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IRS: You Can Still Issue Tax-Exempt Bonds to Advance Refund Most Taxable Bonds, Including BABs

For those who still had doubts, the IRS has now made it crystal clear: You can still issue tax-exempt bonds to advance refund most taxable bonds. In other words, the much-lamented "repeal of tax-exempt advance refunding bonds" in the Tax Cuts and Jobs Act from December 2017 isn't ironclad. The repeal prevents the issuance of tax-exempt bonds to advance refund only (1) other tax-exempt bonds and (2) a very limited subset of taxable bonds. The IRS expressed this conclusion in Chief Counsel Advice Memorandum 201843009, dated August 31 and released on October 26.

Following the logic of this guidance, the only taxable bonds that can't be advance refunded with tax-exempt bonds are taxable bonds that:

- Have a federal subsidy, such as Build America Bonds (i.e., "tax-advantaged bonds," as defined in Reg. 1.150-1(b), that are not tax-exempt bonds) **and**
- Do not lose their subsidy at the time that the tax-exempt bonds that advance refund them are issued.

One way to force a tax-advantaged taxable bond to lose its tax advantage is to "legally defease" it, which happens in almost all advance refundings once the issuer deposits Treasury securities acquired with proceeds of the advance refunding bonds into the refunding escrow on the issue date. Perhaps the only exception – certain governmental bonds cannot be legally defeased under state law.[1]

That's the bottom line. Read on for a little more about this guidance and the history behind it.

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The Public Finance Tax Blog

By Johnny Hutchinson on October 28, 2018

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