PILOT AGREEMENTS HAVE LIFTOFF: *CITY OF LARGO V. AHF-BAY FUND, LLC*

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I. INTRODUCTION

A payment in lieu of taxes ("PILOT") agreement is an agreement between a local government and a tax-exempt land owner to compensate the local government for some or all of the tax revenue that it loses due to the nature of the ownership or use of a particular property.[1] While such agreements have been used for decades in Florida,[2] their validity recently came under attack. After a long, arduous battle, the Florida Supreme Court upheld the validity of PILOT agreements.[3] The Court held that a PILOT agreement was a valid, binding contract, even though the payments it required were calculated in the same manner as ad valorem taxes (i.e., millage rate x assessed value).[4]

This Article first gives a background on PILOT agreements, the use of PILOT agreements throughout the country, and the

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1. Daphne A. Kenyon & Adam H. Langley, *The Property Tax Exemption for Nonprofits and Revenue Implications for Cities*, LINCOLN INST. OF LAND POL. 6 (Nov. 2011), https://www.urban.org/sites/default/files/publication/26756/412460-The-Property-Tax-Exemption-for-Nonprofits-and-Revenue-Implications-for-Cities.PDF [hereinafter Kenyon & Langley, *Property Tax Exemption for Nonprofits*].

2. *See generally* Housing Auth. of City of Poplar Bluff v. Eastwood, 736 S.W.2d 46 (Mo. 1987) (upholding a PILOT agreement between a housing authority and a tax collector).

3. City of Largo v. AHF-Bay Fund, LLC, 215 So. 3d 10, 14, 17 (Fla. 2017).

4. *Id.* at 14, 17.

status of Florida law on PILOT agreements prior to *City of Largo v. AHF-Bay Fund, LLC*. The Article then discusses the legal challenge to PILOT agreements in Florida raised by AHF-Bay Fund. This Part of the Article discusses the facts and legal issues in the Florida Supreme Court's *Bay Fund* decision. Finally, this Article expounds on how the *Bay Fund* decision may extend to other aspects of local government and real property law in Florida.

II. PILOT AGREEMENTS ABOUND

A. PILOT Agreements Throughout the Nation

PILOT agreements are not unique to Florida. They have long been used by local governments throughout the country.[5] All fifty states have laws providing ad valorem tax exemptions for land operated by certain nonprofit organizations.[6] Therefore, what all local governments share in common is that when property is operated by a nonprofit, they lose tax revenue the property would otherwise generate, yet still incur costs providing services to the property for which they are not compensated.[7]

The policy behind state laws granting property tax exemptions for nonprofits is to encourage the development of property that provides a public benefit.[8] While the local government where the property is located bears the entire loss, the services provided by nonprofits are often not geographically limited.[9] Therefore, the loss and burden to the local government may be disproportionate to the benefits it receives from the nonprofit's presence.

Furthermore, tax exemptions for nonprofits impose varying degrees of hardships on different local governments. Variables include the degree to which the local government relies on ad valorem taxes as a revenue source, and the number of landowning nonprofits and the amount of land they own.[10]

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5. *See generally* Daphne A. Kenyon & Adam H. Langley, *Payments in Lieu of Taxes: Balancing Municipal and Nonprofit Interests*, LINCOLN INST. OF LAND POL. (2010), https://www.lincolninst.edu/sites/default/files/pubfiles/payments-in-lieu-of-taxes-full_0.pdf (providing an overview of the implementation and regulation of PILOT agreements nationwide) [hereinafter Kenyon & Langley, *Payments in Lieu of Taxes*].

6. *Id.* at 2.

7. *Id.*

8. *Id.* at 10–11.

9. *Id.* at 2, 11.

10. *See generally* Kenyon & Langley, *Property Tax Exemption for Nonprofits*, *supra* note 1 (summarizing how nonprofit tax exemptions impact city budgets).

Because of these variables, local governments have taken different approaches to PILOT agreements. Some governments determine whether to negotiate PILOT agreements on a case by case basis, while others (typically those with a large number of nonprofits) implement PILOT programs.[11] PILOT agreements also vary considerably in their terms and structure.[12] For example, some call for a one-time payment, while others call for continuous payments over a period of time.[13] Indeed, many PILOT agreements are negotiated on an ad hoc basis.[14] The methods for calculating the payments also vary. Some PILOT agreements require payments that are based on the amount of taxes that would otherwise be due, while others are based on the costs of providing governmental services to the property.[15]

While there is little uniformity in the terms of PILOT agreements, generally they are a way to offset tax revenue losses and to compensate the government for the cost of providing services to the tax-exempt property.[16] Furthermore, one characteristic they all share is that they are voluntary.[17] There is no law in any jurisdiction requiring a nonprofit to enter into a PILOT agreement.

In the wake of the 2009 financial crisis, many local governments experienced a steep decline in ad valorem revenue.[18] Many have yet to recover. As a result, PILOT agreements have become increasingly used throughout the country as means to generate revenue.[19]

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11. *Id.* at 6–7. Indeed, even the federal government has a well-established PILOT program for making payments in lieu of taxation to local governments for properties owned by the federal government within the local government's jurisdiction. *See* 31 U.S.C. §§ 6901–6907 (2012).

12. Kenyon & Langley, *Payments in Lieu of Taxes*, *supra* note 5, at 6.

13. *Id.*

14. *Id.*

15. *Id.*

16. *Id.*

17. *Id.*

18. *See* The Fla. Legislature, *Data: Topics A to F*, OFF. OF ECON. & DEMOGRAPHIC RES., http://edr.state.fl.us/Content/local-government/data/data-a-to-z/a-f.cfm (last visited Mar. 6, 2018) (click Municipalities: CY 1995–2016 for data on ad valorem tax collection in Florida municipalities from 1995 to 2016).

19. Kenyon & Langley, *Payments in Lieu of Taxes*, *supra* note 5, at 6–9.

B. PILOT Agreements in Florida

1. Local Government Home Rule

There is only one statute in Florida discussing the concept of PILOT agreements.[20] However, this statute only applies to public housing authorities and only governs one method of calculating PILOT payments.[21] Therefore, an overview of home rule powers[22] in Florida is appropriate.

In *City of Boca Raton v. State*, the Florida Supreme Court recounted the history of municipal powers in Florida.[23] Under the 1885 Florida Constitution, the legislature had to delegate authority either in a general or special act in order to give power to municipalities.[24] The 1885 Florida Constitution further provided under Article VIII, Section 8, in part, that: "[t]he Legislature shall have power to establish and to abolish municipalities, to provide for their government, to prescribe their jurisdiction and powers, and to alter or amend the same at any time."[25] Under the 1885 Florida Constitution, powers not expressly granted under the Constitution to municipalities were deemed to be a reservation of authority to the legislature, called "Dillon's Rule,"[26] as expressed in John F. Dillon's *The Law of Municipal Corporations*.[27] In accordance with the 1885 Constitution, Florida courts routinely followed Dillon's Rule.[28]

Under the 1885 Constitution, a municipality was powerless if the legislature did not grant it the authority needed to act in a

20. FLA. STAT. § 423.02 (2017).
21. *Id.*
22. FLA. CONST. art. VIII, § 2(b).
23. 595 So. 2d 25, 27 (Fla. 1992).
24. *Id.*
25. *Id.* (quoting FLA. CONST. art. VIII, § 8 (1885), *amended as* FLA. CONST. art. VIII, § 2(b) (1968)).
26. *Id.*
27. JOHN F. DILLON, THE LAW OF MUNICIPAL CORPORATIONS § 55 (1872).
28. *City of Boca Raton*, 595 So. 2d at 27; *see, e.g.*, Williams v. Town of Dunnellon, 169 So. 631, 637 (Fla. 1936) (holding that when a question arises about the existence of a power of a county, district, or municipality, the question should be resolved against the county, district, or municipality); Heriot v. City of Pensacola, 146 So. 654, 655 (Fla. 1933) (recognizing that the legislature has the authority to prescribe the powers of municipalities); Amos v. Mathews, 126 So. 308, 320 (Fla. 1930) (holding that all local powers must have their origin in a grant by the state); Malone v. City of Quincy, 62 So. 922, 924 (Fla. 1913) (holding a city ordinance regulating earth closets outside the city's express grant of power invalid).

desired manner.[29] For example, a municipality was not able to raise revenue through the imposition of a tax unless the state legislature imposed such a tax or delegated the authority to do so directly to the municipality.[30]

When the Florida Constitution was revised in 1968, municipalities, charter counties, and non-charter counties were all granted home rule power.[31] This new provision in essence reversed the way municipalities derived their powers. "Talbot D'Alemberte, the reporter for the Constitutional Revision Commission, explained: 'The apparent difference is that under the new language, all municipalities have governmental, corporate[,] and proprietary powers unless provided otherwise by law, whereas under the 1885 Constitution, municipalities had only those powers expressly granted by law.'"[32] Early court decisions restrictively interpreting these constitutional provisions prompted the legislature to enact the Municipal Home Rule Powers Act in 1973, which makes it clear that the cities have the authority to take any action as long as it is for a municipal purpose and not specifically prohibited by a statutory or constitutional provision.[33] Thereafter, Florida law has acknowledged the vast breadth of municipal home rule power.

With the adoption of the 1968 Constitution and enactment of the Municipal Home Rule Powers Act, municipalities are no longer dependent upon affirmative statutory authority to take action.[34] Because there is no statute or constitutional provision expressly prohibiting cities from entering PILOT agreements, it is a home rule decision for a city to enter into a PILOT agreement.

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29. *See, e.g.*, *Amos*, 126 So. at 319–20 ("If the Legislature has the power to levy the tax, it has the power to prescribe the use to be made of the revenue, so long as the use so prescribed is consistent with the Constitution.").

30. *Id.* at 318.

31. FLA. CONST. art. VIII, §§ 1(f)–(g), 2(b); *see City of Boca Raton*, 595 So. 2d at 27 (explaining that "[a]s Florida's population began to boom after World War II, the legislature was flooded with local bills and population acts designed to permit municipalities to provide solutions to local problems," which resulted in the 1968 Florida Constitution's grant of home rule powers to municipalities).

32. Susan Churuti, Chris Roe, Ellie Neiberger, Tyler Egbert & Zach Lombardo, *The Line Between Special Assessments and Ad Valorem Taxes:* Morris v. City of Cape Coral, 45 STETSON L. REV. 471, 476–77 (2016) (quoting *City of Boca Raton*, 595 So. 2d at 27 (quoting § 26A FLA. STAT. ANN. 292 (1970) (commentary by Talbot "Sandy" D'Alemberte))).

33. FLA. STAT. § 166.021 (2011).

34. *City of Boca Raton*, 595 So. 2d at 28.

2. Florida Law on PILOT Agreements Prior to City of Largo v. AHF-Bay Fund

Prior to the Florida Supreme Court's ruling in *Bay Fund*, there were few Florida legal authorities addressing the validity of PILOT agreements. Florida PILOT agreements were only recognized as legal in certain Florida statutes, bankruptcy cases, and IRS rulings.[35]

Although PILOT agreements have been used in Florida for many years, it was only recently that their validity was challenged and litigated.

III. THE BAY FUND *CASE*

A. Background Facts

> [T]he property [at issue in the *Bay Fund* case] was operated as a residential apartment complex and subject to ad-valorem property taxes. In 2000, a non-profit housing provider, RHF Brittany Bay, LLC ("Brittany Bay"), sought to buy the property and turn it into an affordable housing development under chapter 420, Florida Statutes. [R]eal estate operated as affordable housing by a non-profit entity is exempt from ad-valorem taxation.[36]
>
> To finance the housing project at low-cost, Brittany Bay asked the City to allow Capital Trust Agency (a limited purpose public entity) to issue tax-exempt bonds . . . under the City's bonding authority. While the statute at that time required Brittany Bay to obtain the City's permission, the City was not required to consent [to the financing]. Brittany Bay could finance the housing project with . . . traditional lenders, although at a higher cost than tax-exempt bonds.
>
> To induce the City to authorize the bond issuance, Brittany Bay entered [into a PILOT] agreement with the City to make annual payments . . . equal [to] the amount of property taxes the City would have received from the property if it were not

35. *See* FLA. STAT. § 423.02 (2017) (providing for public housing authorities to make payments in lieu of taxes); In re Atl. Cmty. Care, Inc., 325 B.R. 661, 662 (Bankr. M.D. Fla. 2005) (recognizing PILOT agreement of a nonprofit tax-exempt entity as a valid unsecured claim in bankruptcy); IRS Private Letter Ruling No. 200730012, 2007 WL 2154916 (July 27, 2007) (recognizing PILOT payments as deductible).

36. FLA. STAT. § 196.1978 (2017) (affordable housing property tax exemption).

> exempt ("PILOT Agreement"). Capital Trust Agency [then] issued tax-exempt bonds to fund the purchase and rehabilitation needed to make the property suitable for affordable housing. Since then, the property has been operated as an affordable housing project.
>
> **The PILOT Agreement [Between the City and Brittany Bay]**
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> The PILOT Agreement state[d] that Brittany Bay entered it voluntarily for the purpose of inducing the City to authorize tax-exempt bonds to finance the affordable housing project. By authorizing the bonds, the City enabled Brittany Bay to purchase and rehabilitate the property so the property could "provide safe and affordable housing for persons of low and moderate income." The City also agreed to provide services to the property. . . .
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> The PILOT Agreement include[d] a legal description of the property [and] provide[d] that it [was] binding on Brittany Bay's successors, assigns, transferees, and grantees. [It also stated that it would remain] in effect as long as it [met] both requirements of the affordable housing property tax exemption under section 196.1978[, Florida Statutes]: (i) [the property was] operated as an affordable housing development (ii) by a nonprofit entity.
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> . . .
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> **Memorandum of Agreement Recorded in County Official Records**
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> At the same time Brittany Bay and the City entered the PILOT Agreement, they also executed a memorandum of agreement. The Memorandum was recorded in [the county's] official records in February 2001, as required by . . . the PILOT Agreement. . . . [T]he Memorandum state[d] that the PILOT Agreement [was] "maintained in the office of the City Clerk," and "available for reading and review by interested persons at the office of the City Clerk during that office's regular business hours." [T]he Memorandum [further] explain[ed]:
>
> "This Memorandum is being recorded to give constructive notice to third parties that the City and the Owner have entered into the Agreement, and the ***Agreement imposes*** certain

covenants which run with the title to the Property and are ***binding*** upon ***all persons now and/or hereafter owning title*** or having any interest in title to the Property. ***Prospective purchasers***, tenants, and lenders interested in each Property or improvements thereon are ***advised to make such review of the Agreement as they deem necessary or appropriate***."

. . .

Brittany Bay Convey[ed] the Property to AHF

[AHF-Bay Fund, LLC, an affordable housing provider like Brittany Bay, purchased the property from Brittany Bay in 2005]. Its decision to do so was based on the property's use as an affordable housing development. AHF . . . operated the property as an affordable housing development continuously since [the purchase].

[Originally,] Brittany Bay entered a Purchase and Sale Agreement with [a different entity prior to the purchase]. [That entity] then assigned the Purchase and Sale Agreement to AHF.

The Purchase and Sale Agreement gave the purchaser various due diligence and investigation rights. Brittany Bay had to produce many types of documents—including all operating statements and monthly income/expense reports for the property—automatically without waiting for a request from the purchaser. Other documents—including "all existing contracts [and] agreements . . . affecting the property"—were available for inspection on request. The purchaser could cancel the sale if it was "dissatisfied" with the results of its investigation "for any reason and in Purchaser's exclusive judgment."

The PILOT payments were listed as a separate line item in Brittany Bay's operating statements for the property, which were produced to [the original entity to the Purchase and Sale Agreement] before [it] was assigned to AHF.

[The original entity] provided the operating statement and income/expense reports to AHF. However, AHF claim[ed] it did not learn of the PILOT Agreement by reviewing the documents received from [the assignor], by exercising its right to inspect contracts relating to the property, or [through] a title search.

> The sale closed and Brittany Bay conveyed the property to AHF by special warranty deed . . . . Brittany Bay repaid the [Capital Trust Agency] bonds when the sale closed.
>
> **AHF Fail[ed] to Make PILOT Payments**
>
> Brittany Bay made [timely] payments [under the PILOT Agreement each year it owned the property].[37]

AHF failed to make any payments that came due after it purchased the property.[38]

B. The Trial Court Enforced the PILOT Agreement as a Covenant Running with the Land

The City filed suit for "breach of contract, quantum meruit, . . . and enforcement of the PILOT Agreement as a covenant running with the [land]."[39] At the trial court, the City prevailed on liability at the summary judgment phase.[40] The trial court ruled the PILOT Agreement was enforceable against AHF as a covenant running with the land.[41] The trial court then held evidentiary hearings on damages and entered a final judgment in favor of the City for $695,158.23.[42]

C. The Second District Court of Appeal Found the PILOT Agreement to Be Contrary to Florida Law and Public Policy

AHF appealed to the Second District Court of Appeal, arguing, inter alia, that the PILOT Agreement was not a covenant running with the land and that the PILOT Agreement was contrary to Florida law and public policy.[43] The Second District found AHF's

37. Answer Brief of Appellee at 2–7, AHF-Bay Fund, LLC v. City of Largo, 227 So. 3d 740 (Fla. 2d Dist. Ct. App. 2017) (July 11, 2014) (No. 2D14-408) (internal citations omitted) [hereinafter Answer Brief of Appellee].

38. City of Largo v. AHF-Bay Fund, LLC, 215 So. 3d 10, 14 (Fla. 2017).

39. Answer Brief of Appellee, *supra* note 37, at 7.

40. Order Granting Plaintiff City of Largo's Amended Motion for Partial Summary Judgment as to Counts II and V at 1, City of Largo v. RHF Brittany Bay, LLC, 2013 WL 12183826 (Fla. Cir. Ct.) (Apr. 29, 2013) (No. 2010CA017299).

41. *Id.*

42. *AHF-Bay Fund*, 215 So. 3d at 14.

43. AHF-Bay Fund, LLC v. City of Largo, 169 So. 3d 133, 134 (Fla. 2d Dist. Ct. App. 2015).

argument that the PILOT Agreement was not a covenant running with the land lacked merit.[44]

However, the Second District reversed, concluding that PILOT agreements that calculate payments by the amount of ad valorem taxes a government entity would have received but for a tax exemption are invalid.[45] Specifically, the Second District concluded that: (1) the payments under the PILOT Agreement were, in substance, disguised ad valorem taxes;[46] and (2) the City did not have authority to impose taxes in circumvention of the affordable housing tax exemption.[47] Therefore, the court held that the PILOT Agreement was void as against public policy and violated Article VII, Section 9(a) of the Florida Constitution, which provides that cities may impose taxes only as permitted by law.[48]

The Second District acknowledged that because PILOT agreements are "abound in municipalities throughout Florida[,] . . . the magnitude of [its] opinion . . . may pose a significant hardship on municipalities."[49] Therefore, the court certified the following question to the Supreme Court:

> DO PILOT AGREEMENTS THAT REQUIRE PAYMENTS EQUALING THE AD VALOREM TAXES THAT WOULD OTHERWISE BE DUE BUT FOR A STATUTORY TAX EXEMPTION VIOLATE SECTION 196.1978, FLORIDA STATUTES (2000), AND ARTICLE VII, § 9(a) OF THE FLORIDA CONSTITUTION?[50]

D. The Case Before the Florida Supreme Court

The Florida Supreme Court accepted discretionary jurisdiction.[51] Before the Court, the City took issue with the Second District's characterization of the PILOT payments as an impermissible tax and that the PILOT Agreement was void as against public policy.[52]

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44. *Id.*
45. *Id.* at 138.
46. *Id.* at 136.
47. *Id.* at 138.
48. *Id.*
49. *Id.*
50. *Id.*
51. City of Largo v. AHF-Bay Fund, LLC, 215 So. 3d 10, 13 (Fla. 2017).
52. Answer Brief of Appellee, *supra* note 37, at 31–32; Petitioner's Initial Brief at 10, 15, AHF-Bay Fund, LLC v. City of Largo, 215 So. 3d 10 (Fla. 2017) (Jan. 11, 2016) (No. SC15-1261) [hereinafter Petitioner's Brief].

"What constitutes a 'tax' [is] well established" in Florida.[53] "[A] tax is an enforced burden imposed by sovereign right for the support of the government, the administration of law, and the exercise of various functions the sovereign is called on to perform."[54]

The City argued it did not unilaterally impose any obligation by sovereign right; the payments under the PILOT Agreement were not for the purpose of supporting routine government functions; and the PILOT Agreement actually supported matters of public policy in Florida—including freedom of contract and promoting affordable housing.[55]

In opposition, AHF argued the payments were nothing more than a tax in disguise because payments under the PILOT Agreement were calculated in the same manner as ad valorem taxes; the PILOT Agreement violated the affordable housing ad valorem exemption statute; and the PILOT Agreement was against the public policy to promote affordable housing.[56]

E. The Florida Supreme Court's Decision

The Supreme Court "answer[ed] the certified question in the negative and quash[ed] the decision of the Second District."[57] The Court held that voluntary PILOT agreements are not a "tax" under Florida law—even if payments under the agreement are calculated in the same manner as taxes.[58] The Court further held that PILOT agreements support Florida's public policy to promote affordable housing and freedom of contract.[59]

In doing so, the Court expounded on and clarified many aspects of municipal government and local government law, providing valuable precedent for local governments throughout Florida.

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53. *AHF-Bay Fund*, 215 So. 3d at 16.

54. State v. City of Port Orange, 650 So. 2d 1, 3 (Fla. 1994) (citing Klemm v. Davenport, 129 So. 904, 907 (Fla. 1930)); City of Boca Raton v. State, 595 So. 2d 25, 29 (Fla. 1992).

55. Petitioner's Brief, *supra* note 52, at 11–12, 15.

56. Respondent's Answer Brief at 17–18, 20, City of Largo v. AHF-Bay Fund, LLC, 215 So. 3d 10 (Fla. 2017) (Mar. 7, 2016) (No. SC15-1261).

57. *AHF-Bay Fund*, 215 So. 3d at 17.

58. *Id.*

59. *See id.* at 16 (referencing a policy of favorable affordable housing to low-income families by enabling the owner to receive the financing necessary for an apartment complex and stressing a strong public policy of the freedom of contract between two parties).

IV. THE BAY FUND *PRECEDENT AND REACHING EFFECTS*

A. Taxes Are Imposed by Sovereign Right

In the *Bay Fund* decision, the Court explicitly recognized that "[l]ocal governments operate in several different capacities."[60] Thus, even though a city is a government, this does not mean that every time it acts it does so "by sovereign right." A city's proprietary actions (i.e., when it acts as a party to a contract) are separate and distinct from its governmental actions (i.e., when it acts by sovereign right).[61] For payments to constitute an unconstitutional tax, they must be imposed by sovereign right.[62]

The Court recognized that "the City did not unilaterally impose any obligation[ ]" to make payments under the PILOT Agreement by sovereign right.[63] In the PILOT Agreement, Brittany Bay and the City agreed that, in exchange for the City's agreement to authorize tax-exempt bonds, Brittany Bay would provide consideration.[64] The parties concurred that the consideration would be calculated as the amount the City would have received in ad valorem taxes if the property was not converted to affordable housing.[65] The parties even negotiated and included a provision for determining the amount of Brittany Bay's payment if their agreed-upon method was held invalid.[66] Thus, Brittany Bay's obligation arose solely by virtue of a bargained-for, bilateral agreement.[67]

The Court concluded that the City entered into the PILOT Agreement in its proprietary capacity and Brittany Bay "made a voluntary decision to subject itself to [such] payments."[68] Therefore, such payments did not constitute a tax for the purposes of Article VII, Section 9(a) of the Florida Constitution.

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60. *Id.* at 17 (citing Daly v. Stokell, 63 So. 2d 644, 645 (Fla. 1953); Commercial Carrier Corp. v. Indian River Cnty., 371 So. 2d 1010 (Fla. 1979)).

61. *See id.* (comparing a local government's proprietary actions to the actions of Brittany Bay to entering into a PILOT Agreement).

62. *Id.*

63. *Id.*

64. *Id.* at 13.

65. *Id.* at 16.

66. Petitioner's Brief, *supra* note 52, at 2–3.

67. *AHF-Bay Fund*, 215 So. 3d at 16.

68. *Id.* at 15.

This clear precedent is important for cities. It reinforces a local government's ability to enforce its contractual obligations without fear that such enforcement will be rendered an unconstitutional tax simply because it is a contracting party with certain sovereign rights. A voluntary, contractual obligation by a private party to pay the City, in any amount, does not invoke the City's Article VII, Section 9(a) power to impose taxes.

B. Taxes Are Imposed to Support General Government Functions

The *Bay Fund* Court further acknowledged that authorizing tax-exempt bonds is not a general government function.[69] Brittany Bay needed financing to convert the property to an affordable housing project.[70] It could have financed the project in any number of ways from any number of sources, but Brittany Bay wanted to use tax-exempt bonds.[71] So, it asked the City to allow the issuance of the bonds.[72] The Court explicitly recognized that this was a "non-routine service" provided specifically to Brittany Bay as consideration for the PILOT Agreement—not a general government function.[73]

The Court further dispelled AHF's argument that the City rendered such payments a tax by using the PILOT payments it received from Brittany Bay as general revenue.[74] Not only did the Court recognize that AHF had no evidence to support this argument, it dismissed the argument as nothing more than AHF taking issue with the value of the consideration provided to the City for the PILOT Agreement compared to AHF's perceived benefit.[75]

This conclusion insulates the practice of depositing contractual payments into a general fund without fear that such accounting automatically renders such contractual payments an unconstitutional tax.

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69. *Id.* at 17.
70. *Id.* at 13.
71. *Id.*
72. Petitioner's Brief, *supra* note 52, at 1.
73. *AHF-Bay Fund*, 215 So. 3d at 17.
74. *Id.*
75. *Id.*

C. Just As a Tax by Any Other Name Is a Tax, a Payment Made Under a Bargained-For Agreement Is a Contractual Payment—Not a Tax

There are numerous distinctions between taxes and the contractual payments due under the PILOT Agreement:

Tax	**Contractual Payment**
Mandatory, unilaterally imposed by government[76]	Voluntarily, mutually agreed to[77]
No particular benefit to any specific person or property[78]	Consideration in exchange for benefit to contracting party[79]
Super-priority lien[80]	Unsecured obligation
Billed and collected by county tax collector[81]	Paid directly to contracting party
Enforceable extra-judicially through tax certificate[82] and tax deed procedures[83]	Enforceable only through judicial system[84]

> The payments under the PILOT Agreement [met] none of the [above] criteria to be considered a "tax." The PILOT payments [were] not imposed unilaterally by the City, [were not used for routine government functions,] [were] not entitled to super-priority lien status, [were] not collectable as taxes, and could not be enforced through the tax certificate or tax deed process.

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76. *See* Klemm v. Davenport, 129 So. 904, 907 (Fla. 1930) ("A 'tax' is an enforced burden of contribution imposed by sovereign right . . . .").

77. *AHF-Bay Fund*, 215 So. 3d at 15.

78. *See Klemm*, 129 So. at 907 (contrasting special assessments with taxes by stating that special assessments are "imposed upon the theory that that portion of the community which is required to bear it receives some special or peculiar benefit in the enhancement of value of the property against which it is imposed as a result of the improvement made with the proceeds of the special assessment").

79. *AHF-Bay Fund*, 215 So. 3d at 16–17.

80. FLA. STAT. § 197.122 (2017).

81. FLA. STAT. § 197.332 (2017).

82. FLA. STAT. § 197.432 (2017).

83. FLA. STAT. § 197.552 (2017).

84. *See* Answer Brief of Appellee, *supra* note 37, at 34 ("As illustrated by the very existence of this case, a delinquent PILOT payment cannot be enforced extra-judicially by selling a tax certificate (evidencing a lien with super-priority status) and eventually, selling the property through a tax deed sale.").

> Nevertheless, the Second District . . . concluded that the PILOT payments were ad valorem taxes disguised under another name. The Second District arrived at this conclusion—not by analyzing the above criteria of taxes—but by isolating and misapplying a single principle from [the] Court's [prior] *Port Orange* decision: that the power to tax cannot be broadened by semantics.[85]

The Court explicitly addressed this error by the Second District and held that a payment under a bargained for, voluntary agreement is not a "tax."[86]

D. A Voluntary PILOT Agreement Is Not Void Against Public Policy

> A court may [only] declare a contract void as against public policy in very limited circumstances. A contract is void as against public policy only if it is "clearly injurious to the public good" or "contravene[s] some established interest of society."[87] . . . "Courts . . . should be guided by the rule of extreme caution when called upon to declare transactions void as contrary to public policy and should refuse to strike down contracts involving private relationships on this ground, ***unless it be made clearly to appear that there has been some great prejudice to the dominant public interest sufficient to overthrow the fundamental public policy of the right to freedom of contract between parties sui juris***."[88]

> [The Court recognized that] PILOT agreements are not void as against public policy since: (1) PILOT agreements are not prohibited under any constitutional or statutory provision and tax exemptions are fully waivable; and (2) PILOT agreements actually support and advance other valuable public policies[, including freedom of contract.][89]

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85. Petitioner's Brief, *supra* note 52, at 13–14; *see* AHF-Bay Fund, LLC v. City of Largo, 169 So. 3d 133, 138 (Fla. 2d Dist. Ct. App. 2015) (holding the PILOT agreement's language "was attempting to recoup the ad valorem taxes under a different name").

86. City of Largo v. AHF-Bay Fund, LLC, 215 So. 3d 10, 17 (Fla. 2017).

87. Fla. Windstorm Underwriting v. Gajwani, 934 So. 2d 501, 506 (Fla. 3d Dist. Ct. App. 2005).

88. *Id.* at 506–07 (quoting Banfield v. Louis, 589 So. 2d 441, 446–47 (Fla. 4th Dist. Ct. App. 1991)).

89. Petitioner's Brief, *supra* note 52, at 15–16; *see AHF-Bay Fund*, 215 So. 3d at 15–16 (discussing the public policies that support the use of PILOT agreements).

1. PILOT Agreements Are Not Prohibited Under Any Constitutional or Statutory Provision

> The Second District's opinion [was] flawed in [a] major way—it mischaracterized the statutory tax exemption in section 196.1978, Florida Statutes, enjoyed by affordable housing providers. The Second District state[d]: "section 196.1978 expressly prohibits ad valorem taxation on properties being used for affordable housing[.]"[90] . . .
>
> [As the *Bay Fund* Court recognized,] Section 196.1978 does not "prohibit" ad valorem taxation on affordable housing projects. It simply says that an affordable housing project owned by a 501(c)(3) entity is "exempt from ad valorem taxation to the extent authorized under s. 196.196."[91] Section 196.1978 then says that the owner of the affordable housing project must take affirmative steps to enjoy the benefit of the tax exemption—including that the owner "must comply with the criteria provided under s. 196.195 for determining exempt status and applied by property appraisers on an annual basis."[92] The statute does not make the exemption automatic or "prohibit" ad valorem taxation on affordable housing projects owned by 501(c)(3) entities.
>
> Tax exemptions do serve a public interest, but they are not sacred. Tax exemptions can be waived. Indeed, a property owner need only forget to timely file its annual form with the property appraiser to lose its exemption for that year. Since exemptions may be waived, [a PILOT agreement does not violate the statute providing for a tax exemption.][93]

90. AHF-Bay Fund, LLC v. City of Largo, 169 So. 3d 133, 136 (Fla. 2d Dist. Ct. App. 2015).

91. FLA. STAT. § 196.1978 (2017).

92. *Id.*

93. Petitioner's Brief, *supra* note 52, at 16–17 (citations omitted); *see, e.g.*, Sowell v. Panama Commons L.P., 192 So. 3d 27, 31 (Fla. 2016) (noting that tax exemption is contingent on many factors, including something as simple as failing to timely file an application); Hous. Auth. of City of Poplar Bluff v. Eastwood, 736 S.W.2d 46, 47 (Mo. 1987) (because tax exemptions can be waived, PILOT agreement between city and housing authority did not violate public policy); Clark v. Marian Park, Inc., 400 N.E.2d 661, 664–65 (Ill. App. Ct. 1980) (nonprofit owner of affordable housing project waived tax exemption by agreeing to pay taxes in annexation agreement with city); *see* FLA. STAT. § 196.011 (2017) ("Failure to file a complete application by [the deadline] constitutes a waiver of the exemption privilege for that year . . . .").

The Court likened the PILOT Agreement to the Supreme Court of Missouri's decision in *Housing Authority of Poplar Bluff v. Eastwood*.[94] The *Eastwood* court

> concluded that a PILOT agreement between a city and a tax-exempt housing authority did not violate public policy precisely because tax exemptions are waivable.[95] ["]The PILOT agreement [there] expressly acknowledged that the housing project was exempt from taxes.["][96] The housing authority nonetheless agreed to make payments in lieu of taxes in exchange for the city providing general municipal services. In rejecting the argument that the agreement was void as against public policy, the Missouri Supreme Court reasoned that courts throughout the country have held that tax exemptions are waivable, and that the agreement showed that the housing authority made a voluntary decision to subject itself to payments notwithstanding its exempt status.[97]

2. PILOT Agreements Support and Advance Other Valuable Public Policies

> Since there is no constitutional or statutory prohibition [against PILOT agreements], the Court may only strike down the parties' contract as void against public policy if it clearly injures the public good or contravenes some established interest of society. [PILOT agreements pose] no such injury . . . . To the contrary, [the Court held that] PILOT agreements support and advance other valuable public policies–such as affordable housing and freedom of contract.[98]

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94. *AHF-Bay Fund*, 215 So. 3d at 15.

95. *Eastwood*, 736 S.W.2d at 47–48.

96. *AHF-Bay Fund*, 215 So. 3d at 15.

97. Petitioner's Brief, *supra* note 52, at 17–18; *see Eastwood*, 736 S.W.2d at 47 (citing Sprik v. Regents of Univ. of Michigan, 204 N.W.2d 62, 68 (Mich. Ct. App. 1972) (public university could waive property tax exemption)); Christian Bus. Men's Comm. of Minneapolis v. State, 38 N.W.2d 803, 812 n.7 (Minn. 1949) ("Failure to use due diligence in asserting a right to tax exemption may constitute a waiver of the right."); Rutgers Chapter of Delta Upsilon Fraternity v. City of New Brunswick, 28 A.2d 759, 761 (N.J. 1942) (taxpayer waived tax exemption by failing to claim exemption in manner required by statute and voluntarily paying taxes); *Clark*, 400 N.E.2d at 664–65.

98. Petitioner's Brief, *supra* note 52, at 19.

3. PILOT Agreements Support Affordable Housing

"[T]he Second District recognized . . . [the] strong public policy of 'promoting the provision of affordable housing for low to moderate income families.'"[99] "But it overlooked the role that the PILOT Agreement played in furthering that strong public policy."[100]

The *Bay Fund* Court correctly recognized that "[t]he PILOT Agreement was the catalyst, not a hindrance, to Brittany Bay acquiring and converting the property to affordable housing."[101] Thus, the PILOT Agreement supports—not violates—this public policy.

4. PILOT Agreements Support Freedom of Contract

> There is also a strong, long-standing public policy favoring freedom of contract. "Freedom of contract is the general rule."[102] "[I]t is a matter of great public concern that freedom of contract be not lightly interfered with."[103] "[R]estraint is the exception, and when it is exercised to place limitations upon the right to contract . . . it can be justified only by exceptional circumstances."[104] . . .
>
> [The Court recognized that] the City and Brittany Bay entered into a voluntary agreement, supported by valid consideration. ["]The parties agreed on the method of calculating the consideration for their agreement and, until 2005, performed their respective obligations.["][105] The Court [could] not destroy the parties' freedom of contract simply because the parties have mutually agreed to calculate the payments by using the ad valorem rate as an objective measurement.[106]

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99. *AHF-Bay Fund*, 215 So. 3d at 16.
100. Petitioner's Brief, *supra* note 52, at 19.
101. *Id.*
102. State ex rel. Fulton v. Ives, 167 So. 394, 399 (Fla. 1936).
103. Bituminous Cas. Corp. v. Williams, 17 So. 2d 98, 101 (Fla. 1944).
104. *Ives*, 167 So. at 399.
105. City of Largo v. AHF-Bay Fund, LLC, 215 So. 3d 10, 16 (Fla. 2017).
106. Petitioner's Brief, *supra* note 52, at 20; *see AHF-Bay Fund*, 215 So. 3d at 16 (discussing the nature of the agreement between the City and RHF).

E. Potential Effects on Real Estate Law

Upon remand to the Second District following the Florida Supreme Court's decision, AHF requested that the Second District address an issue it raised tangentially to the district court in the first appeal—whether an affirmative covenant running with the land that requires the payment of money can ever be enforced against a successive property owner through a personal judgment for breach of contract, as opposed to solely *in rem* remedies.[107] AHF argued that it could not be held personally liable for breaching the PILOT Agreement because "it was not a party to or a third-party beneficiary of the contract and because it did not assume or agree to the terms of the contract."[108]

The Second District rejected AHF's argument.[109] The court explained that, "[a] breach of contract action may be based on a party's breach of a covenant."[110] At a minimum, AHF was on constructive notice of the PILOT Agreement when it purchased the property because the memorandum of agreement—which specifically referenced the PILOT agreement and stated that it imposed covenants on the land—was recorded in the property records.[111] Even where a restrictive agreement is unrecorded, a purchaser who takes the property with notice of the unrecorded agreement is bound by it.[112] Therefore, even if the PILOT Agreement was not a covenant running with the land, it was binding on AHF.[113] Finally, the Second District noted that, even if AHF lacked constructive notice of the PILOT Agreement, it would not change the court's conclusion that it was binding on AHF.[114] The court had already concluded that the PILOT Agreement was a covenant running with the land, and a covenant running with the land is binding on subsequent purchasers regardless of notice.[115]

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107. AHF-Bay Fund, LLC v. City of Largo, 227 So. 3d 740, 742 (Fla. 2d Dist. Ct. App. 2017).
108. *Id.* at 742.
109. *Id.*
110. *Id.*
111. *Id.* at 742–43.
112. *Id.* at 743.
113. *Id.*
114. *Id.*
115. *Id.*

Therefore, the Second District's supplemental opinion affects not only local government law, but also real property law throughout the state. It squarely establishes that an affirmative covenant running with the land that requires the payment of money can be enforced against successive property owner(s) through a personal judgment for breach of contract, as opposed to solely in rem remedies.

V. CONCLUSION

Although PILOT agreements are common nationwide, the Florida Supreme Court's decision is the first case in Florida to directly address their validity. Not only did the *Bay Fund* case squarely address the legality and validity of PILOT agreements throughout Florida, but by expounding on and clarifying many aspects of municipal government, the decision provides valuable precedent to local government law practitioners. As cities and counties work to recover from economic deficits, this decision preserves an important revenue-generating tool for local governments and nonprofits to work together in serving their communities.