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# FISCAL IMPLICATIONS

## of Property Tax Exemption for Wind Project

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Any questions about the tool kit, its use and availability should be directed to: Vicki Colello; vac@nyserda.org; 518-862-1090, ext. 3273.

In addition, other reports and information about Wind Energy can be found at www.powernaturally.org in the on-line library under "Large Wind."

## NOTICE

This report was prepared by the Pace Energy Project in the course of performing work contracted for and sponsored by the New York State Energy Research and Development Authority (hereafter "NYSERDA"). Substantial contributions to the report were made by the NYS Department of Environmental Conservation.

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## EXECUTIVE SUMMARY

The Pace Energy Project (Pace), under contract for the New York State Energy Research and Development Authority (NYSERDA), has prepared this paper to evaluate the fiscal impact of property tax exemptions for wind energy development on state school aid. Specifically, we have set out to determine whether property tax exemptions made available to wind energy systems have negative consequences from the standpoint of the local school taxing district receiving its fair share of state aid under state aid formulae.

Under existing New York State law, the assessment of additional property taxes derived from wind energy development may be exempt for a period of 15 years, at the discretion of the local taxing jurisdiction. School districts are among the taxing jurisdictions authorized to exempt wind energy improvements. Exemption from local property taxes could enhance the economic viability of wind energy development in New York State and provide a strong financial incentive to a wind developer considering alternative sites to locate in a jurisdiction where such exemptions are made available. Similarly, the exemption could help offset the initial capital cost of a project for a homeowner or commercial property owner considering such system.

However, some concern has arisen over the negative impact of property tax exemptions for wind projects on the formula used for calculating state school aid. Unless and until this issue is clarified and effectively resolved, property tax incentives may be rendered an ineffective instrument for the promotion of economic development through wind energy promotion.

Our findings indicate that while there are competing tendencies, under most circumstances, the wind energy exemption will have a **favorable** fiscal impact. This conclusion is supported by the following considerations:

- Over half of all financial resources available to school districts derive from revenues raised locally. The exemption of wind energy system equipment from the calculation of "assessed value" means that the school district will collect a lesser amount of property tax than if the equipment had been fully taxable.
- The law exempting wind energy systems from local taxes explicitly recognizes the right of local taxing jurisdictions to separately negotiate Payments in Lieu of Taxes (PILOTS) with developers. Thus, any tax loss associated with the wind energy exemption may be partially offset by annual PILOT payments. It is

anticipated that PILOTS will be more germane to large, utility-scale systems than to smaller customer-sited wind projects.

- A further compensating factor is the positive influence of the wind energy exemption on the formula for calculating state school aid. While there are many state aid formulas, as a general rule, the lower the assessed value of District property per pupil, the greater the state aid; conversely, the greater the assessed value, the lower the state aid. However, because wind energy systems are not considered in the quantification of assessed value, the statutory exemption increases economic activity within the district while maintaining the status quo with respect to the school district's expected state aid.
- As a prominent example, nearly half of all state aid consists of Operating Aid, which is based on weighted attendance and wealth of school districts. The statutory exemption for wind energy systems means that the school district's "wealth" remains constant for purpose of the formula, and will receive the same level of school aid.
- At the time the wind-related property becomes part of the taxable property base, this results in an increase in the assessed value of district property per pupil. Under current formulation, this increase in real property "wealth" is accompanied by a reduction in state aid. Therefore, the impact of property tax incentives for wind development occurs, if at all, after the 15-year period.
- When the statutory exemption expires, the wind farm will come on the rolls based on its depreciated value as a 15-year old asset. Thus, the financial impacts of the expiration of the tax exemption – both positive and negative – will attenuate over time.

The current property tax exemption for wind energy systems is set to sunset on January 1, 2006. NYSERDA will need to consider whether the current law should be extended in its present form.

Additionally, there is some precedent in New York State law for considering the revenues a local taxing district derives through PILOTS in the calculation of state aid to that district. In order to preserve the local taxing district's incentive to remain in the program, the Real Property Tax Law should be amended to explicitly exempt PILOTS from inclusion in assessed value for purposes of the state school aid formula.

Finally, the long-standing approach to allocating school aid in New York State is in the process of a fundamental overhaul by virtue of the *Campaign for Fiscal Equity* decision. There are several competing reform proposals being actively considered by policy makers, each designed to redress the fundamental inequities perceived by the Court of Appeals in the way state support for public education is allocated. While the *CFE* decision necessitates changes to the school aid system, it is far from clear how policy makers will meet the Court of Appeal's mandate. One can surmise, however, that as district "wealth" – as measured by real property values and income -becomes an even more important determinant of state aid, it will become more important for school districts to preserve the exemption for wind energy systems.

## 1. The Problem

Under existing New York State law, the assessment of additional property taxes derived from wind energy development may be exempt for a period of 15 years, at the discretion of the local taxing jurisdiction. School districts are among the taxing jurisdictions authorized to exempt wind energy improvements. Exemption from local property taxes could enhance the economic viability of wind energy development in New York State and provide a strong financial incentive to a wind developer considering alternative sites to locate in a jurisdiction where such exemptions are made available. Similarly, the exemption could help offset the initial capital cost of a project for a homeowner or commercial property owner considering such system.

Some concern has arisen over the negative impact of property tax exemptions for wind projects on the formula used for calculating state school aid. Unless and until this issue is clarified and effectively resolved, property tax incentives may be rendered an ineffective instrument for the promotion of economic development through the establishment of wind energy facilities.

## 2. Scope of Work

The Pace Energy Project (Pace), under contract to the New York State Energy Research and Development Authority (NYSERDA), has prepared this paper to evaluate the fiscal impact of property tax exemptions for wind energy development on state school aid formulas. Specifically, we have set out to determine whether property tax exemptions made available to wind energy systems have negative consequences from the standpoint of the local school taxing district receiving its fair share of state aid under the current and expected state aid formulae.

The scope of work was divided in two main tasks. First, Pace conducted an independent legal analysis of New York State law as it relates to wind energy development and property tax incentives. This consisted of a review of applicable state law, regulations, case law, interpretive bulletins, law review articles and other primary sources. In addition, Pace reviewed litigation concerning state aid formula and its potential impacts on property tax exemptions for wind improvements.

Second, to validate our research and analysis, Pace conducted interviews with individuals who have a working knowledge of these issues to confirm our research results.

## 3. Description of the Current Law as it Relates to Property Tax Associated with Wind Energy Production Facilities

### 3.1 Summary

Originally enacted in 1977 (and amended in 1979 and 1990), Section 487 of the New York State Real Property Tax Law provides a 15-year real property tax exemption for solar, wind or farm waste energy systems constructed in New York State.[1] The exemption enacted in 1990 is subject to local option (see below under 3.7).

The amount of the exemption is equal to the increase in assessed value attributable to the solar, wind, or farm waste energy system.[2] Definitions and guidelines for the eligibility for exemption of solar and wind energy equipment may be found at the Web site of the Office of Real Property Services.[3]

### 3.2 Legislative Intent

The intent of the property tax exemption is to encourage the installation of solar, wind and farm waste energy equipment systems in residential, commercial, institutional and industrial applications. The exemption ensures property owners that their real property taxes will not increase as a result of the installation of these systems.

> The Legislative findings and intent, expressed the following:
>
> The legislature hereby finds that solar energy systems, passive, active or both, or wind energy systems do not require fuel, and thus will aid in energy conservation. Because at this time they involve relatively high initial capital expenditure, the long term economic advantages of an installed solar or wind energy system would be substantially reduced by an increase in property tax. This increase would frustrate state policy to encourage the greater use of solar and wind energy.

The purpose of the legislature is to provide for exemption from real property taxation for approved installations of solar and wind energy systems in order to encourage their

[1] NYS Real Property Tax Law Title 2, Sec. 487 (Date Enacted: 1977; Amended 1990, 2002; Effective Date: Before 7/1/88 or between 1/1/91 & 1/1/06; Expiration Date: 2006); S.B. 6592 of 2001 (Date Enacted: 2002; Effective Date: 2002). On September 17, 2002, the property tax exemption was expanded to include farm waste electric generating equipment, satisfying guidelines established by NYSERDA. S.B. 6592 of 2001. Farm waste electric generating equipment is equipment that generates electric energy from biogas produced by the anaerobic digestion of agricultural waste, such as livestock manure, farming waste, and food processing wastes with a rated capacity of not more than 400 kW. For more information *see:* http://www.nyserda.org/energyresources/wind.html; www.dsireusa.org/.
Note: The exemption is limited to NYS real property tax. Such property is liable for special ad valorem levies and special assessments. *Id.* pp. 20.01 & 20.03.

[2] New York State Office of Real Property Services, *Assessor's Manual*, Solar, Wind, or Farm Waste Energy System, Volume 4: Exemption Administration, Section 4.01, p. 20.04. [hereinafter NYS Assessor's Manual], *available at:* http://www.orps.state.ny.us/assessor/manuals/vol4/part1/section4.01/sec487.htm.

[3] *Id.*

greater use. This offers a tax incentive to property owners without reducing tax income to the community.[4]

### 3.3 System Description

Wind energy systems collect wind energy through a propeller or blade configuration, known as a rotor, and use that energy to drive a generator to produce electric power, to power a drive shaft for mechanical applications or to provide heat.[5]

Section 487 of the Real Property Tax Law contains broad definitions of wind energy systems and wind equipment.[6] More detailed system descriptions and criteria for eligibility for an exemption are found in Appendix B.[7]

### 3.4 Property Use Requirements

While there are no ownership or property location requirements, to be eligible for the exemption the property must contain a wind energy system or wind energy equipment designed to provide heating, cooling, hot water, or mechanical, chemical, or electrical energy by the collection of wind energy and its conversion, storage, protection, and distribution. Wind energy equipment qualifying the property for exemption includes collectors, controls, energy storage devices, heat pumps and pumps, heat exchangers, windmills, and other materials, hardware, or equipment necessary to the process by which wind is collected, converted into another form of energy, stored, protected from unnecessary dissipation, and distributed. It does not include pipes, controls, insulation, heat pumps, or other equipment that is part of the normal heating, cooling, or insulation system of a building. It does include insulated glazing or insulation to the extent that such materials exceed the energy efficiency standards required by law.[8]

Some building's components serve as part of the wind system as well as the building structure. It should be noted, however, that where components serve dual functions, i.e., part of a building structure as well as part of a wind energy system, only the increased assessed value which is attributable to the portion of the components that allows them to serve as part of the wind energy system is eligible for the tax exemption.[9] This aspect of the law is more germane to small, customer-sited wind systems than to utility-scale projects which are fully exempt.

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[4] Laws 1977, ch 322, § 1, as amended Laws 1979, ch 220, § 1, eff June 11, 1979.
[5] See Appendix B, System Description. See also NYSERDA's web site at: http://www.nyserda.org/energyresources/wind.html; AWEA's web site at: http://www.awea.org/smallwind/newyork.html.
[6] See Appendix A, Section 487(1) of the Real Property Tax Law – Statutory Definitions.
[7] New York State Energy Office, Solar and Wind energy Systems: Definitions and Guidelines for Property Tax Exemptions, available at: http://www.orps.state.ny.us/assessor/manuals/vol4/part1/section4.01/solar_report.pdf
Please note that this definitions guidelines booklet issued by the former Energy Office remains in full force and effect until modified or repealed by NYSERDA. Copies of the booklet may also be obtained from NYSERDA.
[8] NYS Assessor's Manual, supra note 2, p. 20.01
[9] New York State Energy Office, Solar and Wind energy Systems: Definitions and Guidelines for Property Tax Exemptions, supra note 7, at 1.

### 3.5 Time requirements

The exemption applies to systems which are:

(a) existing or constructed prior to July 1, 1988

or

(b) constructed subsequent to January 1, 1991 and prior to January 1, 2006.[10]

### 3.6 Eligibility Criteria

To be eligible for the property tax exemption, a wind energy system must be equipped with overspeed controls. In addition, an electric generating wind energy system must be designed to produce not less than 250 watts of power in 25 mile per hour winds.[11]

### 3.7 Local Option

With respect to systems constructed after January 1, 1991, and before January 1, 2006, each county, city, town, village and school district (except the city school districts of New York, Buffalo, Rochester, Syracuse, and Yonkers – also termed "the Big 5") may choose whether to disallow the exemption. The option must be exercised by counties, cities, towns, and villages through adoption of a local law and by school districts by adoption of a resolution.

In other words, wind systems constructed prior to July 1, 1988 may be eligible for the exemption throughout the State. Wind systems constructed between January 1, 1991 and January 1, 1996 may be eligible except where a local municipality or a school district has provided by local law or resolution that no solar or wind exemption shall apply within its jurisdiction for systems constructed after January 1, 1991 or the date of such local law or resolution, whichever is later.[12]

### 3.8 Payments in Lieu of Taxes (PILOTS)

Each county, city, town, village and school district (except the school districts of New York, Buffalo, Rochester, Syracuse, and Yonkers) that has not disallowed the exemption may require the owner to enter into a contract for payments in lieu of taxes. As part of such contract, the property owner may be required to make annual payments in an amount not to exceed the amounts which would have been payable without the exemption. Such a contract may not operate more than 15 years, commencing from the date on which the benefits of this exemption first become effective.[13]

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[10] NYS *Assessor's Manual, supra* note 1, p. 20.02.
[11] *See* New York State Energy Office, *Solar and Wind Energy Systems: Definitions and Guidelines for Property Tax Exemptions, supra* note 7, at 5.
[12] To verify check with the local property assessor, the State Division of Equalization and Assessment or the State Energy Office to determine whether the exemption is available in such locality for systems constructed after January 1, 1991.
[13] NYS *Assessor's Manual, supra* note 2, p. 20.04.

Practically speaking, PILOTS are more likely to be required for large-scale wind farms than for small customer-sited systems. As will be described in Section 4.3.1 below, *PILOTS negotiated with project developers allow the taxing district to recapture some of the revenues that would have otherwise been lost as a result of the wind exemption without negatively affecting the state aid to schools.*

## 3.9 Filing Requirements and Reporting

Filing requirements for the wind exemption by the owner or occupant of the property are quite simple.[14] There are no reporting requirements.

### 3.10 Industrial Development Authority (IDA) Exemption

An Industrial Development Agency is an independent public benefit corporation created through state legislation at the request of one or more sponsoring municipalities. lDAs serve as financing conduits for local government to attract businesses to New York State, retain existing firms and enhance the state's competitive position. IDA's may serve as a vehicle through which large-scale wind development is financed.

As with the more specific wind energy exemption, all property titled to an IDA is exempt from real property, sales and mortgage taxes. Another parallel to the Section 487 exemption for wind energy systems, an lDA often negotiates payments in lieu of taxes (PILOTS) with the private developers participating in lDA projects.[15]

# 4. Assessment of the Legal Impact of Such Exemptions on School State-aid Formulas

### 4.1 Governance of Education in New York State

A brief description of the governance of education and school finance in New York State is helpful to comprehend the issue addressed in this paper. Budget authority for educational aid in New York State rests with the legislature and the executive branch, as it does in other states.[16] The Board of Regents is the policymaking body for all educational institutions in the state and the New York State Education Department.[17] The Regents can take positions on the impact of aid distributions and make aid

[14] Form RP-487 (9/02) - Application for Tax Exemption of Solar, Wind, or Farm Waste Energy Systems. See sample form following Exemption Profile. NYS Assessor's Manual, supra note 2, p. 20.05.
[15] The University of the State of New York, New York State Education Department, State Aid to Schools: A Primer, December 2000, at ii and iii [hereinafter SED, State Aid to Schools: A Primer]. See also NYS Comptroller Report, School Finance Reform --A Discussion Paper- October, 1995 [hereinafter Comptroller Report, School Finance Reform] available at http://www.osc.state.ny.us/reports/schools/1995/10-95.htm (citing to (School Law 1994), New York State School Boards Association, Albany, New York, p. 433).
[16] See James A Kadamus, Federal Formula Allocation For Schools: Historical Perspective and Lessons from New York State, Journal of Official Statistics, Vol. 18, No. 3, 2002, at 465.
[17] Members of the Board of Regents are appointed by a joint session of the Legislature. Id.

proposals independent of the executive and legislative branches. It is generally stated that "[a]lthough the regents have been influential in aid deliberations their relationship is advisory in nature."[18] Thus, within their essential roles, both the legislature and the executive branch govern education and determine school finance in New York State.

### 4.2 School Finance in New York State

According to the New York State Education Department, as of 2000, the state's public education funding came from three sources: approximately four percent (4%) from federal sources, forty four percent (44%) from State formula aids and grants, and fifty-two percent (52%) from revenues raised locally.[19] Local property taxes constitute close to ninety 90 percent of local revenues. State aid for the public schools comes primarily from the State General Fund (approximately 90 percent) wherein the major revenue source is state taxes (e.g. income and sales); the balance (approximately 10 percent) comes from a Special Revenue Fund account supported by lottery receipts.[20] The scheme can be summarized as follows:

> The major source of local revenue for education in all communities is the tax levied by boards of education on residential and commercial properties within the boundaries of each school district. Only the Big 5 cities have constitutional tax limits, and the limits apply to the total municipal budget. Small city school districts (those with a population of less than 125,000 inhabitants) had their constitutional tax limit repealed in 1985. Small city residents were not able to vote on their school budgets until legislation allowing it was passed in 1997...
>
> The State's sales tax laws reserve four percent for the State and permit localities to levy an additional three percent (four percent in the case of New York City and certain other municipalities). Eight counties share a portion of their sales tax with school districts, and are legally permitted to share certain other taxes. The non-property tax revenues derived from distribution of some portion of the local county sales tax are prorated based on the number of public school pupils residing in the county and enrolled in the various school districts partly or wholly located within the county.[21]

Thus, over half of the funds available for school districts come from local property taxes. As a general proposition, the wealthier the school district, the greater the spending on public schools. The close correlation between community wealth and resources available for education is underscored in a recent report of the State Education Department:

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[18] Id.
[19] SED, State Aid to Schools: A Primer, supra note 15, at i.
[20] Id. (All net revenues from the state lottery are statutorily earmarked for school aid. In addition, the General Fund guarantees the level of lottery funds appropriated for education, making up any shortfall in lottery revenues.).
[21] Id. at ii & iii. Small city school districts can impose a utility tax; about one quarter of the 57 small city districts do so. In addition, recent legislation requires that payments in lieu of taxes (PILOTS) be distributed proportionally among the taxing jurisdictions (including school districts) affected by tax exemptions granted by Industrial Development Agencies (IDAs). (School Law 1994), New York State School Boards Association, Albany, New York, p. 433). Id.

> The disparities in fiscal resources are due primarily to the varying ability and willingness of school districts to generate local property tax revenue. As in most states, property values of residences and businesses vary dramatically from school district to school district, as do local assessment practices, and the level of education services desired by the community. In short, a student's access to educational resources depends in large part on where he or she lives, raising serious concerns about the equity of student opportunities.[22]

New York's State Aid system, described more fully in Section 4.3.1 below is an attempt to redress this disparity. The School Aid system is based on the principle of wealth equalization. This holds that state aid is distributed "in inverse proportion to wealth in order to offset dramatic differences in the ability of local school districts to raise local revenue."[23] For example, in 1997-98, the New York State Education Department found that the wealthiest group of districts received an average of only $1,188 per pupil in State aid, while the poorest districts received $4,148. Nonetheless, even with State aid per pupil exceeding that of the wealthiest group of districts by 249 percent, the poorest group of districts cannot begin to approach the spending level of the wealthiest districts.[24]

## 4.3 Method for Distribution of State Aid to Schools

### 4.3.1 School Aid Formulae

The amount of state aid received by any school district is determined by a complex maze of thirty-seven formulae. Of these formulae, the most important relate to operating aid. As explained by the Court of Appeals of New York State:

> Almost half of the State aid component consists of operating aid, which is allocated using a complex statutory formula that apportions various categories of aid based on a district's Combined Wealth Ratio -- which measures its ability to generate revenue -- and student attendance (see *Education Law § 3602*). The statute contains extensive prescriptions regarding how districts may use funds, and it is perhaps the proliferation of highly specific aid categories that most differentiates the current *section 3602* from its shorter, simpler predecessors (see e.g. L 1962, ch 657). (emphasis added)

To understand the impact of an exemption for the increased valuation of wind systems on the amount of state school aid, it is important to disentangle the formulae for operating aid. At its most basic, operating aid is calculated as the product of:

[22] Id. See also the NYS State Aid web site at http://stateaid.nysed.gov/ (Go to the publications tab and towards the bottom of the screen you will see State Formula Aid and Entitlements for Schools in New York State.).
[23] SED, State Aid to Schools: A Primer, supra note 15, at 12.
[24] Id. at iii.

(Aid Per Pupil) X (Number of Pupils)

Aid Per Pupil reflects the school district's ability to meet the basic education needs of its students; by contrast the number of pupils is a proxy for need in providing effective education to all pupils.

Aid Per Pupil is a function of the "wealth" of the school district relative to the average wealth of all districts in the state combined. In turn, wealth is made up of two components: 1) the valuation of taxable real property; and 2) the adjusted gross income. This combined measure is known as the "General Wealth Ratio".

Tracing through, the wind system exemption will have the following directional impact on state school aid. The exemption will:

- *lower* the valuation of taxable real property; which will
- *lower* the "district wealth" relative to that of the rest of the state; which will
- *increase* the Aid Per Pupil; which will
- *increase* the Operating Aid provided by the State to the school district.

Thus, the incremental loss of assessed property value associated with a wind system will have two, contradictory effects. On the one hand, the exclusion of the wind system from the property tax rolls will mean that the local school district will not be able to tax this property at the applicable mill rate. On the other hand, the exemption will translate into more revenues provided by the state under the applicable state aid formula for Operating Aid.[25]

Finally, it is worth noting that the revenues received by the local taxing district from a wind developer pursuant to a negotiated PILOT are not factored into the formula for Operating Aid.[26] In a sense, the local school district has "the best of both worlds" – PILOT revenues coupled with greater state aid in the form of Operating Aid.[27]

### 4.3.2. "Save Harmless" Considerations

The formulas for calculating state aid to schools tell only part of the story. In order to prevent large swings in state school aid from year to year, many provisions have "hold harmless" clauses which ensure that the school district will not receive an amount less

[25] Whether the tax exemption is on net beneficial to the school district will depend upon the facts of a specific case.
[26] There is precedent for including the full value equivalent of PILOT payments received by the local taxing district to the assessed value for purposes of calculating state school aid. See New York Real Property Tax Law § 485. See also New York Education Law § 3602. According to Jim Dunne, Director of Tax Research, New York State Office of Real Property Services (email dated August 20, 2004), so far, the only PILOTS that have been converted to "actual valuation" equivalent have been those associated with few large exempt facilities such as nuclear power plants. It is noteworthy, however, that in the instant case the statute explicitly authorizes the use of PILOTS by local taxing districts. See New York Real Property Tax Law § 487 (9).
[27] Interview with Jim Dunne, Director of Tax Research, New York State Office of Real Property Services, April 6, 2004.

than received under the formula in the preceding year.[28] Additionally, in recent years, the legislature has not strictly adhered to the school aid formula in assigning state aid to individual school districts.[29]

### 4.4 School Finance Reform and its Potential Impact on the Wind Tax Exemption

School finance reform has been a topic of some controversy in New York State almost continuously since the 1960's.[30] The most significant legal development associated with the State formula aids in New York State, is the decision rendered by the Court of Appeals of New York State *In Campaign for Fiscal Equity v. The State of New York*.[31]

In *CFE*, The Court of Appeals ruled that the state constitution's mandate that "[t]he Legislature shall provide for the maintenance and support of a system of free common schools, wherein all the children of this state may be educated," [art. XI, ß [1]] was violated by the state's method of funding New York City's public schools. In a prior decision in 1995 in the case, the Court had held this provision required funds sufficient to provide a "sound basic education" and remanded for trial on that issue. After a lengthy trial, the State Supreme Court found the state's formula failed its purpose. The Appellate Division reversed, and the Court of Appeals, in turn reversed and essentially reinstated the trial court's judgment.

On September 3, 2003, the Governor of New York State issued Executive Order No.131 creating the New York State Commission on Education Reform.[32] The Governor charged the Commission with studying and recommending to the Executive and the Legislature suggested reforms to the education finance system in New York State and to any other State or local laws, rules, regulations, collective bargaining agreements, policies or practices, to ensure that all children have an opportunity to obtain a sound basic education, in accordance with the requirements of Article XI, Section 1 of the State Constitution and applicable State court decisions.

Other groups, special commissions, and legislative task forces have also taken up the issue and produced voluminous reports.[33] The issue of school funding remains today a central

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[28] Interview with Burt Porter, State Education Department, Director of Finance New York State Education Department, April 6, 2004. See also, SED, State Aid to Schools: A Primer, supra note 15, at 2.
[29] Id.
[30] Comptroller Report, School Finance Reform, supra note 15.
[31] 86 N.Y.2d 307 [1995].
[32] See e.g. New York State Commission for Education Report, Ensuring Children an Opportunity for a Sound Basic Education (2004)(known as the Zarb Commission Report). The link for the Commission Report is: http://www.state.ny.us/pdfs/finalreportweb.pdf. See also NYS Governor's Press Release on the Zarb Commission Report noting that "[o]ver the years, the State has added distribution formulas to the State aid system that have made it overly cumbersome and difficult to understand. Currently, there are thirty-seven categories of aid. The Commission's recommendations for changes in the State's school aid formula would make it fair, sustainable and understandable. If enacted, the Commission's recommendations would reduce the number of categories of aid to eleven." available at http://www.state.ny.us/governor/press/year04/march29_04.htm.
[33] There are many studies and reports on this matter. Find other reports and documents at: http://www.osc.state.ny.us/reports/schools/1996/10-96.htm; http://www.nyssba.org/; http://www.cfequity.org/; http://www.nysut.org/.

topic of ongoing negotiations between the Governor, the Speaker of the Assembly and the Senate Majority Leader.[34]

It is difficult to predict the state's response to the *CFE* decision and its bearing on the interaction between the statutory property tax exemption for wind and state school aid. Nevertheless, the following tentative conclusions can be ventured. The essence of the *CFE* decision is that the state is not providing sufficient state aid to ensure that students enrolled in New York City public schools receive a sound basic education. To address the perceived funding inequities, either local taxing districts will have to further tax local residents and businesses, or the state will have to further close the wide disparity in funding inequities through the state aid formula.

Placing additional tax burden on the local districts seems unlikely. As noted by the Zarb Commission:

> [I]f the State believes that deficient New York City fiscal effort contributed to educational problems in New York City, the State could mandate increased effort. However, previous efforts in New York to require a minimum local effort have been ineffective …
>
> In addition, based on extensive research, the Commission found that the vast majority of the states do not have local effort requirements. In fact, only eight states outside of New York do have specific local effort requirements in their public school funding structure. The Commission does not recommend that the State school finance system mandate any minimum local property tax effort, or local property tax increases.[35]

A more likely course is some recalibration of the school aid formula such that poorer districts will receive a greater proportion of the available school aid funds.[36] The latter course will necessarily place greater emphasis on the district's "wealth" relative to the state average, making the wind tax exemption more valuable from the standpoint of the local school district.

## 5. Conclusions and Recommendations

New York State law exempting eligible wind energy systems from property taxes will have an impact on the financial resources available to local taxing districts, including school districts, within which the project resides. While there are competing tendencies,

[34] See e.g. Michael Cooper, Albany Legislature Set to Adjourn Without Doing Much Legislating, N. Y. Times, June 21, 2004, Section A, Page 1, Column 5.
[35] Zarb Commission Report, supra note 32, at 28-29.
[36] See NYS Governor's Press Release on the Zarb Commission Report, supra note 32.noting that "[o]ver the years, the State has added distribution formulas to the State aid system that have made it overly cumbersome and difficult to understand. Currently, there are thirty-seven categories of aid. The Commission's recommendations for changes in the State's school aid formula would make it fair, sustainable and understandable. If enacted, the Commission's recommendations would reduce the number of categories of aid to eleven."

it is our conclusion that, under most circumstances, the wind energy exemption will have a **favorable** fiscal impact. This conclusion is supported by the following considerations:

- Over half of all financial resources available to school districts derive from revenues raised locally. The exemption of wind energy system equipment from the calculation of "assessed value" means that the school district will collect a lesser amount of property tax than if the equipment had been fully taxable.
- The tax loss associated with the wind energy exemption will be partially offset by any Payments in Lieu of Taxes the school district negotiates with wind developers. It is anticipated that PILOTS will be more germane to large, utility-scale systems than to smaller customer-sited wind projects.
- A further compensating factor is the positive influence of the wind energy exemption on the formula for calculating state school aid. While there are many state aid formulas, as a general rule, the lower the assessed value of District property per pupil, the greater the state aid; conversely, the greater the assessed value, the lower the state aid. However, because wind energy systems are not considered in the quantification of assessed value, the statutory exemption increases economic activity within the district while maintaining the status quo with respect to the school district's expected state aid.
- As a prominent example, nearly half of all state aid consists of Operating Aid, which is based on weighted attendance and wealth of school districts. The statutory exemption for wind energy systems means that the school district's "wealth" remains constant for purpose of the formula, and will receive the same level of school aid.
- At the time the wind-related property becomes part of the taxable property base, an increase in the assessed value of District property per pupil, results in lower state aid. Therefore, the impact of property tax incentives for wind development occurs, if at all, after the 15-year period.[37]
- When the statutory exemption expires, the wind farm will come on the rolls based on its depreciated value as a 15-year old asset. Thus, the financial impacts of the expiration of the tax exemption – both positive and negative – will attenuate over time.

The findings of this research indicate are no legal or economic barriers to the continued offering of the wind property tax exemption. However, there are two risks that could be mitigated or eliminated through legislation.

[37] If the wind equipment remains in the hands of the original developer, the wind equipment should be fully depreciated by Year 6 under the Modified Accelerated Cost Recovery System (MACRS). Under MACRS, wind property is currently provided a depreciation life of 5 years, substantially shorter than the 15 to 20 year depreciation lives of non-renewable power supply investments. Faster depreciation results in tax benefits early in a project's life, and is preferred by investors because an after-tax dollar is worth more today than in later years. <www.dsireusa.org>
If at the end of the depreciation period, the project were sold to another developer, the purchaser's basis for depreciation would be his cost to buy those used turbines. Under the mid-year convention, federal tax depreciation deduction for the first year would be 20%, the second year 32%, the third year 19.2%, the fourth year 11.52%, the fifth year 11.52%, and the sixth year 5.76%. E-mail correspondence from Edwin Ing, American Wind Energy Association, to Fred Zalcman, dated Sep, 1, 2004.

First, by its terms, the wind tax exemption only applies to systems constructed prior to 2006. Insofar as numerous wind projects around the state now in the developmental stage may not go on-line until after 2006, it is important to resolve any uncertainty over their expected property tax status. NYSERDA will need to carefully examine whether to continue of the property tax exemption in its current form given technological development, how tax incentives integrate with other available state and federal subsidies, clean energy[38] and air quality targets, and fiscal considerations among other issues.

Second, there is some risk that the full value equivalent of PILOTS will be accounted for in the calculation of state aid, although it would take special legislation to do so. The Real Property Tax Law should be amended to explicitly exempt PILOTS from inclusion in assessed value for purposes of the state school aid formula.

Finally, it must be underscored that, as of this writing, the Governor and the legislature have yet to agree on a response to the *Campaign for Fiscal Equity* imperative set out by the Court of Appeals for fundamental school finance reform. The findings and conclusions we reach herein could be invalidated depending upon the specific nature of the reforms worked out.

[38] State of New York, Public Service Commission, Case 03-E-0188 – Proceeding on Motion of the Commission Regarding a Retail Renewable Portfolio Standard, Recommended Decision, issued June 3, 2004.

## Appendix A

### Substance of Pertinent Statutory Provisions

**Section 487(2) of the Real Property Tax Law – Scope**
Real property which includes a solar or wind energy system or farm waste energy system approved in accordance with the provisions of this section shall be exempt from taxation to the extent of any increase in the value thereof by reason of the inclusion of such solar or wind energy system or farm waste energy system for a period of fifteen years. When a solar or wind energy system or components thereof or farm waste energy system also serve as part of the building structure, the increase in value which shall be exempt from taxation shall be equal to the assessed value attributable to such system or components multiplied by the ratio of the incremental cost of such system or components to the total cost of such system or components.

**Section 487(5) of the Real Property Tax Law – Time Requirements**
The exemption granted pursuant to this section shall only be applicable to solar or wind energy systems or farm waste energy systems which are (a) existing or constructed prior to July first, nineteen hundred eighty-eight or (b) constructed subsequent to January first, nineteen hundred ninety-one and prior to January first, two thousand six.

**Section 487(8) of the Real Property Tax Law – Local Option**
Notwithstanding the provisions of subdivision two of this section, a county, city, town or village may by local law or a school district, other than a school district to which article fifty-two of the education law applies, may by resolution provide that no exemption under this section shall be applicable within its jurisdiction with respect to any solar or wind energy system or farm waste energy system constructed subsequent to January first, nineteen hundred ninety-one or the effective date of such local law, ordinance or resolution, whichever is later. A copy of any such local law or resolution shall be filed with the state board and with the president of the authority.

**Section 487(1) of the Real Property Tax Law – Statutory Definitions**
(a) "Solar or wind energy equipment" means collectors, controls, energy storage devices, heat pumps and pumps, heat exchangers, windmills, and other materials, hardware or equipment necessary to the process by which solar radiation or wind is (i) collected, (ii) converted into another form of energy such as thermal, electrical, mechanical or chemical, (iii) stored, (iv) protected from unnecessary dissipation and (v) distributed. It does not include pipes, controls, insulation or other equipment which are part of the normal heating, cooling, or insulation system of a building. It does include insulated glazing or insulation to the extent that such materials exceed the energy efficiency standards required by law.

(b) "Solar or wind energy system" means an arrangement or combination of solar or wind energy equipment designed to provide heating, cooling, hot water, or mechanical,

chemical, or electrical energy by the collection of solar or wind energy and its conversion, storage, protection and distribution.

(c) "Authority" means the New York state energy research and development authority.

(d) "Incremental cost" means the increased cost of a solar or wind energy system or farm waste energy system or component thereof which also serves as part of the building structure, above that for similar conventional construction, which enables its use as a solar [fig 1] or wind energy or farm waste energy system or component.

**Section 487(3) of the Real Property Tax Law – Guidelines**
The president of the authority shall provide definitions and guidelines for the eligibility for exemption of the solar and wind energy equipment and systems and farm waste energy equipment and systems described in paragraphs (a) and (b) of subdivision one of this section.

**Section 487(4) of the Real Property Tax Law –Use Requirements**
No solar or wind energy system or farm waste energy system shall be entitled to any exemption from taxation under this section unless such system meets the guidelines set by the president of the authority and all other applicable provisions of law.

**Section 487(6) of the Real Property Tax Law – Application**
Such exemption shall be granted only upon application by the owner of the real property on a form prescribed and made available by the state board in cooperation with the authority. The applicant shall furnish such information as the board shall require. The application shall be filed with the assessor of the appropriate county, city, town or village on or before the taxable status date of such county, city, town or village. A copy of such application shall be filed with the authority.

**Section 487 (9) of the Real Property Tax Law – Payments in Lieu of Taxes**
*(Added, L 2002)*
(a) A county, city, town, village or school district, except a school district under article fifty-two of the education law, that has not acted to remove the exemption under this section may require the owner of a property which includes a solar or wind energy system which meets the requirements of subdivision four of this section**,** to enter into a contract for payments in lieu of taxes. Such contract may require annual payments in an amount not to exceed the amounts which would otherwise be payable but for the exemption under this section.

(b) The payment in lieu of a tax agreement shall not operate for a period of more than fifteen years, commencing in each instance from the date on which the benefits of such exemption first become available and effective.

## Appendix B

**System Descriptions, Eligibility Criteria and Guidelines for Calculating Exemptions for Wind Energy Systems**[39]

## System Description

Wind energy systems collect wind energy through a propeller or blade configuration, known as a rotor, and use that energy to drive a generator to produce electric power, to power a drive shaft for mechanical applications or to provide heat.

Electric generating wind energy systems may appear in varying use patterns. A wind energy system may be a property owner's sole, principal or supplementary source of electricity. Such a system may be isolated from the electric grid and connected to on-site storage or to another property owner's facilities for the sale of excess power, or it may be connected to a utility distribution line, enabling excess electricity to be sold to the utility or others and enabling supplemental or back-up power to be purchased from the utility. Further, a wind energy system may produce electricity solely or principally for sale to a utility or others (e.g., as in the case of a wind farm arrangement where multiple wind generators produce power for input to the utility grid), or be used as part of an electric utility generating system.

Typical components of an electric generating wind energy system include a rotor assembly which captures the wind energy; a generator and accessories which convert the mechanical energy of the spinning rotor into electrical energy; a tower and base which support the rotor and generator; control and regulation systems; power conditioning and transmission equipment; and, in some instances, storage batteries.

Mechanical wind energy systems are typically used in rural settings for pumping water for immediate use or for storage in a tank or pond. They may also be used in industrial process applications to provide direct mechanical drive. The major components of a mechanical wind energy system include a tower, pump, pump rod, rotor assembly and coupler.

Wind energy systems can also be used to produce thermal energy, either by direct mechanical heating of water in a water twister, or by generating electricity to operate resistance heaters which heat a thermal storage medium. The stored heat may be extracted and used for space heating, hot water or operation of an absorption chiller for cooling.

[39] New York State Energy Office, *Solar and Wind energy Systems: Definitions and Guidelines for Property Tax Exemptions, available at*: http://www.orps.state.ny.us/assessor/manuals/vol4/part1/section4.01/solar_report.pdf
Please note that this definitions guidelines booklet issued by the former Energy Office remains in full force and effect until modified or repealed by NYSERDA. Copies of the booklet may also be obtained from NYSERDA.

## Eligibility Criteria

To be eligible for the property tax exemption, a wind energy system must be equipped with overspeed controls. In addition, an electric generating wind energy system must be designed to produce not less than 250 watts of power in 25 mile per hour winds.

## Guidelines for Calculating the Amount of the Exemption

Eligible wind energy systems should qualify for an exemption an amount equal to the assessed value of the entire system, including the following components:

a) Wind turbines (including rotors, generators, pumps, power transmissions and controls) which collect the wind energy and convert it into electrical, mechanical or thermal energy;

b) Supporting towers, foundations, frames and bracing;

c) Electric wiring, switchgears and pipes to the point of storage or connection with a conventional system;

d) Power conditioning equipment;

e) Associated safety equipment and metering devices;

f) Storage devices used solely for the wind generated energy; and

g) Other connecting parts and components necessary for the operation of the system.