

MEMORANDUM

February 25, 2009



TO: Selkirk Yards Industrial District Focus Group Meeting Participants
FROM: Justin S. Miller, Esq. (jmiller@harrisbeach.com 518.701.2710)
RE: SYID Focus Group Meeting #2 - 02/25/2009
Implementation Methods for Study Recommendations
Outline of IDA, LDC and MDA Entities as Economic Development Tools
CC: Town of Bethlehem Industrial Development Agency

Please accept this memorandum as a brief outline and discussion of the purposes and powers of Industrial Development Agencies (“IDAs”), Local Development Corporations (“LDCs”) and Municipal Distribution Agencies (“MDAs”) and how they may be used as economic development tools in New York State. The following summaries are provided in the context of ongoing discussions by the Town of Bethlehem (the “Town”), the Town of Bethlehem Industrial Development Agency (the “Agency”) and the Selkirk Yards Industrial District Focus Group regarding economic development strategies to develop the “Selkirk Yards Industrial District” (the “District”).

I. IDA’s – Generally.

Generally, industrial development agencies (“IDAs”, including the Agency) are formed under Article 18-A of the New York State General Municipal Law (the “GML”), as amended (the “Act”), as public benefit corporations. IDAs are empowered to provide financial assistance to private entities through tax incentives in order to promote the economic welfare, prosperity and recreational opportunities for residents of a municipality (the “Benefited Municipality”). An IDA’s ability to provide financial assistance for any particular project is limited to the powers contained within the Act. The current provisions of the Act allow IDA’s to provide four basic forms of financial assistance that include: (i) a mortgage recording tax exemption; (ii) a sales and use tax exemption; (iii) real property tax abatement; and (iv) interest rate savings via tax exempt financing.

IDA’s are empowered to sponsor industrial and manufacturing projects like those present and proposed within the District. In addition, and as noted above, IDA’s, as public benefit corporations, can act in quasi-governmental capacities that include the ability to access public funding sources like New York’s Industrial Access program (“IAP”) and the Multi-Modal Program. The structure of an IDA-assisted transaction most often takes the form of a lease-leaseback transaction whereby the Agency appoints a company its agent to undertake a project, leases an entire project from the sponsoring company, and then leases all rights, save for certain unassigned rights, in the project back to the sponsoring company to act as beneficial owner and operator. The IDA’s retained interest is minimal and intended exclusively to empower the IDA to confer financial assistance upon the Company and to retain non-recourse status.

As noted above, IDA’s also serve as “qualified issuers” of TEB’s and can confer significant interest rate savings for qualified manufacturing projects. Further, IDA’s are empowered to leverage payments made under a payment-in-lieu-of-tax agreement (“PILOT

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Agreement”) through a mechanism called PILOT Increment Financing (“PIF”). PIF provides a unique revenue stream that can be incorporated within standard IDA straight-lease and bond finance transactions. With the consent of affected tax jurisdictions, an IDA and Company may negotiate a payment in lieu of tax equal to full taxes and allow the increment (difference between full taxes and otherwise negotiated amount) to be used to repay debt service related to certain infrastructure improvements. Elements of PIF have been incorporated into IDA PILOT’s associated with industrial parks and other economic development projects as means by which to finance public infrastructure and improvements, including roadway, water, sewer, utility and environmental remediation purposes.

Most often, PIF is utilized where a company qualifies for a 100% refund of real property taxes through the New York State Empire Zone Program. PIF can also be utilized without the benefit of the Empire Zone Program as long as an IDA has the support of at least one of the local tax jurisdictions. Pursuant to Section 858(15) of the IDA Act, unless otherwise agreed by the “affected tax jurisdictions” (as such term is defined within Section 854(16) of the IDA Act), all PILOT agreements must provide that PILOT payments be allocated among affected tax jurisdictions in proportion to the amount of real property tax and other taxes which would have been received by each affected tax jurisdiction had the project not been tax exempt due to the status of the IDA involved in the project.

II. LDC’s – Generally.

Economic development projects in New York often involve a local development corporation (“LDC”). In fact, use of LDCs pre-dates the existence of IDAs, and is often the vehicle through which local economic development is conducted. LDCs are formed and empowered to conduct certain projects pursuant to Not-For-Profit Corporation Law § 1411.

LDCs are predominately formed by, and work closely with, municipalities and IDAs by providing not only greater transactional flexibility for undertaking economic development projects, but also added liability protection because the LDC is a bankruptcy remote entity.

Distinguished from IDAs (which exist as public benefit corporations), LDCs are established as charitable corporations that are empowered to construct, acquire, rehabilitate and improve for use by others, industrial or manufacturing plants in the territory in which its operations are principally to be conducted (“Benefited Territory”). LDCs can provide financial assistance for the construction, acquisition, rehabilitation, improvement, and maintenance of facilities for others in its Benefited Territory. Specific LDC powers include the ability to: (i) disseminate information and furnish advice, technical assistance and liaison services to federal, State and local authorities; (ii) to acquire by purchase, lease, gift, bequest, devise or otherwise, real or personal property; and (iii) to borrow money and to issue negotiable bonds, notes and other obligations. LDCs are also uniquely empowered not-for-profit corporations because without leave of a court, LDCs are empowered to sell, lease, mortgage or otherwise dispose of or encumber facilities or any real or personal property or any interest therein upon such terms as they may determine.

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Of particular import is the LDC's ability to directly acquire real property from municipalities without the need for public bidding or full market value consideration. (See N-PCL § 1411(d).) Notwithstanding the liability protections that may be afforded by building a bankruptcy-remote entity into a development project, the LDC's ability to acquire realty is a unique asset. More often than not, economic development efforts are significantly hindered by traditional constraints on municipally-owned realty. This special power granted to municipalities for the disposition of realty has become a crucial element in sophisticated economic development projects undertaken in recent years.

LDCs also offer great latitude to development professionals because they do not require special legislation to be created. However, great care must be employed when LDCs are formed because their structure and membership will dictate how the entity must undertake day-to-day business operations. Because these entities are quasi-governmental in nature and exist specifically to lessen the burdens of government, the make-up of an LDC's membership and board of directors can subject it to New York's open government laws, including the Public Authorities Accountability Act ("PAAA"), the Open Meetings Law and FOIL.

LDCs can provide financial assistance packages to developers similar to those provided by IDAs, except that LDCs are not specifically exempted from real property taxes (see RPTL § 420-a), and therefore cannot provide a real property tax exemption to for-profit beneficial owners. Hence, the IDA PILOT structure cannot be employed by an LDC without involvement of the IDA. Despite this, LDCs can provide significant project savings through mortgage recording tax exemptions (see Adv Op Comm T&F, TSB-A-95(16)R and TSB-A-97(7)R) and sales and use tax exemptions. (See Tax Law § 1116(a)(4).)

Generally, LDCs may provide financial assistance in the form of exemptions from mortgage recording taxes and/or sales and use taxes. N-PCL § 1411(f) states that "the income and operations of corporations incorporated or re-incorporated under this section shall be exempt from taxation." Based on § 1411(f), the commissioner of the Tax Department (the "Commissioner") has indicated in several advisory opinions that the involvement of an LDC in the construction and/or finance aspects of a qualifying project may allow for an exemption from sales and use taxes and/or mortgage recording taxes. (See TSB-A-93(13)-R, TSB-A-95(16)-R, TSB-A-97(7)-R, and TSB-A-97(54)-S.) However, it should be noted that the facts and circumstances set forth within each of these advisory opinions are unique and that the use of an LDC should be carefully structured to assure that the exemptions sought are proper and obtainable. It is recommended that an advisory opinion be sought for projects of significant size and/or impact.

III. MDA's – Generally.

Often, co-located manufacturing and industrial facilities seek to establish cost saving mechanisms that involve energy production, transmission and, in some cases, sales to other energy consumers. In many cases, these industries work closely with an established MDA in furtherance of the purchase and distribution of electric and/or thermal power generated either on-

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site or at nearby facilities. The following is a summary of the formation requirements for an MDA and how an MDA could assist with the development, generation, transmission and sale of energy to occupants of the District and elsewhere.

The Town, as the Agency's Benefited Municipality and host to the District, is empowered to establish an MDA pursuant to GML Section 360. An "MDA" is a Municipal Distribution Agency, created for the purpose of providing public utility service, which includes "works, structures, poles, lines, wires, conduits, mains, systems, waterpower and any and all other real and personal property" relative to the furnishing of services provided by public utility companies. In order to establish an MDA, the sponsoring municipality would be required to adopt a local law subject to mandatory referendum.

Once established, a municipally-controlled MDA could contract directly with private parties for the purchase of energy produced at the Facility. The sponsoring municipality would be further empowered to finance all or portions of the cost of providing such a service pursuant to the Local Finance Law. A structure for discussion purposes could involve the Town acting as a sponsoring municipality for purposes of establishing an MDA whose board membership matches that of the Agency. This merged structure would allow for the efficient administration of such a plan within the District, including the development, production and distribution of alternative energy produced within the District.

GML Section 360 grants powers to cities, towns, counties or villages to establish, own and operate certain public utility services. Specifically, GML Section 360(2) states that any county, city, town or village may "construct, lease, purchase, own, acquire, use and/or operate" any public utility service within or without its territorial limits, for the purpose of providing for itself or for compensation to its inhabitants, any service similar to that provided by any public utility company as specified in Article 4 of the Public Service Law. Pursuant to GML Section 360(2), a municipal corporation may further purchase gas or electricity from the state, a state agency, another municipal corporation, or from any private or public corporation for such purpose. Therefore, the Town, by and through a newly-established MDA, would be empowered to directly purchase electricity generated by one or more enterprises within the District.

a) Establishing an MDA

In order to establish an MDA, GML Section 360(3) requires the sponsoring municipality, by local law, to propose a method of constructing, leasing, purchasing or acquiring plant facilities for public utility service, together with the maximum and estimated costs of such service, and the method of furnishing such service. This local law must be submitted for the approval of the electors of the sponsoring municipality at the next general election or at a special election called for such purpose, in the matter provided by, and in accordance with the provisions of the Municipal Home Rule Law ("MHRL") relative to the submission of other local laws required to be submitted in a mandatory referendum and in accordance with the procedure

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provided by the election law for general or special elections. The mandatory referendum referenced above must take place before the local legislation may take effect.

A local law subject to mandatory referendum must be submitted for the approval of the electors at a general election held not less than sixty (60) days after the adoption of the local law, unless such local law provides for submission for approval at a special election, or unless, within thirty (30) days after the adoption of such local law, a signed authenticated petition subject to certification by the clerk is filed with the clerk requesting submission at a special election (MHRL Section 23(1)). Notice of the submission of the local law or resolution to the electorate must be published in one or more newspapers published within the sponsoring municipality once in each week for six consecutive weeks immediately preceding the election (GML Section 360(5)).

An MDA formed for the purposes outlined above has the power to construct or acquire by purchase or condemnation “any transmission lines or pipes connecting it with any source or sources of gas, either natural, artificial or mixed or electric power or production and to share with other municipal corporations the cost of transmission lines or pipes” (GML Section 360(6)).

b) Sale of Energy by an MDA.

Whenever a surplus exists over the amount of public utility service required by a municipality and the corresponding residents of such municipality, the municipality may sell the surplus to (i) individual persons; (ii) public or private corporations; or (iii) other municipal corporations. Inter-municipal agreements with any other municipal corporations authorized to exercise these powers, may extend public utility service to such other municipal corporation under contractual terms as may be agreed upon between them, provided that, at the time of the agreement, a public utility service is actually being furnished in such other municipal corporation. However, such agreements are not be effective without the approval of the Public Service Commission (“PSC”).

c) Financing the Cost/Revenue Collection

The sponsoring municipality may finance the cost of public utility service in whole or in part by levying taxes in the same manner as taxes are levied pursuant to law for any permanent improvement. In addition, the utility service may be financed in whole or in part pursuant to the Local Finance Law. The method of operation, the rates, rentals, and/or charges for utility service, and the procedure for revenue collection, may be fixed by the governing board of the sponsoring municipality pursuant to GML Section 360(7). This provision has been interpreted to give implicit authority to municipalities to use various procedures in collecting utility bills, including resorting to the services of a private collection agency. (See Op. State Compt. 79-142)

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In addition, the sponsoring municipality may earn a fair return on the value of the property used in the operation of the public utility service, over and above costs of operations and necessary and proper reserves (See, GML Section 94). Such profits may be used for the payment of expenses or obligations incurred by a municipality for municipal purposes or for the payment of refunds to customers.

d) Construction of Public Utility Service Improvements.

GML Section 363 states that the purchase, acquisition, leasing and construction of a public utility service must be effectuated by the sponsoring municipality in the same manner and by the same officers or boards as other authorized public improvements. However, the Local Law to be adopted may provide a different method or agency for the purchase, acquisition, leasing and construction not inconsistent with New York State law applicable thereto. Funds for the aforementioned uses shall be paid out in a manner prescribed by law for the payment of the expenses of other public improvements authorized for and effected by the MDA. However, this section of the GML does not authorize the implied power to issue bonds in the same manner as other authorities, absent express legislative power enacted by the sponsoring municipality (See *Tierney v. Cohen*, 268 N.Y. 464, 198 N.E. 225 (1935)).

e) Utility Regulation

Sponsoring municipalities are specifically exempted from application to the PSC for a certificate of authority to provide a public utility service under the GML. (See, GML Section 364)