

# Bond Case Briefs

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## An Inconvenience of Qualified Equity: Squire Patton Boggs

Like me, at some point in your childhood, you were probably told not to “look the gift horse in the mouth.” After reading this blog post, the same could be said to me. We have written in great detail (see [here](#), [here](#), and [here](#)) about the increased flexibility afforded issuers by the recently promulgated [Final Treasury Regulations](#) governing, among other things, allocating proceeds of tax-exempt bonds and other sources to projects that involve both qualified and private uses (the “Allocation and Accounting Regulations”). The Allocation and Accounting Regulations permit “qualified equity” to be allocated first to private business use and then to governmental use. As discussed in the prior posts, “qualified equity” is essentially defined as amounts other than tax-exempt proceeds. However, there are timing and other restrictions on what is eligible to be considered “qualified equity.”<sup>[1]</sup> These restrictions have led to an inconvenience that is the topic of this blog.

### **The reimbursement window is larger than the qualified equity window**

Qualified equity includes amounts other than proceeds of tax-exempt bonds that are spent on the same eligible mixed-use project as the proceeds of the applicable bonds. To be spent on the same eligible mixed-use project, the qualified equity must be spent pursuant to the “same plan of financing.”

The preamble to the Allocation and Accounting Regulations says that qualified equity is spent under the same plan of financing if

“the qualified equity is spent on capital expenditures of the project no earlier than the earliest date on which the expenditure would be eligible for reimbursement were the bonds from which the proceeds are derived issued as reimbursement bonds . . . .”

The rule, as enunciated in the preamble, makes perfect sense. However, the actual language of the rule in the Allocation and the Accounting Regulations says that qualified equity is spent under the same “same plan of financing” if

“the qualified equity pays for capital expenditures of the project on a date that is no earlier than a date on which such expenditures would be eligible for reimbursement by proceeds of the applicable bonds under [Regulations] 1.150-2(d)(2) . . . .”

Regulations 1.150-2(d)(2) says that a reimbursement allocation must be made not later than 18 months after the later of (a) the date of the original expenditure or (b) the date the project is placed in service or abandoned, but in no event more than 3 years after the original expenditure is paid (collectively, the “Reimbursement Period”).

If you are reading this blog, you may know that there are certain expenditures that are eligible to be

reimbursed even though they were paid before the Reimbursement Period began. Specifically, a de minimis amount of pre-Reimbursement Period expenditures may be reimbursed as well as a certain amount of preliminary expenditures. Therefore, the window of time during which qualified equity can be used to finance a project begins after the period of time that expenditures would be eligible to be reimbursed under the reimbursement rules!

In reality, this discrepancy is less significant than it may initially seem. As discussed in the previous paragraph, the pre-Reimbursement Period expenditures are eligible for reimbursement even though the amounts paid to finance such expenditures are not eligible to be qualified equity. Therefore, a reimbursement allocation could be made on or after the issue date and the issuer could be reimbursed for the amount of equity that it used to finance the pre-Reimbursement Period expenditures. The issuer could then contribute the equity made available by the reimbursement allocation to finance a portion of the mixed-use project. Because the equity contribution occurs within the Reimbursement Period (assuming the mixed-use project has not yet been placed in service), it is contributed pursuant to the same plan of financing.

[1] As a technical matter, the restrictions do not preclude amounts other than tax-exempt bond proceeds from being qualified equity; rather, the restrictions prohibit the qualified equity from financing a project under the same plan of financing.

**By Joel Swearingen on November 11, 2016**

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