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IRS Rules that No Abusive Arbitrage Device Was Used in Connection With Bond Issue: Tax Analysts

In technical advice, the IRS concluded that no abusive arbitrage device was used in connection with bonds used to refund in advance a portion of the issuer's outstanding indebtedness.

Under section 148, the tax exemption for interest on state and local bonds does not apply to any arbitrage bond. Reg. section 1.148-10(a)(1) provides that bonds of an issue are arbitrage bonds if an abusive arbitrage device is used in connection with the issue.

The IRS found no evidence to indicate that any action was taken by the issuer to enable it to exploit the difference between tax-exempt and taxable interest rates to obtain a material financial advantage. Therefore, the IRS determined that no abusive arbitrage device was used in connection with the issue.

The IRS also concluded that neither the reserve portion nor the current portion of the bonds constitutes excess gross proceeds under reg. section 1.148-10(c)(2) because both are replacement proceeds in sinking funds for the refunding issue. Lastly, the IRS determined that the bonds were not an advance refunding in which a device was employed to obtain a material financial advantage apart from savings attributable to lower interest rates.

Summary by Tax Analysts®

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Citations: TAM 201538013

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