DEVELOPMENT AUTHORITIES AND TAX INCENTIVES

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Prepared by

GRAY PANNELL & WOODWARD LLP
Attorneys at Law

The Realty Building
24 Drayton Street, Suite 1000
Savannah, GA 31401
(912) 443-4040

One Buckhead Plaza
3060 Peachtree Road, N.W., Suite 730
Atlanta, GA 30305
(404) 480-8899

gpwlawfirm.com

JONATHAN B. PANNELL
jonpannell@gpwlawfirm.com

JAMES R. WOODWARD
jwoodward@gpwlawfirm.com

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INTRODUCTION

There are numerous types of state and local authorities in Georgia. These materials outline substantive provisions of Georgia law relating to certain types of authorities, in particular general enabling act or statutory development authorities and downtown development authorities, constitutional amendment authorities and authorities created by local act (e.g. public facility authorities). Such authorities provide a valuable tool to cities and counties in connection with financing of certain types of projects for the benefit of such cities and counties. General enabling act or statutory development authorities and certain constitutional amendment authorities may also be used to provide economic incentives (e.g. project tax abatements) to prospective companies in order to induce such companies (and the correlating jobs and capital investment) to move to their jurisdiction.

SECTION I

GENERAL ENABLING ACT OR STATUTORY DEVELOPMENT AUTHORITIES, CONSTITUTIONAL AMENDMENT AUTHORITIES; AND AUTHORITIES CREATED BY LOCAL ACT

1. Introduction

Authorities are separate governmental entities, which provide certain services within the jurisdiction of and for the benefit of a specific governmental unit or units (cities and counties). Under Georgia law, authorities were/are created by (1) general enabling legislation, (2) constitutional amendment, or (3) local act. Authorities have certain powers that cities and counties do not have, making them valuable tools for local governments in connection with bond financings and providing economic incentives to companies to increase employment. There are many types of authorities that may be created under state law (hospital authorities, housing authorizes, jail authorities, etc.), but these materials will focus particularly on development authorities created pursuant to the Development Authorities Law (O.C.G.A. Section 36-62-1 *et seq.*) (the "Development Authorities Law"), downtown development authorities created pursuant to the Downtown Development Authorities Law (O.C.G.A. Section 36-42-1 *et seq.*), constitutional amendment authorities, and local act authorities. Each type of authority has certain enumerated powers and purposes and is authorized by statutory law or case law to assist with certain types of projects. Local government attorneys should review the authorizing legislation of the authorities in their jurisdiction to determine which specific projects such authorities are authorized to undertake.

2. Types of Authorities

a. General Enabling Act or Statutory Development Authorities

Most authorities are authorized to be created pursuant to a general enabling act of the General Assembly and are activated by a resolution of the county commission or city council. These types of authorities are typically referred to as general enabling act or statutory authorities. Two common examples of general enabling act or statutory authorities are development authorities created and activated pursuant to the Development Authorities Law and downtown development authorities created and activated pursuant to the Downtown Development Authorities Law. Each development authority or downtown development authority has the powers (and may be used for the purposes) as described in its respective general enabling act.

Development Authorities (Development Authorities Law)

Pursuant to the power granted to the General Assembly pursuant to GA CONST. Art. IX, Sec. VI, Para. III[1], the Development Authorities Law (O.C.G.A Section 36-62-1 *et seq.*) was enacted by the General Assembly to create in and for each county and city in the state a development authority with the power to accomplish the public purpose of promoting trade, commerce, industry, and employment by facilitating certain economic development projects. A local development authority may be activated by a resolution of the county commission or city council. Joint development authorities may also be created and activated by (1) any two or more municipal corporations; (2) any two or more counties; (3) one or more municipal corporations and one or more counties; or (4) any county in this state and any contiguous county in an adjoining state. Each development authority shall have all of the powers necessary or convenient to carry out and effectuate the purposes and provisions of the Development Authorities Law, including, in particular the power -

> "To borrow money and issue its revenue bonds and bond anticipation notes from time to time and to use the proceeds thereof for the purpose of paying all or part of the cost of any *project*, including the cost of extending, adding to, or improving the *project*, or for the purpose of refunding any such bonds of the authority theretofore issued and to otherwise carry out the purposes of this chapter and to pay all other costs of the authority incident to or necessary and appropriate to such purposes, including the providing of funds to be paid into any fund or funds to secure such bonds and notes, provided that all such bonds and notes shall be issued in accordance with the procedures and subject to the limitations set forth in Code Section 36-62-8."

[1] Ga. Const. Art. IX, Sec. VI, Para. III. "The development of trade, commerce, industry, and employment opportunities being a public purpose vital to the welfare of the people of this state, the General Assembly may create development authorities to promote and further such purposes or may authorize the creation of such an authority by any county or municipality or combination thereof under such uniform terms and conditions as it may deem necessary. The General Assembly may exempt from taxation development authority obligations, properties, activities, or income and may authorize the issuance of revenue bonds by such authorities which shall not constitute an indebtedness of the state within the meaning of Section V of this article."

The term "project" includes, but is not limited to, the following:

- Any one or more buildings or structures to be used in the production, manufacturing, processing, assembling, storing, or handing of agricultural, manufactured, mining, or industrial product or any combination of the foregoing;
- The acquisition, construction, equipping, expansion, modernization of new or existing industrial facilities;
- Air or water pollution control facilities;
- Sewage disposal facilities or solid waste disposal facilities;
- Peak shave facilities;
- Aircraft maintenance facilities;
- Certain sports facilities;
- Convention and trade show facilities;
- Airports, docks, wharves, mass commuting facilities, parking facilities, or storage or training facilities;
- Facilities for the local furnishing of electric energy or gas;
- Facilities for the furnishing of water, if available, on reasonable demand to members of the general public;
- Hotel and motel facilities for lodging in connection with and adjacent to convention, sports, or trade show facilities;
- Amphitheaters with seating capacity exceeding 1,000;
- Acquisition or development of land as the site for an industrial park;
- Acquisition, construction, leasing, or financing of an office building facility and related real and personal property for use by any business enterprise or charitable corporation which will further the development of trade, commerce, industry, or employment opportunities;
- Skilled nursing homes or intermediate care homes;
- Certain community antenna television systems;
- Research and development systems; and
- Other capital projects use for the essential public purpose of the development of trade, commerce, industry and employment opportunities if determined by a majority of the members of the authority that such project or projects and the use thereof would further the public purpose of the Development Authorities Law.

Downtown Development Authorities

Pursuant to the power granted to the General Assembly pursuant to Article IX, Section 6, Paragraph III of the Constitution of the State of Georgia, the Downtown Development Authorities Law (O.C.G.A Section 36-42-1 *et seq*.) was enacted by the General Assembly to create in and for every municipal corporation in the state a downtown development authority for the purpose revitalizing and redeveloping central business districts of such municipal corporations of this state. Downtown development authorities are granted the power to finance projects to develop and promote for the public good and general welfare trade, commerce, industry, and employment

opportunities. A local downtown development authority may be activated by a resolution of the city council. Each downtown development authority shall have all of the powers necessary or convenient to carry out and effectuate the purposes and provisions of the Downtown Development Authorities Law, including, in particular the power -

> "To issue revenue bonds, notes, or other obligations of the authority and use the proceeds thereof for the purpose of paying, or loaning the proceeds thereof to pay, all or any part of the cost of any *project* and otherwise to further or carry out the public purpose of the authority and to pay all costs of the authority incidental to, or necessary and appropriate to, furthering or carrying out such purpose."

The term "project" includes (A) (1) the acquisition, construction installation, modifications or rehabilitation of land, buildings, structures or other improvements located within a downtown development area and the acquisition, installation, modification, renovation, rehabilitation, or furnishing of fixtures, machinery, equipment, furniture or other property in connection therewith, (2) any undertaking authorize pursuant to the City Business Improvement District Act (O.C.G.A. §36-43-1 *et seq.*), (3) any undertaking authorized pursuant to the Redevelopment Powers Law (O.C.G.A. §36-44-1 *et seq.*), or (4) any undertaking authorized pursuant to the Urban Redevelopment Law (O.C.G.A. §36-61-1 *et seq.*) and (B) the provision of financing to property owners for the purpose of installing or modifying improvements to their property in order to reduce the energy or water consumption on such property or to install an improvement to such property that produces energy from renewable resources.[2]

A "project" may be for any industrial, commercial, business, office, parking, public, or other use, provided that a majority of the members of the authority determine, by a duly adopted resolution, that the project and such use thereof would further the public purpose of the Downtown Development Authorities Law. Such term shall include any one or more buildings or structures used or to be used as a not for profit hospital, not for profit skilled nursing home, or not for profit intermediate care home subject to regulation and licensure by the Department of Community Health and all necessary, convenient, or related interests in land, machinery, apparatus, appliances, equipment, furnishings, appurtenances, site preparation, landscaping, and physical amenities.

b. Constitutional Amendment Authorities

Prior to 1969 (the year the original Development Authorities Law was enacted pursuant to the power granted to the General Assembly by GA CONST. Art. IX, Sec. VI, Para. III), development authorities could only be created pursuant to a local amendment to the Constitution of the State of Georgia. These types of authorities are typically referred to as constitutional amendment authorities. Like other local constitutional

[2] O.C.G.A. §36-42-3(6).

amendments, each local constitutional amendment to create a constitutional amendment authority had to be approved by a majority of the voters of the affected jurisdiction. Each constitutional amendment authority has unique purposes and powers, which are generally broader than the purposes and powers of general enabling act or statutory authorities. Local government attorneys should review the constitutional amendment creating any constitutional amendment authority in their jurisdiction to determine which specific projects such authorities are authorized to undertake.

The Constitution of the State of Georgia of 1983 prohibits the creation of new local constitutional amendment authorities. However, constitutional amendment authorities already existing at the time of the ratification of the Constitution of the State of Georgia of 1983 were authorized to be continued by local law if such local law was enacted prior to 1986.

c. Local Act Authorities

Authorities may also be created pursuant to a local law or local act. These types of authorities are typically referred to as local act authorities. A bill proposing to create a local act authority is generally introduced in the General Assembly by the local legislative delegation at the request of a local government. A common form of local act authority is a public facility authority.

City and counties typically create local act authorities to provide such authorities with certain powers that may not be available to general enabling act or statutory authorities (e.g. the power to finance certain governmental projects) or to limit certain powers that might be available to general enabling act or statutory authorities (e.g. membership requirements for the board of the authority, the power to finance only a certain type of project, etc.).

SECTION II

Conduit Financings - Revenue Bonds and Intergovernmental Contracts

1. Introduction

If an appropriate authority is available, counties and cities may use an authority to issue revenue bonds to finance certain types of projects on its behalf. Pursuant to an intergovernmental contract between the authority and the local government[3], the authority issues revenue bonds to finance the costs of certain projects, and the local government, in consideration of the authority's doing so, is obligated to make payments to the authority in amounts sufficient to pay the debt service on such revenue bonds. The payments made by the local government pursuant to the intergovernmental contract are not considered a general obligation debt of the local government, however, the contractual obligation to make the contract payments and to levy such tax as may be necessary for purposes of making the contract payments is a legal, binding, and enforceable obligation and the local government may directly exercise its taxing powers for such purpose. These types of transactions are often referred to as "contract-backed" bonds.

Since the revenue bonds for these transactions are issued by authorities, the projects are limited to those types of projects which may be financed by the governmental authority. In addition, the intergovernmental contract must deal with joint facilities or services which each of the contracted parties are authorized by law to provide.[4] There are several types of authorities (all with different powers), but the most common type of governmental authority available to local governments is a development authority created and activate pursuant to the Development Authorities Law. Generally, development authorities may only finance projects which promote trade commerce and industry and increase employment opportunities.[5] Courts have determined that most governmental projects may not be financed by these development authorities.[6] Generally, governmental projects are financed by constitutional amendment authorities and local act authorities. Prior to commencing an intergovernmental "contract-backed" transaction, the local government should research which types of governmental authorities are available and which types of projects may be financed by these authorities.

2. Revenue Bond Law

The Revenue Bond Law (O.C.G.A. Section 36-82-60 *et seq.*) authorizes the issuance of revenues bonds to provide funds to pay the costs of the acquisition, construction, reconstruction, improvement, betterment, or extension of any

[3] Ga. Const. Art. IX, Sec. III, Para. I.
[4] Nations v. Downtown Dev. Auth., 338 S.E.2d 249 (1986); Nations v. Downtown Dev. Auth., 345 S.E.2d 581 (1986); and City of Decatur v. DeKalb County, 713 S.E.2d 846 (2011).
[5] Odom v. Union City Downtown Development Authority, 305 S.E.2d 110 (1983) and Haney v. Development Authority of Bremen, 519 S.E.2d 665 (1999).
[6] Id.

undertaking in anticipation of the collection of revenues of such undertaking. Revenue bonds may be issue by a city, county or other political subdivision or through the use of various authorities, including general enabling act or statutory authorities (development authorities and downtown development authorities), constitutional amendment authorities and local act authorities.

Revenue bonds may be issued for the following purposes:

1) Causeways, tunnels, viaducts, bridges and other crossings
2) Transportation facilities, including highways, parkways, airports, docks, piers, wharves, terminals, and other facilities
3) Water supply, water treatment, wastewater collection, treatment and disposal systems
4) Solid waste
5) Gas and electric generating and distribution facilities
6) Dormitories, laboratories, libraries and related facilities
7) Parks, golf courses, tennis courts, swimming pools, stadiums, athletic fields, grandstands and stadiums, etc.
8) Combinations of sea wall, groin, and beach erosion protection systems
9) Public parking areas and public parking buildings
10) Parking meters
11) Facilities necessary for the use of motor buses, trackless trolleys, electric trolleys, or any other means of transportation of passengers on streets and highways
12) Facilities for lease to industries to relieve abnormal unemployment conditions
13) Jails.

The issuance of revenue bonds does not require an election (except for revenue bonds issued to finance electric generating and distribution systems), but rather may be authorized by resolution of the governing body of the county or municipality, which may be adopted at a regular or special meeting by a majority of the members of the governing body.

3. Revenue Bonds Secured by Intergovernmental Contracts

The taxing powers of a political subdivision may be indirectly pledged as security for the payment of revenue bonds pursuant to GA CONST. Art. IX, Sec. III, Para. I(a) (the "intergovernmental contracts provision")[7], which states that the State of Georgia and any municipality, county, school district, or other political subdivision of the State may:

> "contract for any period not exceeding 50 years with each other or with any other public agency, public corporation, or public authority for joint

[7] Building Authority of Fulton County v. State of Georgia, 321 S.E.2d 97 (1984); Thompson v. Municipal Electric Authority of Georgia, 231 S.E.2d 720 (1976); Nations v. Downtown Dev. Auth., 338 S.E.2d 249 (1986) and Nations v. Downtown Dev. Auth., 345 S.E.2d 581 (1986).

> services, for the provision of services, or for the joint or separate use of facilities or equipment, but such contracts must deal with activities, services or facilities which the contracting parties are authorized by law to undertake or provide. By way of specific instance and not limitation, a mutual undertaking by a local government entity to borrow and an undertaking by the state or a state authority to lend funds from and to one another for water or sewerage facilities or systems pursuant to law shall be a provision for services and an activity within the meaning of this Paragraph."

The type of authority and the nature of the undertaking affect the ability to use an intergovernmental contract-backed transaction to finance projects.

SECTION III

An Overview of Ad Valorem Tax Abatements in Georgia Utilizing Authorities

1. Introduction

Like many states throughout the country, Georgia offers ad valorem property tax abatements to entice new and expanding companies to select Georgia as the location of their investment. While the objective in each instance is the temporary reduction of property tax for the investing company, each state's abatement program is somewhat unique and is designed to navigate the ever-evolving case law on the subject. Georgia has developed a relatively complicated sale-leaseback structure which requires the issuance and validation of industrial revenue bonds by development authorities prior to an award of a property tax abatement. Below is a brief summary of the Georgia courts' treatment of ad valorem property tax abatements. Sale-leaseback transactions may be structured in many different formats. Below is a highlight of the essential elements of a basic sale-leaseback model which has become one of the most common vehicles for structuring ad valorem property tax abatements in Georgia.

2. Legal Analysis of Georgia Tax Abatements

a. General Requirements

Pursuant to Georgia law, all real and personal property are taxed according to its fair market value.[8] Such tax shall be uniform and shall be charged against the owner of the interest in the property.[9] Local governments may not grant property tax abatements directly to private parties, and pursuant to the Georgia Constitution, all laws exempting property from ad valorem taxation are void.[10] Nonetheless, the Georgia Supreme Court has upheld tax abatement arrangements in certain instances.[11] In these cases, the private taxpayer may not receive the benefits of the abatement directly, and the general public must receive certain notices relative to the project. In light of these core requirements, Georgia attorneys have developed a sale-leaseback arrangement whereby the property subject to an abatement is transferred to a governmental entity (an authority), and the public, as well as the local taxing jurisdictions, receives notice of the transfer pursuant to an industrial revenue bond validation proceeding.

b. Transfer of Property

While private property must be taxed according to its full, fair market value, public property is exempt from property tax so long as it remains owned by a public

[8] O.C.G.A. §48-5-6.
[9] Ga. Const. Art. VII, Sec. II, Para. I; O.C.G.A. § 48-5-9.
[10] Ga. Const. Art. VII, Sec. II, Para. I.
[11] Hart County Bd. of Tax Assessors v. Dunlop Tire & Rubber Corp., 314 S.E.2d 188 (Ga. 1984); Charlton Dev. Auth. v. Charlton County, 317 S.E.2d 204 (Ga. 1984).

entity.[12] Accordingly, by transferring privately-held property to a governmental entity, a private entity may enjoy all or some of the tax savings available to the government. The recipient of this property is typically a local development authority (e.g. a general enabling act or statutory development authority or a constitutional amendment authority) which has been created specifically to promote the expansion of industry and trade within the designated county or municipality.[13] By statute or constitutional amendment, this authority generally has the power to acquire, sell or lease property as well as the power to issue bonds.[14] The county, city or authority attorney should review the enabling statute or constitutional amendment of the transferee to ensure that the local authority has the requisite power to transfer the desired tax savings to the company. For example, in rare cases the constitutional amendment creating an authority will provide that the property of such authority will have the same immunity from taxation as the property of the county or municipality in which the authority resides.[15] In such instances, the taxpayer's property will avoid tax entirely and will receive a full ad valorem exemption on the transferred property. Conversely, other constitutional amendments state explicitly that the authority's exemption from taxation shall not extend to its tenants or lessees.[16] Most often, however, a court will conclude that, while a development authority's fee interest in the property is exempt from taxation, the private company, as the tenant of such property, must pay ad valorem tax on its leasehold interest in the property.[17]

c. Taxation of Leasehold Estates

An interest in land will fall into one of three property classes: (i) the absolute or fee simple estate; (ii) the estate for years, or the leasehold estate; or (iii) the usufruct.[18] The fee simple estate is the broadest form of ownership, and the usufruct, which is essentially a mere license to use certain property, is the most limited interest in land. An intermediate estate is the leasehold estate which provides the occupant with broad possessory rights to use and develop property subject to a lease agreement with the fee owner. A leasehold estate is a severable interest in the land and, for tax purposes, is classified as a distinct real property estate.[19] As taxable property (except if the fee simple estate is held by certain types of constitutional amendment authorities as described below), the local board of tax assessors may levy ad valorem tax on the leasehold estate. However, because the owner of a fee simple estate is typically assessed taxes upon the full value of the property, the owner of a leasehold interest ordinarily is not required to pay ad valorem tax on its property interest.[20] Any determination

[12] Delta Air Lines v. Coleman, 131 S.E.2d 768, 771 (Ga. 1963).
[13] O.C.G.A. §36-62-6.
[14] Id.
[15] See footnote 11.
[16] See Hart County Board of Tax Assessors v. Dunlop Tire & Rubber Corp., 314 S.E.2d at 190 (citing Kingsland Development Authority, Ga. L. 1962 pp. 813, 814; Americus-Sumter Payroll Development Authority, Ga. L. 1962, pp. 933, 938; LaGrange Development Authority, Ga. L. 1964, pp. 779, 780).
[17] See Delta Air Lines, 131 S.E.2d at 771.
[18] DeKalb County Bd. of Tax Assessors v. W.C. Harris & Co., 282 S.E.2d 880 (Ga. 1981); Diversified Golf v. Hart County Bd. of Tax Assessors, 598 S.E.2d 791 (Ga. Ct. App. 2004).
[19] See Delta Air Lines, 131 S.E.2d at 771.
[20] Id. at 773.

otherwise would result in the imposition of a double tax on the same property. However, when a development authority or other tax-exempt entity owns a fee simple interest in the land, the board of tax assessors may levy a tax upon the leasehold estate at the time it passes to private ownership.[21] If the development authority is a constitutional amendment authority, the leasehold interest may be exempt from ad valorem taxes altogether. The Supreme Court of Georgia has ruled that if the development authority is created by local constitutional amendment, the development authority's interest in the property and the lessee's leasehold interest are exempt from ad valorem property taxes provided that the local constitutional amendment does not specifically state that the exemption shall not extend to the authority's tenants and lessees.[22]

d. Negotiating the Leasehold Value of a Leasehold Estate

Although a company's leasehold interest is subject to taxation (except if the fee simple estate is held by certain types of constitutional amendment authorities as described above), the company may negotiate with the local board of assessors to reach an agreement on the value of such leasehold interest.[23] In effect, this negotiated rate may serve as a tax abatement on the property. If approved by the board, the abatement may extend to realty, personalty or both, but it may not circumvent Georgia's constitutional requirement of uniform taxation.[24] For instance, if a county typically limits property tax abatements to 50% of the tax otherwise due on such property, a company that negotiates an abatement on similar property (providing the same type of employment and employees) in excess of 50% may contravene Georgia's constitutional requirement of uniform taxation and risk losing the abatement entirely.[25] Likewise, if a municipality has a history of limiting ad valorem abatements to real property, an abatement that extended to personalty would violate this requirement of uniform taxation. According to the court, taxable property within the same class within a county must be assessed with uniformity among similarly situated taxpayers. Accordingly, if a company reaches an agreement with a local board of assessors to reduce the value of such company's leasehold interest in property that has been transferred to a local development authority, a Georgia court most likely will uphold such agreement provided the negotiated value of the leasehold interest is comparable to values designated for similarly-situated taxpayers.[26]

As stated above, when a development authority is created by local constitutional amendment and the ad valorem property tax exemption is not expressly limited to the authority (the leasehold interest is also exempt), the company will probably not have to pay taxes on its leasehold estate. Notwithstanding the fact that a company may not be obligated to pay ad valorem taxes on its leasehold estate because it is exempt or because it has not value, typically, in connection with a sale-leaseback transaction, the company

[21] Id. at 771.
[22] See footnote 11.
[23] Coweta County Board of Tax Assessors v. EGO Products, Inc., 526 S.E.2d 133, 134 (Ga. Ct. App. 1999).
[24] Id. at 136.
[25] See Id.
[26] Id.

makes a payment in lieu of taxes which equals the negotiated amount that the company would have paid on its leasehold estate as if the exemption did not apply.

e. Gratuities Clause

The issuance of industrial development revenue bonds enables the sale-leaseback structure to avoid violation of the Gratuities Clause of the Georgia Constitution,[27] and it provides certain legitimacy to the arrangement by subjecting the transaction to public scrutiny and a court validation. GA CONST. Art. III, Sec. VI, Para. I(a) Article 3 provides, "Except as otherwise provided in the Constitution, the General Assembly shall not have the power to grant any donation or gratuity or to forgive any debt or obligation owing to the public...."[28] This provision against the granting of gratuities by the General Assembly has been interpreted by Georgia courts to apply to cities and counties as well.[29] While this prohibition does not impact a company's ability to transfer private property to a governmental entity, it may preclude a development authority from conveying such property back to the company following the expiration of the tax abatement. To avoid any risk of violating the Gratuities Clause, most Georgia attorneys advocate the issuance of bonds which, as described below, will generate a stream of rental payments from the company, as lessee. By paying rent during the term of the tax abatement, the company accumulates equity in the property and may purchase the property for a nominal fee following the expiration of the abatement, or lease, term, thereby acquiring the property for value and avoiding the Georgia Constitution's prohibition against gratuities.

f. Bond Validation

Georgia law requires revenue bonds issued by a governmental body to be validated by a superior court of the state.[30] While this process is somewhat laborious and time-consuming, one advantage of the validation is the receipt of a judicial approval or "blessing" of the transaction. The validation process also requires the development authority, as issuer of the bonds, to publish notice of the validation proceedings in a local newspaper.[31] This notice provides the general public, as well as the local taxing jurisdictions, with an opportunity to contest the bond issue and underlying transaction. In the event a party fails to contest the bonds and such bonds are validated according to Georgia law, a court is likely to deny subsequent challenges to the bonds or any matters, such as the property tax abatement, which are addressed in the validation pleadings.[32]

[27] Ga. Const. Art. III, Sec. VI, Para. VI.
[28] Id.
[29] City of Lithia Springs v. Turley, 526 S.E.2d 364 (Ga. Ct. App. 1999).
[30] O.C.G.A. §36-82-73.
[31] O.C.G.A. §36-82-22.
[32] See Charlton Dev. Auth., 317 S.E.2d at 204 (holding that a tax levy agreement which was referred to in bond validation proceedings was beyond subsequent challenge by the county).

3. Overview of Sale-Leaseback Bond-Financing Documents

a. Inducement Resolution

Once a new or expanding company has negotiated with a county or municipality to receive an ad valorem tax abatement, the local development authority in such county or municipality will pass an inducement resolution or approve a memorandum of understanding. This inducement resolution or memorandum of understanding reflects the authority's commitment to issue bonds to finance the project for lease and exclusive use by the company.

b. Bond Resolution

Following a commitment by the development authority to issue bonds, the bond documents are drafted, negotiated and ultimately approved pursuant to a bond resolution. This resolution authorizes the chair or vice-chair of the development authority to execute the necessary documents to issue bonds, and the primary bond documents (the trust indenture, the lease agreement, the guaranty and the bond purchase agreement) are attached as forms approved by the authority.

c. Trust Indenture

Often, a corporate trustee (e.g., a bank) is selected to serve as trustee for the benefit of the bondholders. Pursuant to the trust indenture, the bank agrees to represent the interests of the bondholders, and the bank receives from the development authority, as issuer of the bonds, a security interest in the rental payments received from the lessee of the project (i.e., the taxpayer company) and in the limited warranty deed. In other words, the trust indenture is analogous to a loan agreement whereby the borrower (i.e., the development authority) agrees to make certain payments of principal and interest, as more fully set forth in the bond, to the lender (i.e., the holders of the bond). As with most loans, the lender receives certain collateral (i.e., assignment of the rent payments and a security deed) as assurance that the borrower will satisfy its debt obligations.

The indenture also outlines the process for payment of the bond proceeds to the borrower as well as the process for repayment of such funds. Essentially, the bonds are sold to the bondholders in various installments as funds are needed to finance the project. For instance, when the taxpayer company (acting as construction agent for the development authority) desires reimbursement for certain project expenses, the taxpayer company (on behalf of the development authority) will notify the trustee that it wishes to take a draw from the bonds. A bond is sold, and the bond proceeds are placed in a project fund. The taxpayer company will provide the trustee with a requisition and supporting documentation (e.g., project invoices). The trustee transfers funds from the project fund to the taxpayer company.

Note that, in a true financing, the bonds would be sold by a marketing agent to one or more parties. A bond issue whose sole purpose is to support a property tax abatement typically is sold exclusively to the beneficiary of the abatement (i.e., the

taxpayer company). For this reason, such bonds are often called "phantom" bonds. In other words, the company serves both as the provider and the recipient of the bond proceeds and the transaction does not reflect a true (i.e., third-party) financing arrangement.

d. Repayment of the Bonds.

The development authority, as issuer of the bonds, is obligated to make payments of principal and interest on the bonds to the bondholders (in this case, the taxpayer company). This obligation, however, is not guaranteed by the full faith and credit for the development authority or local community. Instead, the debt service is financed from the rent payments received from the taxpayer company which leases the project for the term of the tax abatement. In other words, as landlord of the project, the development authority receives rent equal to the principal and interest owed on the bonds. These payments of principal and interest are transferred to the trustee who remits such funds to the bondholders (i.e., back to the taxpayer company). Because the company serves as tenant of the project as well as holder of the bonds, the indenture states that the company may make rental payments to itself pursuant to a Home Office Payment Agreement, thereby permitting the company to avoid the hassle and expense of wiring funds to and from the trustee.

e. Sale and Leaseback of the Project.

As stated, a taxpayer company may not receive an ad valorem tax abatement until the abated property has been transferred to a local development authority or other governmental unit. Accordingly, at the outset of the abatement, the taxpayer company must transfer to the development authority all real property pursuant to a warranty deed and all personal property pursuant to a bill of sale. Following the initial transfer, all future real property improvements will become property of the development authority by virtue of the deed; however, subsequently-acquired personal property must be transferred to the development authority. As a result, by December 31 of each year, the taxpayer company should transfer all personal property acquired during the year to the development authority. These additional transfers will ensure that the newly-acquired personal property will be owned by the development authority as of January 1, the determination date for property tax liability.

Once the development authority has acquired title to the project pursuant to a bill of sale and warranty deed, the authority will lease the agreement to the taxpayer company pursuant to a lease agreement in exchange for rent equal to the debt service due on the taxable bond issue. The authority will lease and operate the project for the duration of the property tax abatement and will transfer the property to the company via bill of sale and/or quitclaim deed upon the expiration of the abatement (and the lease agreement). Because the lease agreement is deemed a capital lease, the company may acquire the project for a nominal fee without violating the Gratuities Clause of the Georgia Constitution. Under federal tax law, the lease is a financing lease and the company retains all tax benefits (depreciation rights, etc.).

f. Bond Purchase Agreement and Guaranty Agreement.

Pursuant to a bond purchase agreement, the company agrees to purchase all bonds issued by the development authority in connection with the project. The company, therefore, will be the sole holder of the bonds and, therefore, the sole lender of financing for the project. Because the bonds are not sold to the public, any SEC filing and disclosure requirements are avoided. As additional security for the bonds, the company, as lessee of the project, also executes a guaranty agreement whereby the company guarantees repayment of the principal of and the interest on the bonds.

g. Zero Sum Transaction.

Unless the bonds are sold to a third party (i.e., someone other than the taxpayer company), the transaction does not represent a typical financing arrangement. The development authority issues the bonds for sale to the company. While the development authority is obligated to the company (as holder of the bonds), this obligation is commensurate with the company's obligation to pay rent to the authority (as landlord of the project). Likewise, the company must transfer funds for the purchase of the bonds, but this cash outlay is commensurate with the funds the company receives as construction agent or manager of the project. The transfers of funds are a wash and do not ultimately require any outlay of funds from the development authority or the company (other than funds the company otherwise would have spent to acquire the project).

h. Illustration.

Assume that a company desires to acquire a conveyor system for $1 million and to receive a tax abatement on such equipment. The company will purchase the conveyor system as it would irrespective of the tax abatement. The company then transfers the conveyor system to a local development authority. The authority acquires the conveyor with funds it has received from the company as purchaser of a bond issued by the authority. While the company has transferred (on paper) $1 million to the authority upon purchase of the bond, the company immediately receives a refund of such payment after showing proof that the company, as agent for the authority, spent $1 million to acquire the equipment. The authority must pay to the company the principal and interest due on the $1 million bond; however, this stream of funds is provided by the company as rent for the exclusive use of the conveyor system, which is owned by the authority.

4. Conclusion

Georgia typically classifies the interest of a private company in a sale/leaseback arrangement as a leasehold estate that is subject to taxation. Although the property is subject to tax, the company may negotiate with the local board of tax assessors to obtain an abatement of the tax. If obtained with the board's consent, the abatement may extend to real and personal property, but it may not violate Georgia's constitutional requirement of uniform taxation.

SECTION IV

Valuation of Leasehold Estates

Overview

As discussed earlier, there are two types of development authorities – those created by local constitutional amendment and those created by general law (i.e. the Development Authorities Law or the Downtown Development Authorities Law). If the development authority is created by local constitutional amendment, the company's leasehold interest may be exempt from ad valorem property tax altogether. If the development authority is created by general law, the company's leasehold estate will not be exempt from ad valorem property taxes, and the company will have to pay taxes based upon the fair market value of its leasehold interest.

Georgia law provides that each county board of tax assessors has a legal duty to "see that all taxable property within the county is assessed and returned for taxes at its fair market value."[33] Georgia law also provides that "each county board of tax assessors shall . . . exercise its powers and discharge its duties and is specifically authorized, without limitation, to use a method or methods of valuation for leases related to revenue bonds or other revenue obligations issued by a local government authority for a capital project or projects to be leased primarily to a nongovernmental user or users, based on assessments of the increasing interest of the nongovernmental user or users in the real or personal property, or both, over the term of the lease, or to use a simplified method or methods employing a specified percentage or specified percentages of such leasehold interests."[34]

The Supreme Court has provided that a board of tax assessors' methodology for determining the fair market value of the leasehold interest will not be set aside provided that the methodology is not arbitrary and unreasonable.[35]

[33] O.C.G.A. §48-5-306(a).
[34] O.C.G.A. §36-80-16.1(e)
[35] See DeKalb County Bd. of Tax Assessors v. W.C. Harris & Co., 282 S.E.2d 880 (Ga. 1981); see also Coweta County Board of Tax Assessors v. EGO Products, Inc., 526 S.E.2d 133, 134 (Ga. Ct. App. 1999); and see also SJN Properties, LLC V. Fulton County Board of Tax Assessors, No. S14A1493, WL 1393398 (Ga. Mar. 27, 2015).