

BRIEF OVERVIEW OF PILOTs AND RABs

“**PILOT**” is an acronym that means “payments in lieu of taxes”. Under the New Jersey *Long Term Tax Exemption Law, N.J.S.A. 40A:20-1 et seq.* (the “**LTTE Law**”) the technical term is “**annual service charge**”.

Basically, the LTTE Law permits a municipality, under specific circumstances required by statute, to enter into a financial agreement with an “urban renewal entity” (“**URE**”), pursuant to which the URE, in lieu of paying real property taxes in respect of the improvements on the subject property, pays an annual service charge, or PILOT. Taxes on the value of the land continue to be paid, but in the typical financial agreement, and as permitted by statute, the URE gets a credit towards the annual service charge for land taxes timely paid in the prior 4 quarters.

From the municipality’s standpoint PILOTs can be very advantageous, even where the amount of the PILOT on its face appears to be substantially less than the amount of otherwise applicable taxes. This is because the municipality gets to retain 95% of the annual service charge. (The other 5% goes to the County in which the property is located.) Typically a municipality retains far less of each tax dollar it collects under generally applicable taxes, sharing the revenues with both the local school district and the county.

Calculation of the amount of a PILOT and of increases in the PILOT over time ordinarily are based on statutory formulas in the LTTE Law, but where redevelopment area bonds are involved can be negotiated.

“**RAB**” means “redevelopment area bonds”, which a municipality can issue, again under specific circumstances required by statute, pursuant to the *Redevelopment Area Bond Financing Law, N.J.S.A. 40A:12A-64 et seq.* (the “**RAB Law**”).

The RAB Law authorizes a municipality, in connection with certain local or State “redevelopment” projects, to issue RABs and to pledge to the repayment of those RABs the annual service charge/PILOT payments due to the municipality under a financial agreement between the municipality and the redeveloper. All or a portion of the PILOTs can be pledged to the amortization of the RAB. As a practical matter, what this means is that RABs can help finance redevelopment projects where traditional funding sources such as equity and conventional debt may not suffice.

Typically, the RAB proceeds are paid over to the redeveloper and applied towards the cost of construction of the project, thereby reducing the amount of construction loan required. The proceeds of the RABs can be used to fund infrastructure improvements, but can also be used to cover project costs as well.

RABs are not necessarily tax-exempt, even though issued by a governmental entity. Tax exempt status will depend upon the use of the proceeds. Infrastructure projects, for example, may qualify as tax-exempt purposes under the applicable provisions of the Internal Revenue Code while RABs issued to subsidize the construction of a private parking structure would likely be deemed taxable.

RABs may include a pledge of municipal credit as security, but such a pledge is not required. While a pledge of municipal credit can serve as a credit enhancement and thus decrease the cost of borrowing, local governments can and do issue RABs on a non-recourse basis.

The financial agreement providing for RABs must be reviewed and approved by the State's Local Finance Board, with input from the New Jersey Economic Development Authority. The approved and executed agreement gets recorded in the property records of the County, and upon such recordation the financial agreement is a lien on the property equal in priority to any other municipal lien, including tax liens, and would take precedence over other liens, including mortgage liens.

At the time of issuance of the RABs the parties will enter into an Indenture of Trust with a corporate trust institution, providing for an irrevocable pledge of the PILOTs received by the Trustee for the payment of debt service and other RAB costs. Once those amounts have been paid the surplus funds can be utilized by the municipality for other municipal purposes.