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IRS Amends TED Bond Volume Cap Rules To Accommodate Draw-Down Loans: Holland & Knight

HIGHLIGHTS:

- The Internal Revenue Service (IRS) has issued Notice 2015-83, which will make it easier for Indian tribal governments to use tribal economic development (TED) volume cap for “draw-down” loan structures in which the lender advances funds for the loan on different dates.
- Draw-down loans are often a preferred means for tribal governments to borrow money for new construction projects because construction funds are borrowed in stages as needed, thereby reducing the “negative carry” associated with notes or bonds in which the full construction costs are borrowed and interest begins to accrue upon the sale of the securities.
- In addition, since draw-down loans are not considered securities subject to registration with the U.S. Securities and Exchange Commission (SEC), tribes can utilize them to borrow funds without incurring such increased costs.

The Internal Revenue Service (IRS) issued Notice 2015-83 on Dec. 4, 2015, a change that will make it easier for Indian tribal governments to use tribal economic development (TED) volume cap for “draw-down” loan structures in which the lender advances funds for the loan on different dates. Under a legislative provision enacted in 2009 as part of the American Recovery and Reinvestment Act, tribal governments may apply for TED volume cap in order to finance on-reservation, non-gaming economic development projects with tax-exempt debt. However, relatively few tribal governments have taken advantage of TED bonds or loans since they first became available in 2010.

Draw-down loans are often a preferred means for tribal governments to borrow money for new construction projects because construction funds are borrowed in stages as needed, thereby reducing the “negative carry” associated with notes or bonds in which the full construction costs are borrowed and interest begins to accrue upon the sale of the securities. Further, securities – such as bonds or notes – issued by a tribal governments are not exempt from registration requirements of the U.S. Securities and Exchange Commission (SEC) under the federal securities laws, often resulting in higher rates of interest and closing costs. Since draw-down loans are not considered securities subject to registration with the SEC, tribes can utilize them to borrow funds without incurring such increased costs.

In 2012, the IRS issued Notice 2012-48, under which a tribal government would have to issue debt obligations utilizing its allocated TED volume cap within 180 days of receiving the allocation. It was not clear how the IRS’ 180-day rule, which was put in place administratively to encourage tribal governments use allocation awards promptly, would apply to draw-down loans. Arguably, draw-down loans were at odds with the IRS timing requirements because typically the loan proceeds would be drawn down over a longer period of time, sometimes two or three years.

Overview of Notice 2015-83 Requirements

Under Notice 2015-83, the IRS established new rules that accommodate the use of TED volume cap in the draw-down loan context. If a tribal government receives a TED allocation for a tax-exempt draw-down loan and spends at least 10 percent of the borrowed money within 180 days, it will have up to three years from the date of the allocation to spend the remaining volume cap amount. To have a full three years from the original allocation date, the tribal government must not only meet the 10 percent requirement above, it must also spend at least 50 percent of the proceeds of the draw-down loan within the first two years.

Notice 2015-83 also requires tribal governments to meet certain information reporting requirements to demonstrate readiness and compliance. First, a tribal government applying for a TED allocation must submit a commitment letter from a financial institution stating that the institution reasonably expects to advance the total principal amount of the draw-down loan no later than three years after the date of the allocation letter. Second, a tribal government awarded a TED allocation must submit notices of issuance to the IRS not later than 15 days after:

- the 180-day period
- the 2-year period
- the 3-year period

Each of the notices must indicate the amounts drawn and the remaining unused allocation (if any) for each period.

Notice 2015-83 states that the new rules are effective for applications for TED bond volume cap submitted on or after December 4, 2015. It also applies to applicants that have received TED volume cap that has not expired before December 4, 2015.

Considerations for Tribal Governments

In summary, Notice 2015-83 offers useful guidance for tribal governments that would like to participate in the advantages associated with tax-exempt financing without having to issue bonds that may have disadvantages when compared with draw-down loans.

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.

Last Updated: December 8 2015

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