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ABA Tax Section Seeks Withdrawal of Proposed Issue Price Definition for Tax-Exempt Bonds.

Michael Hirschfeld of the American Bar Association Section of Taxation has submitted comments on proposed regulations (REG-148659-07) on arbitrage investment restrictions applicable to tax-exempt bonds and other tax-advantaged bonds, requesting that proposed changes to the current definition of issue price be withdrawn and that any other changes to the current regs be reproposed.

According to the tax section, the proposed changes to the issue price definition don't reflect a cost-benefit analysis of replacing the "reasonable expectations" provision of the current regs with the "actual facts" approach of the proposed regs. Section members believe that the changes to long-established market practices will harm intergovernmental comity and will increase rather than diminish uncertainty for issuers and other market participants.

Thus, the tax section suggests that the proposed regs should not replace the current regs, which could be improved as suggested by the tax section in its November 2010 comments on the determination of issue price applicable to tax-exempt bonds and all tax credit and Build America Bonds. If Treasury and the IRS decide to retain the actual facts approach, the tax section suggests many changes and additions to the applicable provisions of the proposed regs to retain some critical benefits of the current regs.

January 23, 2014

Hon. John Koskinen

Commissioner

Internal Revenue Service

1111 Constitution Avenue, NW

Washington, DC 20024

Re: Comments Concerning the Definition of Issue Price for Tax-Exempt Bonds and Other Tax-Advantaged Bonds

Dear Commissioner Koskinen:

Enclosed are comments concerning the definition of issue price for tax-exempt bonds and other tax-advantaged bonds. These comments represent the view of the American Bar Association Section of Taxation. They have not been approved by the Board of Governors or the House of Delegates of the American Bar Association, and should not be construed as representing the policy of the American Bar Association.

Sincerely,

Michael Hirschfeld

Chair, Section of Taxation

American Bar Association

Washington, DC

Enclosure

AMERICAN BAR ASSOCIATION

SECTION OF TAXATION

COMMENTS CONCERNING THE DEFINITION OF ISSUE PRICE FOR

TAX-EXEMPT BONDS AND OTHER TAX-ADVANTAGED BONDS

These comments (the “Comments”) on certain portions of Proposed Treasury Regulation section 1.148-1 are submitted on behalf of the American Bar Association Section of Taxation (the “Section”) and have not been approved by the House of Delegates or Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

Principal responsibility for preparing these Comments was exercised by Arthur Anderson of the Committee on Tax-Exempt Financing (the “Committee”). Substantive contributions were made by Faust Bowerman, Stefano Taverna, Christie Martin, Robert Kaplan and Mark Norell. The Comments were reviewed by Nancy M. Lashnits, Chair of the Committee, and by Frederic L. Ballard, Jr., reviewer for the Committee on Government Submissions, and Bahar Schippel, Council Director for the Committee.

Although the members of the Section who participated in preparing these Comments have clients who might be affected by the Federal tax principles addressed by these Comments or have advised clients on the application of such principles, no such member (or the firm or organization to which such member belongs) has been engaged by a client to make a government submission with respect to, or otherwise to influence the development or outcome of, the specific subject matter of these Comments.

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Date: January 23, 2014

EXECUTIVE SUMMARY

On September 16, 2013, the Internal Revenue Service (the “Service”) and the United States Treasury (the “Treasury”) published in the Federal Register proposed regulations[1] on the arbitrage restrictions under section 148[2] applicable to tax-exempt bonds and other tax-advantaged bonds. These Comments relate only to the portions of the proposed regulations related to the changes to the current definition of issue price, which is found in Regulations section 1.148-1 (the “Existing Regulations”).[3] Hereinafter such portions of the proposed regulations will be referred to as the

“Proposed Regulations.” The Section is submitting separate comments on other aspects of the proposed regulations, including provisions relating to working capital expenditures, grants and treatment of qualified hedges.

As used herein, the terms “tax-advantaged bonds” and “bonds” encompass all of the tax-exempt and other tax-advantaged bonds to which the Proposed Regulations will apply, if finalized.4

For the following reasons, the Committee respectfully requests that the Proposed Regulations be withdrawn and that any other changes to the Existing Regulations be re-proposed. The Proposed Regulations do not properly assess the significance of the perceived problems with the Existing Regulations nor do they reflect a cost-benefit analysis of replacing the “reasonable expectations” provision of the Existing Regulations with the “actual facts” approach of the Proposed Regulations. The Committee believes that the changes to long-established market practices will harm intergovernmental comity and will increase rather than diminish uncertainty for issuers and other market participants. Therefore, the Existing Regulations should not be replaced by the Proposed Regulations. However, the Existing Regulations could be improved as recommended in comments submitted by the Section in 2010 and attached hereto as Appendix A.

If the Service and Treasury decide to adhere to an actual facts approach, the Committee suggests a number of changes and additions to be made to the Proposed Regulations to retain certain critical benefits of the Existing Regulations.

I. RETAIN THE EXISTING REGULATIONS

A. Introduction.

For all types of tax-advantaged bonds, the issue price is the starting point for determining compliance with all arbitrage-related matters. It is also the starting point for determining compliance with other key requirements applicable to certain types of tax-advantaged bonds, including those relating to volume cap, private business use limitations and the restrictions on bond-financed costs of issuance. For “direct pay” tax-advantaged bonds such as “build America bonds” issued under section 54AA and section 6431, issue price determines whether an issuer has complied with the premium limit and, thus, along with other provisions, whether the issuer is entitled to receive the subsidy from the U.S. Treasury.5

Section 148(h) provides that the “yield on an issue shall be determined on the basis of the issue price (within the meaning of sections 1273 and 1274).” The Existing Regulations define issue price as follows:

Issue price means, except as otherwise provided, issue price defined in section 1273 and 1274. Generally, issue price of bonds that are publicly offered is the first price at which a substantial amount of bonds is sold to the public. Ten percent is a substantial amount. The public does not include bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters or wholesalers. The issue price does not change if part of the issue is later sold at a different price. The issue price of bonds that are not substantially identical is determined separately. The issue price of bonds for which a bona fide public offering is made is determined as of the sale date based on reasonable expectations regarding the initial public offering price. If a bond is issued for property, the applicable Federal tax-exempt rate is used in lieu of the Federal rate in determining the issue price under section 1274. The issue price of bonds may not exceed the fair market value as of the sale date.6

The “reasonable expectations” provision of Existing Regulations allows the final determination of the issue price of an issue of tax-advantaged bonds on the sale date. Thus, the issuer will know, on the sale date, whether the tax-advantaged bonds will satisfy the many requirements that depend on the issue price. Having a final issue price on the sale date also enables the issuer to make many calculations required for compliance with tax law (such as the yield on the bonds), which can be critical if yield-restricted investments are being purchased.

The Proposed Regulations would amend the issue price definition in a number of significant respects. Most importantly, the Proposed Regulations would base the determination of issue price on actual sale prices to the public instead of on reasonably expected sale prices. The Proposed Regulations would also remove the definition of "substantial amount" as ten percent. Instead, the Proposed Regulations would provide a safe harbor under which an issuer may treat the first price at which a minimum of 25 percent of the bonds of a maturity is actually sold to the public as the issue price, so long as all orders at this price received from the public during the offering period are filled (to the extent that the public orders at such price do not exceed the amount of bonds sold). The actual facts approach would eliminate, for a standard publicly-offered, tax-advantaged bond issue, the ability to determine with certainty whether the issue complies with tax provisions dependent on the issue price until after the sale date.

The "reasonable expectations" standard of the Existing Regulations does not require an issuer to delve into the intent of any particular purchaser of its tax-advantaged bonds. Issuers can form and rely on reasonable expectations about both the price at which the bonds will be sold and the identity and intent of the potential bond purchasers. In apparent recognition of this problem, in the Proposed Regulations the Service and Treasury attempt to clarify and simplify the distinction between a purchaser who is a member of the public and a purchaser who is not. The Proposed Regulations define the term "public" to mean any person other than an "underwriter." "Underwriter" is defined to mean any person that purchases bonds from the issuer for the purpose of effecting the original distribution of the bonds, or otherwise participates directly or indirectly in the original distribution. An issuer will find it fairly easy to identify as underwriters the financial firms with which it has a contractual relationship, such as, for example, through a bond purchase agreement. Under the Proposed Regulations, however, issuers would be required to determine intent in assessing purchases by security dealers and others who are not part of the underwriting syndicate, who may be acting "for the purpose of effecting the original distribution of the bonds."

B. Identifying the Problems and Assessing Their Significance.

The legislative history of Section 148(h) is clear. In enacting the provision as part of the Tax Reform Act of 1986, Congress intentionally overturned State of Washington v. Commissioner, 692 F.2d 128 (D.C. Cir. 1982), which held that an issuer's calculation of arbitrage yield should reflect the "all-in" costs of its borrowing, including the underwriter's compensation and the other costs of issuance. The underwriter's discount or commission is a major component of the costs of issuance for the issuer of any publicly-offered, tax-advantaged bond issue. Including costs of issuance in the issue price raises the issue price, and a higher issue price for a given principal amount of tax-advantaged bonds lowers the arbitrage yield thereon. Section 148(h) in effect prohibits an issuer from increasing the arbitrage yield on its bonds to recover the costs of issuance through the investment of bond proceeds at the higher yield.

The preamble to the Proposed Regulations identifies the problems the Service and Treasury see with the Existing Regulations. First, the preamble asserts that the ten percent standard does not always produce a representative price for tax-advantaged bonds due to the execution by underwriters of the first ten percent of the sale of a maturity of the bonds at the lowest price (and thus the highest yield) of the range of prices being offered. In other words, there is not a "bona fide public offering" of all of the bonds of the maturity at the stated issue price. Second, the public availability of certain actual pricing information on the Internet — most importantly through the Electronic Municipal Market Access ("EMMA") platform developed by the Municipal Securities Rulemaking Board (the "MSRB") — has led the Service and Treasury to question the ability of the reasonable expectations standard of the Existing Regulations to produce a representative issue price. The reported trade data has shown, in certain instances, actual sales to the public that differ significantly from the reasonably expected issue price. Third, the reported trade data has also shown sales to underwriters and security dealers being counted as sales to the public. Essentially, the Service and Treasury believe that the Existing Regulations are facilitating the understatement of the issue price of tax-advantaged bonds and the underwriter's compensation, producing an arbitrage yield higher than Section 148(h) permits.

Although the problems are adequately identified, the preamble fails to assess the significance of the problems.7 For example, it does not assess the loss to the Federal government resulting from lower rebate payments or higher subsidy levels. An underwriter who is holding back a portion of a maturity of tax-advantaged bonds may be faced with selling at a loss if the market moves away from it. An intermediary purchasing bonds on the sale date with the intent to "flip" them before the issue date may be in the same position. The reality is that markets go down as well as up.

Compounding the failure to assess the significance of the problems is the mislaying of the burden of fixing the problems. All three of the problems identified in the preamble — not making a bona fide public offering of all of the bonds of a maturity at their stated issue price, significantly different actual sale prices, and sales to "flippers" being counted as sales to the public — stem from the actions of underwriters and securities dealers. Issuers have little incentive or ability to control or alter the actions of these other market participants. The Existing Regulations should not be abandoned without a complete consideration of whether there are other tools available (such as MSRB or SEC rules) to address the problems without placing the burden on issuers.

C. Cost/Benefit Analysis.

The Service and Treasury should ascertain whether the benefits of the Proposed Regulations would be greater than the costs.8 If an issuer decides to eliminate the possibility of unsold maturities on the sale date, it will be forced to accept lower prices and higher yields in negotiated underwritings. In order to ensure that no unsold maturities exist, underwriters will have less incentive to market bonds aggressively. They will instead accept lower prices and higher yields just so bonds can be "put away" on the sale date. Due to the nature of competitive sales, it is virtually impossible to eliminate the possibility of unsold maturities. Underwriters in competitive sales cannot know whether they will have the opportunity to purchase bonds until the sale date, which discourages pre-sale marketing of those bonds. Alternatively, if the issuer determines to continue to sell its bonds as such sales occur in the current market, where the possibility of unsold maturities exists, the issuer will be forced to incur additional legal and financial advisory costs in attempting to determine issue price based on actual sales to the public. Additional bonds are likely to be issued to cover the higher costs. The Service and Treasury should determine whether the benefits of ascertaining what they believe to be a more accurate representative price of bonds may be offset by (i) the higher bond interest rates produced by discouragement of market pricing through competitive sales and the other ways in which the Proposed Regulations may narrow the market, and (ii) the higher fees paid to financial advisors and legal counsel because of the additional analyses that will need to be performed under the Proposed Regulations.

D. Effects on State and Local Governments.

Recent years have been difficult for State and local governments. Their finance staffs are currently thin and suffer from high rates of turnover. The Service and Treasury should consider the administrative burden that would be imposed on State and local finance officials if they are required to obtain, evaluate and apply the information about the identity of bond purchasers and pricing necessary to satisfy the actual sales standard in the Proposed Regulations.[9]

The burden could be particularly acute, and compliance may be impossible in the short-term, if issuers are required to determine the intent of a market participant (including participants with whom there is no privity of contract) in purchasing bonds — in other words, whether the purchaser is purchasing bonds for the purpose of effecting the original distribution of the issue. Although EMMA has clearly made pricing in the tax-advantaged bond market more transparent, it is not possible to ascertain a purchaser's intent through EMMA. The Committee's understanding is that EMMA was designed to provide general market transparency and that it was not designed to serve as a tool to establish issue price. The use of EMMA to gauge issue price can lead to erroneous conclusions. Therefore, State and local governments will likely be forced to add personnel or spend more money on lawyers and financial advisors to perform the due diligence needed to make the determinations of intent. These issues must be viewed in light of the fact that for governmental bond issues, only the yield would change as a result of the application of the Proposed Regulations. Neither the amount nor the timing of the debt service to be paid by the issuer nor the net proceeds to be received by the issuer at issuance would be affected by assigning bonds a higher issue price and thus a lower arbitrage yield for events occurring after the sale date.

In addition, the Committee believes that competitive sales will be difficult under the Proposed Regulations. Competitive sales generally ensure the lowest cost of capital for issuers (and hence minimize the arbitrage yield). Competitive sales are also required by the law of a significant number of States.[10]

The actual facts regime of the Proposed Regulations requires a protracted and continual tracking of actual sales of bonds and the determination of which purchasers are or are not underwriters. The possibility that the arbitrage yield on an issue could change after the sale date will require issuers to put additional cushion in the savings and other parameters in their authorizing resolutions if they are so permitted by State law. Furthermore, while the Proposed Regulations permit issuers to make a yield reduction payment in connection with advance refunding escrows the yield of which would exceed the yield on the bonds, issuers will certainly face additional costs in computing the yield reduction payments and many issuers may not have the funds to make any such payments. Overburdening State and local governments with the actual facts regime of the Proposed Regulations would be harmful to intergovernmental comity.

E. Reducing Uncertainty.

The greatest virtue of the Existing Regulations is certainty. Issuers are able to calculate the issue price and arbitrage yield on the sale date. Advance refunding issues can be verified, and refunding escrow securities can be locked in well before the closing date. Practitioners have also relied on the Existing Regulations to test compliance with many other tax and structuring requirements, such as whether the issuer has sufficient volume cap or has properly sized a debt service reserve fund. Official statements can be finalized in a timely manner. Furthermore, the certainty provided by the Existing Regulations allows issuers to proceed to closing with the knowledge that the sale date number runs would conclusively show compliance with the bond authorization parameters. For example, under the Existing Regulations an issuer can award bonds and purchase a refunding escrow on the sale date with the certainty of compliance with an authorizing resolution that requires a showing of a three percent present value debt service savings. The Proposed Regulations do not provide such level of certainty, and the Committee does not believe that the Service and Treasury have made the case that the savings either to the Federal government or to issuers will be sufficient to justify the loss of certainty.

F. Section II Conclusion: Retain the Existing Regulations.

The Committee believes that the Proposed Regulations should not be adopted.

The Committee acknowledges that the Existing Regulations would benefit from additional guidance to make them work more effectively. In this regard, the Committee references the comments on the definition of issue price submitted by the Section in 2010, a copy of which is attached as Appendix A. The Committee would welcome the inclusion in a re-proposed issue price definition of any or all of the suggestions set forth in the 2010 comments.

II. COMMENTS ON THE PROPOSED REGULATIONS

A. Introduction.

If the Service and Treasury decide to abandon the Existing Regulations, the Committee proposes the changes to the Proposed Regulations set forth below. The Committee respectfully requests that the market be given an opportunity to comment on any of these changes the Service and Treasury may determine to make and that such changes, along with the Proposed Regulations modified thereby, be re-proposed.

B. Twenty-Five Percent versus Ten Percent.

The 25 percent “substantial amount” safe harbor threshold is too high. Issuers will strive to achieve as much finality on the sale dates of their bonds as they can. The actual facts regime of the Proposed Regulations will result in issuers insisting on a demonstration by the underwriters that 25 percent of each maturity of an issue is actually sold to the public on the sale date. At times in the current market, the underwriter will not have actual sales of ten percent of each maturity on the sale date, much less 25 percent. The Committee believes that the narrowing of the market will result from the higher threshold, particularly when combined with the requirement to fill all orders for bonds at the safe harbor threshold price, and will drive up yields. The ten percent figure has been used for more than two decades by practitioners and market participants in the taxable market as well as by the tax-exempt market to establish how much of a particular maturity is a “substantial amount.”11 The removal of the substantial amount definition, therefore, affects not just the tax-exempt bond market, but also the taxable market. The Committee urges that the threshold remain at ten percent.

When a large number of substantially similar products, commodities or financial instruments (for example, multiple bonds of the same maturity) are offered for sale, there are likely to be multiple prices for such products, commodities or financial instruments. An increase in the substantial amount threshold from ten percent to 25 percent exacerbates this problem. If the Service and Treasury settle on the higher threshold, then it will be critically necessary to provide guidance on how issue price for a maturity is to be determined when multiple prices occur and less than 25 percent is actually sold at one price.

C. Competitive Sale Safe Harbor.

The Proposed Regulations surprisingly lack accommodation for competitive sales. Many issuers are required by the laws of their states to sell bonds competitively, and many others prefer competitive sales because they are believed to result in better bond pricing and streamlined procurement. Moreover, in competitive sales the issuer and the purchasers of the bonds do not have the same privity and contractual relationship that issuers enjoy in negotiated underwritings. This lack of accommodation is particularly surprising in light of past indications from the Service that the abuses observed in the determination of issue price, which were perceived occurring in negotiated transactions, were not apparent with competitive sales.

Given the compressed time periods and lower underwriting spreads in the competitive sale arena, the Committee believes that few competitive sales as currently configured will be able to satisfy the 25 percent safe harbor on the sale date. This may encourage issuers to choose the negotiated sale or private placement routes, if possible. This may have the unfortunate effect of raising tax-advantaged bond yields, harming both the Federal government and issuers.

The Committee urges the Service and Treasury to retain the basic reasonable expectations rules under the Existing Regulations for bond issues sold in competitive sales that meet requirements analogous to those for the establishment of fair market value prices for yield-restricted escrows and guaranteed investment contracts.

The Committee also urges the Service and Treasury to set the “substantial amount” threshold in competitive sales at the current market expectation — that is, ten percent — and to eliminate the requirement that all orders be filled at the stated offering price during the offering period. The nature of competitive sales simply does not permit the kind of pre-sale market testing that would encourage a bidder to take risks with the initial offering prices. Again, the Committee fears that yields will go up and harm both the Federal government and issuers.

D. Authorize Reliance on Certain Certificates.

The goal of an issuer in selling tax-advantaged bonds is to obtain the best possible pricing of debt instruments to finance a school, a municipal building or a road system. The issuer sells its bonds through underwriters and securities dealers because these intermediaries are in the business of finding bond purchasers and dealing with them. The Committee urges the Service and Treasury to add a provision to the Proposed Regulations, if finalized in their current form, authorizing an issuer to rely in good faith on a certificate from the managing underwriter or successful bidder regarding (i) the first price at which 25 percent of a maturity of tax-advantaged bonds is sold, (ii) the filling of all orders from the public at the first price during the offering period, and (iii) the identity of each underwriter of the bonds (including each “related party” underwriter). “Good faith” would mean the absence of abuse (for example, bid rigging, pay-to-play, or price-fixing) or actual contrary knowledge by the issuer.

In fact, underwriters, who are best positioned to know the facts surrounding any particular pricing, are already bound by MSRB standards dealing with factual representations. The standards provide that “all representations made by underwriters to issuers of municipal securities in connection with municipal securities underwritings (e.g., issue price certificates and responses to requests for proposals), whether written or oral, must be truthful and accurate and may not misrepresent or omit material facts.”12 Obtaining issue price representations, mostly written, is part of a well-established practice of bond tax counsel. In addition, the Committee supports specific identification rules, similar to those of section 1236(b) relating to dealer’s identification of securities held for investment, so long as the responsibility for making the specific identification resides with the underwriters and securities dealers.13 Those identification requirements should remain with the market participants and can be used as evidence of truthfulness about the underwriter’s representations.

The underwriters of a tax-advantaged bond issue have, or can cost-effectively obtain, the background needed to make the certifications necessary to satisfy the safe harbor issue price rule. Policing mechanisms exist to assure the veracity of the certifications. The Committee urges the Service and Treasury to make it clear that an issuer can satisfy the safe harbor issue price rules through good faith reliance on an underwriter’s certificate.

E. Need for Actual Sales Price Data.

Although technological improvements (such as EMMA) are mentioned in the preamble to the Proposed Regulations, the text of the Proposed Regulations does not specify where an issuer is to obtain the information about the actual sales of its bonds. EMMA in its current form does not provide a viable solution, because of its various timing and misidentification problems, which have been mentioned above and discussed with the Service and Treasury in other contexts. EMMA can only serve as a tool to verify in some, but not all, cases, the certifications provided by paid professionals that are supposed to comply with securities laws. If the Service and Treasury require that the issue price of sales be based on actual facts, they should first make sure that issuers have access to the necessary data to comply or to verify the certifications of the underwriters. Prior to requiring that prices be based on actual sales prices, the Committee recommends that significant lead time be provided so as to ensure that databases (whether from EMMA, from underwriters or by other means) exist to ensure transparent and accurate information for compliance with the tax law. Additionally, the Committee recommends that prior to effectiveness of the Proposed Regulations, the Service review those databases to ensure that it is satisfied with the quality and sufficiency of the data.

F. Defined Safe-Harbor Offering Period.

The Proposed Regulations have the potential to create enormous uncertainty by the requirement to track — possibly long after the closing date of a bond issue — the actual sale prices of the bonds. This tracking may be necessitated by (i) the need to assure that even if the required portion of a maturity of bonds is actually sold at the initial offering price, all orders for bonds of the maturity at the initial offering price during the "offering period" are filled, and (ii) situations in which less than the required threshold of the maturity is sold at the initial offering price. The Proposed Regulations do not define "offering period," but most market participants assume that it has the same meaning as under the securities laws. This means, for a particular maturity of bonds, a period ending on the date the underwriters no longer retain an unsold balance of the bonds for sale to the public. The end date need not correspond to the closing date of the issue.

In order to provide issuers some finality and certainty in the process of determining issue price, the Committee urges the Service and Treasury to include the concept of a defined safe-harbor offering period. This is, admittedly, a rough-justice approach, but it reflects the undeniable fact that markets go down as well as up in the two-week to four-week period between the sale date and the closing date of a typical governmental bond issue and certainly fluctuate after the closing date. The Service and Treasury should consider whether any net loss in terms of overstated yields will be negated by the cost of the bonds that will have to be issued to cover the additional issuance costs.

The Committee recommends that the offering period end six business days after the sale date. The six-day period is chosen for two reasons. First, six business days would always require the holding of the initial offering price or a position in the to-be-issued bonds over a weekend. Second, six business days would allow the final determination of issue price in time for the issuer to meet its obligation under SEC Rule 15c2-12 to deliver the final official statement within seven business days after the sale date. Such a rule would not only promote certainty but would also reflect that tax laws related to issue price do not operate in a vacuum. It would promote intergovernmental comity by dovetailing with the other regulatory guidelines with which issuers and underwriters must comply.

The Service and Treasury could alternatively consider defining the offering period by reference to the 13-day or 15-day periods established under Regulations Section 1.1275-1(f) or 1.150-1, even though this approach would not work as well with existing market requirements and practices as the six business day offering period. If two bond issues that are sold 15 days apart from each other are deemed to be separate issues, the Service and Treasury should view the sale of the second bond of a maturity 15 days after the sale of the first bond of the same maturity as not affecting each other.

The concept of a definite safe harbor offering period would also facilitate addressing the situation in which less than 25 percent (or ten percent) of a maturity can be sold at the initial offering price (or at the "first price," if different). If by the end of the safe-harbor period less than 25 percent (or ten percent) of a maturity is actually sold to the public, the issue price of that maturity should be the initial offering price at which that maturity was marketed to the public on the sale date in a bona fide public offering.

G. Bifurcated Rule.

If the concern of the Service and Treasury is that the yield on new money financings is too high based on the Existing Regulations, then they should consider finalizing the Proposed Regulations with a bifurcated rule under which refunding escrows would be subject to one rule and new money transactions, which include longer term investments in construction and acquisition funds, as well as reserve funds, would be subject to a different rule.

H. Non-Yield-Related Consequences of the Actual Facts Regime.

The Committee does not believe that issuers can adequately assess the potential consequences of the Proposed Regulations without knowing how the Service and Treasury intend to address the many other provisions of the Code the compliance with which is determined based on the issue price of the bonds. For example, the actual facts regime may not allow an issuer to secure adequate volume cap. In addition, the limits on costs of issuance may also be violated if the issue price becomes less than originally anticipated. This is the most important reason for the Committee's request that any change in the issue price definition be re-proposed.

FOOTNOTES

1 Prop. Reg. § 1.148-1, 78 Fed. Reg. 56,842 (2013).

2 References to a "section" are to a section of the Internal Revenue Code of 1986, as amended, unless otherwise indicated.

3 Reg. § 1.148-1.

4 Prop. Reg. § 1.150-1(b), 78 Fed. Reg. 56,842 (2013), defines a "tax-advantaged bond" to mean:

[A] tax-exempt bond, a taxable bond t hat provides a Federal tax credit to the investor with respect to the issuer's borrowing costs, a taxable bond that provides a refundable Federal tax credit payable directly to the issuer of the bond for its borrowing costs under section 6431, or any future similar bond that provides a Federal subsidy for any portion of the borrowing costs. Examples of tax-advantaged bonds include qualified tax-credit bonds under section 54A(d)(1) and build America bonds under section 54AA.

5 I.R.C. § 54AA(d)(2)(C) (for "build America bonds") and Notice 2010-35, 2010-19 I.R.B. 660 (for qualified tax-credit bonds).

6 Reg. § 1.148-1(b).

7 The Committee will make several references to Exec. Order No. 12,866, 58 Fed. Reg. 51,735 (October 4, 1993) ("EO 12866"). In EO 12866 President Clinton set forth the principles to which

Federal agencies are to adhere in promulgating regulations. One of these principles requires Federal agencies not only to identify the problem intended to be addressed by a regulation, but also to assess the significance of that problem. On January 18, 2011, President Obama issued Exec. Order No. 13,563, 76 Fed. Reg. 3821 (January 21, 2011), to reaffirm and supplement EO 12866. President Obama made no substantive changes to any of the regulatory principles of EO 12866.

8 In developing a regulation, EO 12866 requires a Federal agency to:

[A]ssess both the costs and the benefits of the intended regulation and, recognizing that some costs and benefits are difficult to quantify, propose or adopt a regulation only upon a reasoned determination that the benefits of the intended regulation justify its costs. . . .

9 EO 12866 requires Federal agencies to be sensitive to the views of State, local and tribal governmental entities. In developing a regulation, an agency must:

[A]ssess the effects of Federal regulations on State, local, and tribal governments, including specifically the availability of resources to carry out those mandates, and seek to minimize those burdens that uniquely or significantly affect such governmental entities, consistent with achieving regulatory objectives. In addition, as appropriate, agencies shall seek to harmonize Federal regulatory actions with related State, local, and tribal regulatory and other governmental functions. . . .

10 See, e.g., Thomas A. Schweich, Missouri State Auditor, General Obligation Bond Sales Practices (November 2013), http://www.auditor.mo.gov/Press/2013116769245.pdf.

11 David C. Garlock, Federal Income Taxation of Debt Instruments, ¶ 203.03 (6th ed. 2010).

12 See, MSRB Notice 2012-25 (May 7, 2012) (providing interpretive notice on the application of MSRB Rule G-17).

13 Reg. § 1.1236-1 clearly imposes the responsibility for identification of a security as “held for investment” on the securities dealer.