4(e)(3) provide that a PILOT arrangement will not be considered a special charge merely because the payor under the arrangement benefits or uses an improvement, provided that the PILOTs are commensurate with and not greater than the amounts imposed by a statute for a tax of general application. Payors of taxes of general application may benefit from an improvement and such benefit does not transform such a tax into a private payment. (*See*, *e.g.*, PLR 8945032.) PILOTs should be treated similarly.

3. "Commensurate" Requirements. The Proposed Regulations expand the requirement that a payment be commensurate with generally applicable taxes in Treas. Reg. §1.141-4(e)(5) by providing a "standard" that would prohibit many PILOT arrangements that are designed for legitimate reasons and are unrelated to the avoidance of the private payment limitations of the Code.

i. Fixed Percentage. NABL notes that not all property taxes are computed as a simple percentage of assessed or market value of the subject property, as, for example, where State and local governments include various factors in their calculations such as homestead exemptions, discounts for senior citizens, or credit provisions relating to taxation of "brownfields."[6] Not only may a business or project owner negotiate (and/or be assessed) different PILOTs for its property, depending on State or local law, greater or less specificity regarding the parameters for determining PILOTs may be present. And while such PILOTs may

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6 *See, e.g.*, the description of Minnesota PILOT arrangements, discussed in Exhibit C.

thus not be uniform as contemplated by the proposed commensurate standard, NABL recommends that PILOTs not be treated as "special charges" if the PILOTs will never exceed the taxes otherwise payable because the PILOT arrangement, in such instance, is economically equivalent to the payor paying taxes of general application and perhaps receiving a subsidy from the applicable State or local governmental unit. A subsidy by a State or local governmental unit generally will not transform taxes of general application into private payments and will not entail special restrictions on providing the level of subsidy. (*See* Treas. Reg. §1.141-4(e).) PILOTs should be treated in a similar manner.

ii. Changes to Payments. The Proposed Regulations would allow only a single change in the fixed percentage of taxes that are payable as PILOTs. This restriction is problematic because many incentive packages of political subdivisions provide for a phase-in of taxes through a PILOT agreement, so that the user of a facility may pay no PILOTs or minimal PILOTs during the start-up period of a project followed by an increased percentage each year until the PILOTs reach an amount equal to the taxes that would otherwise have been payable with respect to the property.[7] NABL recommends that all such PILOT arrangements be permitted as they are motivated by legitimate economic development reasons. No apparent abuse arises if more than one change to the PILOTs is allowed throughout the time applicable, as long as the PILOTs are less than the otherwise applicable tax payment. As previously stated, provision of the subsidy for PILOT arrangements should be as flexible as that permitted for taxes of general application.

iii. Not Tied to Debt Service. Many PILOT agreements created pursuant to State statute are designed to establish PILOTs at fixed, unchanging amounts that *include* debt service, other costs of maintaining the bond-financed property, and an amount that will end up in the taxing authority's coffers for other governmental purposes. The inclusion of debt service on bonds (whether taxable or tax-exempt) may not be the impetus behind the sizing of the amount of the PILOTs but, as noted above, a financing may be a factor in determining the overall effect of the incentive package offered to the beneficiary. This circumstance is no different from governmental use of general tax revenues to pay debt service on an issue that

[7] *See, e.g.*, the Arkansas phased-in approach, discussed in Exhibit C. Similarly, in South Carolina, legislators have provided for five-year PILOT reset periods (*see* Exhibit C).

benefits a private user. In view of the complex and integrated nature of economic development arrangements, the requirement in the Proposed Regulations that a payment not be based on debt service introduces risk into any transaction that, where a private user of proceeds is making PILOTs, the IRS could assert that this requirement is not satisfied. NABL recommends that this restriction be deleted, as a more workable and realistic approach is to ensure that PILOTs are not in *excess* of generally applicable taxes that would be paid. Thus, any adjustment to the rate or amount of the PILOTs or valuation of property that produces PILOTs *less than or equal to* the tax that would otherwise be paid should be permitted.

4. No "Private Loan" Created. Similar to Treas. Reg. §1.141-5(d)(3) that treats tax payments in connection with a tax-increment financing as not resulting in a private loan, NABL recommends that the final regulations make clear that any PILOTs that satisfy the PILOT Regulation will not be considered to result in a private loan.

5. Cancellation of Tax. Based on certain statements made by the IRS in the Stadium Rulings, NABL recommends an additional clarification of the PILOT Regulation. In those rulings, the IRS stated that the projects were not automatically exempt from taxation, and that the issuer of the bonds and owner of the project had to take action to cancel the taxes and enter into the PILOT agreement in order to effectuate the transaction. NABL notes that this approach is unusual and that a far more common approach is for a property to become exempt from tax immediately upon the property becoming governmentally owned. The PILOT agreement is then entered into to replace all or a portion of the tax cancelled. NABL sees no reason why this element of local law that was present in the Stadium Rulings is relevant to the analysis of PILOTs and recommends that the final regulations clarify that this factor is not necessary for the PILOT Regulation to apply.

6. Effective Date. Finally, the Proposed Regulations apply to bonds sold after February 19, 2007. Not only do the Proposed Regulations impose a retroactive effective date, but this effective date applies prior to the finalization of these regulations. For a number of years, the IRS has avoided issuing proposed regulations with a retroactive effective date. NABL supports the issuance of proposed rules that become effective only after an opportunity for public comment and the issuance of final regulations. While NABL understands that rare cases exist in

which rules need to be made effective immediately, NABL does not believe that this is one of those instances. NABL recommends that the IRS announce a revised effective date for some period after finalization.

In addition, NABL believes that in selecting an effective date, the IRS should consider the importance of avoiding disruption of State and local governmental economic development programs and related financings. Thus, if the IRS retains the effective date in the Proposed Regulations, NABL recommends that PILOTs, which are commingled with other revenues (as described above) be retroactively treated as generally applicable taxes regardless of whether the other requirements of any final regulations are satisfied. NABL believes that where payments have been so treated, they have, *ipso facto*, not been used as security for specific transactions in a way that circumvents the intent of the PILOT Regulation; this provision would effectively preserve the *status quo* in countless State and local governmental financings.

Also, consideration should be given to the timing of execution of PILOT agreements vis-à-vis related financings. NABL recommends that effective date provisions be structured to permit, after the effective date, refundings of bonds issued prior to the effective date, if no extension of the weighted average maturity of the bonds occurs. This recommended provision would permit governments that might have outstanding bonds caught by the change in law to nevertheless realize savings as a result of a refunding transaction.

Finally, depending on the date of promulgation of the final regulations and effective date, consideration should be given to permitting issuers to use existing PILOTs done in anticipation of a financing as intended. NABL recommends that States and local governments be granted some period of time to use PILOT agreements entered into prior to the promulgation of the final regulations and to adapt their economic development programs to any change in law.

EXHIBIT A

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EXHIBIT B

Example. The following example illustrates that certain State law structures involving bonds supported by *ad valorem* real property taxes (and a subsidy by the issuer) can be economically similar to those involving PILOTs.

Under California law, as under the laws of many other States, the *ad valorem* tax is made applicable to governmentally-owned property that is leased to a nongovernmental person through application of the tax on the "possessory interest" of the lessee. In such jurisdiction, local governmental redevelopment agencies are empowered to capture incremental *ad valorem* tax revenues arising from enhanced property values in redevelopment areas.[1] Tax allocation bonds in California have financed a broad range of redevelopment projects, including shopping centers and other retail improvements, parking facilities, affordable housing, convention centers, and recreational areas. While in California many alternative structures would be available for the tax-exempt financing of a municipal facility, such as a convention center, hotel, or other property subject to private business use, one simple structure might include: (i) the creation of a redevelopment agency, the determination by the agency that the proposed site is subject to blight and that the proposed facility would contribute to the elimination of the blight, and on that basis, the creation of a redevelopment project area; (ii) the issuance of tax allocation bonds payable out of a portion of the incremental tax revenues in the redevelopment project area, the proceeds of which would be applied to subsidize the capital costs of the facility; (iii) the lease of the facility to the private user; and (iv) the execution by the redevelopment authority of a continuing grant

[1] Often, this process involves the identification of blight and the formation of a redevelopment project area in the affected location. Property values within the boundaries of the project area are then fixed at a "base level" and *ad valorem* property tax revenues attributable to any increases in value above the base level are allocated to the redevelopment agency for a specified period. The incremental tax revenues generated by increases in value above the base level and retained for use by the redevelopment agency often must be used for the costs of economic redevelopment, affordable housing, and related purposes within the relevant project area. All or a portion of the incremental tax revenues may be pledged to secure and be applied to repay the bonds issued by the redevelopment agency ("tax allocation bonds") the proceeds of which are to be used to finance redevelopment agency projects in the redevelopment project area.

contract[2] under which the agency would pay a portion of the incremental tax revenues received by the agency (the possessory interest tax) to be applied to reduce the possessory interest tax burden as an inducement for the private user to participate in the redevelopment project.

The California structure (described above) would produce the same effect as would a negotiated PILOT financing of the same project in a different jurisdiction where the taxing jurisdiction has determined that it is in its interest to subsidize the project by (i) providing to a private user the right to develop the project; (ii) taking action through transfer to a political subdivision or otherwise to remove the property from *ad valorem* tax rolls; (iii) negotiating a long-term PILOT schedule to be made by the private user in exchange for such removal from the rolls; and (iv) making the proceeds of bonds of the political subdivision supported by all or a portion of the PILOTs available for capital costs of the project.

Just as in the case of tax increment financing coupled with grant or abatement, by using PILOTs, the political subdivision is applying its sovereign taxing power indirectly (through the inducement of PILOTs) to subsidize the development of the project and, through the effective partial abatement of the additional taxes that would have been paid on the project. No difference in the treatment of these transactions under the Code is warranted if they are both authorized under State or local law and are economically similar.

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[2] The grant contract might be for the entire period of use of the facility; the net effect of the continuing grant would be a flexible abatement of the incremental tax burden by reason of the possessory interest tax.

EXHIBIT C

The State and local laws establishing PILOTs are extremely broad and varied, and typically delegate substantial authority for the specifics of the PILOT arrangement to a political subdivision benefiting from or incentivizing the relevant project. Specific examples of the law in several States demonstrate the variety and breadth of PILOT arrangements.

States and political subdivisions throughout the country use PILOTs (also referred to as "fees in lieu of taxes" or "service charges in lieu of taxes") as vehicles to encourage a wide variety of governmental purposes, such as economic development, the provision of low- and moderate-income housing, and reimbursement of relevant governmental entities for a portion of the costs of essential public services and infrastructure, otherwise funded by tax revenues. A State statute may authorize political subdivisions to set up PILOT programs but leave the specific details, such as the amount of the PILOTs, to be negotiated by the political subdivision and the private party. The following examples of PILOT programs were obtained via an informal Internet survey or from the experience of the NABL members participating in these comments. **Many of these statutes and arrangements described below would not satisfy the requirements of the Proposed Regulations in one or more respects**.

a. **Arkansas**. Real and personal property financed by revenue bonds and general obligation bonds may be exempt from property taxes during the lease-amortization period in which a political subdivision or industrial development authority retains title to the property. Payments by businesses to political subdivisions in lieu of property taxes are generally encouraged and negotiated between the parties involved. The negotiated PILOTs may not be less than 35% of the property taxes that would have been paid had the property been on the tax rolls. (*See* metrolittlerockalliance.com.) These PILOT agreements are often structured so that the buildings and personal property benefiting from the PILOT agreement are completely brought into the tax rolls over time. Accordingly, the percentage of the assessed value of the buildings increases periodically, often annually, so that in, for example, 15 years, the PILOTs are based on 100% of the property's assessed value; personal property arrangements are structured

similarly but over a shorter amortization period. Finally, as evidence of their economic incentive importance, these agreements often include specific benchmarks in terms of employment, capital investment, etc., at the facility in order to continue entitlement to the PILOT benefits.

b. Colorado. Pursuant to the State constitution, the imposition of a tax, whether property or sales-and-use tax, is subject to a vote of the people. If a governmental unit lowers a tax, it is required to revote the tax if it later wants to raise the tax back to its prior level. The purpose for which the tax revenues may be used is also limited by the State constitution, as well as State and local law. When a governmental unit wishes to finance a purpose for which tax revenues may not be used, it enters into a PILOT agreement with the taxpayer, collects and applies the PILOTs for the desired purpose, and gives the taxpayer a credit against its tax liability for the amount of the PILOTs made. Because the credit is treated as the equivalent of a tax payment, in this way, the alternative purpose may be financed while not requiring the issuer to reduce its tax levy. The governmental unit receiving the PILOTs may be different from the governmental unit giving the credit for the otherwise collectable tax. Colorado law provides for "intergovernmental agreements" between and among local governmental units that may facilitate the transfer of such payments. For example, a redevelopment authority may agree with a city or county to collect PILOTs to be used for redevelopment purposes that the city or county then credits against its generally applicable property or sales-and-use taxes.

c. Maryland. Under Maryland law, PILOTs are payable by lessees of land owned by the federal, State, or local government in cases where the property is used in a private trade or business. The Code contemplates that these funds may be pledged as security for bonds by governmental units as part of incremental tax revenues used for infrastructure financings. This legislation appears to have been structured in response to the needs of Maryland political subdivisions in addressing the relative size and urban locations of federal facilities with the State of Maryland and their increasing privatization under federal initiatives. (*See, e.g.,* Annotated Code of Maryland, Article 41 §14-214.)

Maryland local governments have also negotiated PILOT agreements with nonprofit organizations. (*See, e.g.,* the specific statutory provisions addressing PILOT agreements for senior and/or low-income housing projects in the Housing and Community Development Article

of the Annotated Code of Maryland, §12-104(b), and the Tax-Property Article of the Annotated Code of Maryland, §7-502.)

d. **Massachusetts**. Nonprofit universities are not required to pay property taxes. Some, however, may make annual contributions to help cover the cost of municipal services. Harvard, for example, has entered into an agreement under which it will make annual payments to Cambridge that will increase by 3% each year for the next 20 years. In addition, the base payment to the city will increase by $100,000 every 10 years. MIT has agreed to pay Cambridge $1.5 million, which will increase by 2.5% annually. (*See* Boston Globe, February 15, 2005.)

e. **Michigan.** In order to encourage the development of low-income housing, under the State Housing Development Authority Act (1966 PA 346, as amended, MCL 125.1401 *et seq.*), such housing is exempt from all *ad valorem* property taxes. For example, pursuant to an ordinance introduced by the City of Crystal Falls, the developer would pay an annual service charge for public services in lieu of all *ad valorem* property taxes. The annual service charge is equal to 4% of the difference between the amount of annual shelter rents actually collected on the low-income housing units and the amount paid for utility service for the same period. (*See* crystalfalls.org, ordinance introduced December 11, 2006.)

f. **Minnesota.** Minnesota law provides for payments in lieu of taxes that are time-limited and may be based on factors other than a simple percentage of the amount of tax abated, in connection with permitted real property tax abatements to encourage (i) the development of housing in redevelopment projects and (ii) the attraction or expansion of businesses in "border city development zones." In each case, the tax abatements are limited to projects that would not go forward without the tax subsidy. Minnesota Statutes, section 469.043 permits a partial tax exemption for an approved housing project. The partial exemption may not extend for more than 10 years and may amount to up to 50% of the increase in the "net tax capacity" (*see* below) of the project that occurs from the time of the original acquisition of the property for redevelopment purposes. Development contracts may provide for PILOTs. Minnesota Statutes, section 469.1734 permits partial or complete exemption from property taxes for up to five years in order to encourage job creation in border cities. The authorizing city may require PILOTs based on actual or estimated levels of taxation, which may vary over time to reflect

future expansion plans and other considerations. The city also may authorize a tax credit against property taxes for up to five years, with the amount of the credit based on a percentage of the salaries and wages paid to certain employees of the business.

Under Minnesota law, real property taxes are levied as a percentage of the property's "tax capacity," which is the assessed market value of the property times the applicable "class rate." (*See* Minn. Stat. §273.13, subd. 21(b).) Neither market values nor class rates are uniform for all property of a given type. Section 273.11 limits the percentage by which the assessed value of a property of various types may increase in any year. Class rates differ between types of real property (generally based on how the property is used), and, within a class of property, the class rate may be greater for property value in excess of a stated threshold. (*See* Minn. Stat. §273.13, subd. 22.)

In addition, counties are authorized under Minnesota Statutes, §272.028 to negotiate an exemption from the normal tax on wind energy production, provided that negotiated PILOTs exist in order to provide fees or compensation to the city or town and the county in which a facility is located to maintain public infrastructure and services. The payment in lieu of the wind energy production tax may be based on production capacity, historical production, or other factors agreed upon by the parties, and must have duration identical to the period of the tax exemption.

g. New Jersey. To encourage redevelopment projects, long-term tax incentives are provided that exempt the value of the improvements of a property for a period of time negotiated in a tax agreement between the developer and the municipality. The time period can extend for a maximum of 30 years from the issuance of a certificate of occupancy or 35 years from the date that the tax agreement is executed. For example, the Township of Cinnaminson negotiated a PILOT arrangement with a developer to develop a shopping mall. Under that arrangement, the township will receive payments of $491,500 annually for the first decade and eventually $941,000 annually in the later stages of the 25-year agreement. (*See* PhillyBurbs.com, December 26, 2006.)

Additionally, the Long Term Tax Exemption Law (P.L. 92, c.431) provides a formula for negotiating the service charge of a redevelopment project. Other than projects providing housing

for income-restricted households, the service charge can be negotiated as a floor of either 2% of total project costs or 15% of gross annual revenues. For income-restricted housing projects, the floor becomes a ceiling and the service charge can be negotiated down to zero.

h. New York. The State of New York has a plethora of statutes authorizing PILOT agreements for both charitable exemption and lending of public credit–economic development purposes. Unlike many States that have a general statute authorizing the creation of issuers for economic development purposes with uniform provisions, New York's practice has been to create separate Industrial Development Agencies for its cities and counties pursuant to separate pieces of legislation, which are not uniform in their provisions. In addition, the Legislature has authorized the issuance of bonds by, among others, the Urban Development Corporation, the New York Job Development Agency, the Dormitory Authority, the Empire State Development Corporation, the Brooklyn Bridge Park Development Corporation, and many Local Development Corporations, including the New York Liberty Development Corporation. Many of these entities utilize the leasing mechanism when they are conduit issuers, and all are authorized to enter into PILOT agreements when providing real estate tax exemptions (but may vary in how the PILOTs are to be used). Indeed, each issuer is required to have a Uniform Tax Exemption Policy governing the exemption from real estate taxes for each of its projects and the PILOT agreements that may be entered into for each of its projects.

While each of these statutes may provide for an exemption from real property taxes (as well as mortgage recording, sales, and use taxes), and each may authorize the use of PILOT agreements, none of them provides a uniform policy regarding how the payments to be made under a given PILOT agreement will be computed. Each arrangement is separately negotiated. While the Urban Development Corporation Act provides for a minimum amount of PILOTs that must be made for nonresidential projects, the usual payment is solely the result of give-and-take negotiations between the governmental issuer and the private developer. As a result, a multitude of variations in the computation of PILOTs exists.

One common method has been to provide for a fixed annual payment for the period of the agreement, a method favored by developers because of its certainty. Occasionally, this fixed-dollar amount is modified by limiting the fixed amount to the real estate taxes on the land and

using another method for the improvements thereon. Frequently, a method is used that results in a non-fixed total payment but with partially fixed provisions. For example, the annual payment may be equal to the actual real estate tax, minus a fixed-dollar amount. A variation on this method stabilizes the real estate taxes by applying the annual rate but fixes the appraised valuation of the land to the value prior to the improvements, which are not taken into account or may be phased in over time.

Other PILOTs employ totally formulaic computation methods. For example, PILOTs may be based on actual real estate taxes minus credits for employees hired, sales taxes generated, or commercial rental taxes imposed on the tenants. Another technique is to provide credits against the actual real estate taxes by the value of the improvements, which will become taxable upon the expiration of the PILOT agreement. Frequently the agreement will phase in the actual real estate taxes on the improvements or on the entire assessed value in annual increments (*e.g.,* 10% per year).

The discussion below of PILOTs entered into for charitable exemption purposes under the laws of Pennsylvania applies to the laws of New York as well, except that the vague restrictions on the use of proceeds from such PILOT agreements that apply in Pennsylvania do not apply in New York.

i. Pennsylvania. Some years ago, Pennsylvania changed its laws to permit the direct lending of the proceeds of exempt facility and small issue bonds to private borrowers. Issuers of such private activity bonds do not have to acquire the bond-financed property and lease it to the ultimate borrower in order to make the bond proceeds available to that borrower. Therefore, there is no need for the lending of public credit PILOT agreements. Pennsylvania does exempt, however, institutions of purely public charity from local real estate taxes. As a result, the need remains for charitable exemption PILOT agreements.

Pennsylvania's Act 1997-55 authorizes PILOT agreements for charitable exemption purposes. State law encourages, but does not require, voluntary agreements "or payments-in-lieu of taxes." In enacting the statute, the General Assembly noted that institutions of purely public charity benefit substantially from local governmental services. The General Assembly found that, while these institutions have significant value to the Commonwealth and its citizens, the

need exists for revenues to maintain local government services provided for the benefit of all citizens, including institutions of purely public charity. The Act then provides that—

> A political subdivision may execute a voluntary agreement with an institution that owns real property within the political subdivision. All contributions received from such voluntary agreements shall be used to help ensure that essential governmental, public or community services will continue to be provided in a manner that will permit an institution to continue to fulfill its charitable mission.

This statute is permissive, not mandatory. The statue does not specify how the PILOTs are to be computed and does not provide how the payments must be used, except in the broadest terms, by the recipient political subdivision. The statute encourages such agreements only by taking the payments into account in its determination of whether an institution is a purely public charity and thus is exempt from local real estate taxes in the first instance. The statute also provides that the Board of an institution that enters into an agreement to make PILOTs will not thereby be in breach of its fiduciary duty towards that institution.

While the payments received by a political subdivision may be used to pay the salaries of police and firefighters, they are not restricted to such use. These broadly worded provisions permit use of the PILOT agreement proceeds to support debt service on bonds used for a multitude of purposes. For example, a PILOT agreement may be entered into by a 501(c)(3) hospital as part of an agreement with a City for the closing of a money-losing public hospital. The City may agree to use the PILOTs it receives from the 501(c)(3) hospital to pay the debt service on bonds used for building an emergency room at that hospital to provide medical care for its police and firefighters, and for the indigent, who were formerly treated by the closed public facility. The amount of the PILOTs need not be determined by any formula and may be keyed only to the debt service on the bonds.

Pennsylvania also has several statutes that authorize PILOT agreements between the Commonwealth and its local political subdivisions. Under these agreements, the Commonwealth may provide PILOTs for the lands it acquires by eminent domain for public parks, bridges, dams, etc. These PILOT agreements do not involve bond issues. One other PILOT provision, however, exists in The Municipality Authorities Act that may involve bonds for the benefit of a

nongovernmental user. That Act exempts such authorities from taxes or assessments on property acquired or used by them for the increase of commerce and prosperity and for the improvement of health and living conditions. When such authorities act as conduit issuers for nongovernmental borrowers, they do not acquire land. When they act as water utilities, however, they frequently acquire land. PILOT agreements are authorized when, in certain counties, more than 10% of the land area in a political subdivision is acquired by an authority for waterworks and the political subdivision is not provided with water service by the authority. Section 5620 of the Act provides that—

> in lieu of such taxes or special assessments the authority may agree to make payments in the county to the taxing authorities of any or all of the political subdivisions where any land has been taken. The bonds issued by any authority, their transfer and the income from the bonds, including any profits made on their sale, shall be free from taxation within the Commonwealth.

The nongovernmental usage and bond issuance occurs when the Authority in question is managed by a for-profit water company under a contract that does not satisfy Rev. Proc. 97-13. For example, that authority may issue bonds to pay for the erection of public recreational facilities at a large reservoir in a political subdivision to which the authority does not provide water services. The authority and the political subdivision may enter into a PILOT agreement whereby the PILOTs will be used by the political subdivision to pay debt service on the recreation bonds. Again, the statute is permissive, not mandatory. The statute authorizes an authority to make voluntary PILOTs, and does not specify how the PILOTs are to be computed or how they may be used by the recipient political subdivision.

j. **South Carolina.** South Carolina provides for a fee-in-lieu-of tax ("FILOT") under S.C. Code Ann. Section 4-12-30 *et seq*, S.C. Code Ann. Section 4-29-67, and S.C. Code Ann. Sections 12-44-10 *et seq*, pursuant to which a company may negotiate to pay a fee instead of paying property taxes. The real property tax is generally the value of the property multiplied by an assessment ratio set by State law multiplied by the millage rate for taxes set by local government. A company and a county can agree to reduce the assessment ratio, to freeze the millage rate applicable to the property to a set millage rate, or adjust the millage rate every five

years for the period that the FILOT is in effect. In fact, these FILOTs are often used as the source of repayment of special source revenue bonds issued to finance the costs of multi-county economic development parks. (*See* "*South Carolina Economic Development Incentives,*" Erik P. Doerring, Esq., McNair Law Firm, P.A.)

k. South Dakota. State law creates a housing and redevelopment commission in each county and municipality for the purpose of providing various housing projects. The property of each commission is exempt from all taxes and special assessments. State law (SDCL 11-7-73) also provides for PILOTs equal to 10% of the aggregate shelter rentals of the housing project, unless a greater amount is permitted pursuant to federal legislation and is agreed upon by the commission and the municipality, but may not exceed the amount that would be payable in taxes on the project if it were not exempt from taxation.

l. Tennessee. Tennessee law provides three statutes pursuant to which three types of conduit issuers are permitted to negotiate PILOTs: industrial development boards; health, educational, and housing boards; and housing authorities. Ninety-six counties and over 100 municipalities exist in Tennessee, and most of them have industrial development boards, each of which may formulate its own policies and formulas for PILOTs. The statutes provide these conduit issuers with flexibility to negotiate PILOTs in a manner that allows them to accomplish their goal of attracting and retaining businesses and furthering the governmental purposes of the conduit issuers of improving the health and housing of their citizens. Many of the local PILOT programs permit the PILOTs to be fixed at the amount that was paid in taxes on the property used prior to improvement.

m. Federal PILT (Payment in Lieu of Taxes) Program. The Interior Department collects revenues of $3 billion to $4 billion annually from commercial activities on federal lands, such as oil and gas leasing, livestock grazing, and timber harvesting. A portion of these revenues is shared with States and counties in the form of revenue sharing payments, with the balance deposited in the U.S. Treasury. In 2006, $232.1 million was distributed to approximately 1,850 local governments with jurisdictions containing tax-exempt federal lands. The annual PILTs to local governments are computed based on the number of acres of federal entitlement land within each county or jurisdiction, with a cap based on population. By statute, the per-acre and

population variables used in the formula to compute payment amounts are subject to annual inflationary adjustments using the Consumer Price Index. (*See* Press Release by U.S. Department of the Interior, June 15, 2006, www.doi.gov.)

n. Senior Living Communities. In a report prepared by Ziegler Capital Markets Group dated February 2006, 60 corporate finance officers of senior living communities from various States around the country (*e.g.,* Illinois, Massachusetts, Michigan, Minnesota, New York, Ohio, Pennsylvania, and Wisconsin) responded to an inquiry regarding their experience in negotiating PILOT agreements. In many instances, the negotiations were based on reductions in taxes related to services not used. Some involved modest increases for an initial period, with higher annual increases in later years. Others provided for the lesser of the assessed tax or a fixed-dollar amount. As stated by one respondent, "each deal has a story;" it is clear, however, that each PILOT agreement is negotiated based on the particular needs of the senior living community and its particular circumstances.