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New Legislation May Hinder Uses Of Industrial Development Agencies

Costs of Bond Financings Have Significantly Increased

BY PETER L. CURRY

INDUSTRIAL Development Agencies (IDAs) are a primary source of the economic benefits necessary to retain and attract jobs to the cities, counties and towns of New York. IDAs have long been utilized by manufacturing businesses for their ability to issue long-term tax exempt industrial revenue bond financing in amounts up to 100 percent of project development costs, while granting real estate tax, sales tax and mortgage tax abatements to reduce the costs of expansion, modernization and relocation. Not-for-profit agencies have also benefitted from the issuance of tax-exempt civic facility bonds, which have fueled the construction of new hospitals, care facilities, and treatment centers by providing financing at low rates and with long-term amortization.

In the 1990s, the agencies became increasingly flexible in granting benefits to a wider group of "for-profit" and "not-for-profit" companies, including financing housing and equipment purchases. IDAs also entered into significant numbers of "straight lease" transactions, where no bonds were issued, to attract and retain employers in their localities.

The use of IDAs has proved to be wildly popular. In 2001, the IDAs in New York State, together with the New York City Housing Development Corporation, issued $397.6 million in tax-exempt bonds. In 2002, the tax-exempt bonds issued by these agencies totaled $349.8 million. In each of these years, the agencies were also involved in increasing numbers of "straight lease" transactions.

Peter L. Curry *is a partner in the real estate, corporate and banking group at Farrell Fritz.*

IDAs have always faced scrutiny from the State Legislature, local school districts and watchdog groups concerned that the benefits granted to large and small companies and not-for-profits result in actual employment generation and retention, and result in significant economic and social benefit to New York State and local economies. Abatements in school taxes, in particular, have faced increased criticism as federal and state sources of funding have been reduced.

In 2002, the New York State Legislature enacted, and Governor Pataki signed into law, various additional revenue-generating measures to bridge significant budgetary gaps. As a consequence of this new legislation, IDAs face new regulations and challenges that may hinder their roles as engines of job retention and growth.

Costs Increase Significantly

IDA bond financings have always involved expensive closing costs. Purchasers of real property typically pay closing costs for title insurance charges, mortgage taxes, property and casualty insurance fees, bank commitment fees, surveys, architects' and engineers' fees, environmental investigation fees, and attorneys' fees for the purchaser and its lender. Companies entering into taxable or tax-exempt bond transactions pay additional fees to the IDA, the bond underwriter, bond purchaser, and the fees of each of their counsel. These additional expenses aggregate approximately 3 percent of the costs of a project. The recent changes enacted by the New York State Legislature have now significantly increased the costs involved in IDA bond financings.

Amendments to Public Authorities Law §2976 became law on May 29, 2002. This statute, originally enacted in 1989, had imposed a bond issuance charge on bonds issued by the New York State Dormitory Authority and other public benefit corporations. The 2002 amendments added IDAs to the list of the public benefit corporations issuing bonds, note or other obligations that " … shall pay to the state a bond issuance charge upon the issuance of such bonds."

The charge is determined by multiplying the original principal amount of the bond by a percentage, ranging from .14 percent for bonds of $1 million or less, to .70 percent for bonds of more than $20 million. For example, a bond of $10 million would require the payment of a fee of .42 percent, or $42,000. The issuance of a bond of $15 million would result in a payment of .56 percent, or $84,000. A $22 million bond would have an issuance charge of $154,000.

The charge is due to the New York State

Department of Taxation and Finance no later than 15 days after the end of the month in which the issuance of the bonds occurs, accompanied by Tax Form TD-6, Bond Issuance Charge Pursuant to Public Authorities Law §2976. The completed form must indicate the amount of the bonds and the issuance charge to be paid, and is executed by a representative of the IDA.

Notwithstanding the statutory amendments, the New York State Department of the Budget has the authority to waive the payment of this charge. As of this date, the Department of the Budget has issued waivers for transactions involving the issuance of bonds of less than $10 million, if an application is made by the subject agency prior to the issuance of the bonds.

Of course, notwithstanding the plain language of the amendments, this bond issuance charge is clearly to be passed along to the company receiving the agency benefits, and paid at the closing of the bond issuance. Thus, a significant additional expense impacts the decision to undertake IDA bond financing.

Fee for Health Care Projects

The legislative amendments also added an additional provision, §2976-A, entitled Fees in Connection with Certain Health Care Facility Financings. This section imposes a fee in connection with bonds issued for the benefit of health care-related projects requiring the approval of the New York State Commissioner of Health. Such projects are typically hospitals, nursing homes, certain assisted living facilities, diagnostic and treatment centers, and hospices.

If the cost of the construction of the health care facility is to be reimbursed pursuant to Article Twenty Eight of the Public Health Law, subdivision 1 of the section states: " … the Commissioner of Health shall charge a fee of nine tenths of one percent of the original principal amount of the bonds … " In subdivision 2 of the section, the charge is reduced to .50 percent of the bond amount for bonds issued in connection with the refunding of refinancing of existing bonds.

This amendment clearly states that the fee is due from " … the entity which owns or operates the facility to the State Department of Health upon the closing of such bonds or obligations." Thus, hospitals, nursing homes, and other health care-related facilities could pay as much as 1.6 percent of the principal amount of IDA bonds as an issuance fee, in addition to the other closing expenses. Given their not-for-profit role and the community service they perform, this seems to be an odd and counter-productive revenue-generating measure. Also, there is no possible waiver of the §2976-A fee by the Department of the Budget.

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Incredibly enough, the statute then goes on to say, in paragraph 4 of §2976-A, that the fees paid pursuant to the earlier subdivisions " … shall be deemed allowable capital costs in the determination of reimbursement rates established pursuant to Article Twenty Eight of the Public Health Law." Further, these costs would not be subject to any ceiling or penalty established by the Commissioner of Health in order to "cap" the reimbursements that would be made for any such capital project.

The capital costs incurred in construction projects for such facilities are subject to reimbursement as part of the approved Medicaid rate. Thus, the initial outlay of fees paid by the not-for-profit facility to the Department of Health at the bond closing would be repaid to the facility, dollar for dollar, over time, by Medicaid payments given by New York State and the United States.

Other Proposed Changes

State legislators proposed numerous other changes to the IDA structure, as well as to the statutes governing Empire Zones and other economic development tools, in 2002. Most would have resulted in increased oversight over the agencies, and continued the trend of requiring greater reporting of benefits granted and employment and other results achieved. There was even some concern that the portions of the statutes governing the issuance of tax-exempt civic facility bonds for the benefit of not-for-profit agencies would expire and not be extended for an additional three-year period.

In the end, the issuance of civic facility bonds continues for an additional three years, few other proposals passed, and, other than for the implementation of the additional issuance costs, the IDA statutory framework remains essentially the same.

However, school budgetary issues remain. A new report issued by the National Education Association casts doubt on whether the job retention and growth resulting from IDA involvement in the acquisition and development of real estate justifies the loss of real estate taxes payable to school districts in these transactions.

New York State requires other sources of additional revenue. It remains to be seen what new legislative proposals will attempt to further regulate IDAs and the economic benefits they can offer.