Bond Case Briefs

Municipal Finance Law Since 1971

Market Groups Likely to Urge Agencies to Scrap Political Subdivision Rules.

WASHINGTON – Municipal market participants will most likely recommend the Treasury Department and the Internal Revenue Service scrap their controversial proposed rules that seek to redefine which political subdivisions can issue tax-exempt bonds, several attorneys said on Monday.

The rules were listed among eight tax regulations that were either proposed, issued as temporary, or finalized between Jan. 1, 2016 and April 21, 2017 and found by Treasury to be significant and to warrant abandonment or major modifications under an executive order President Trump issued on April 21.

The list of eight was announced by the IRS on Friday in Notice 2017-38, which is to be published in the Internal Revenue Bulletin on July 24. Treasury asked market participants to submit public comments to it by Aug. 7 on whether the regulations "should be rescinded or modified."

The political subdivision rules were proposed in February 2016 by Treasury and the IRS to redefine what constitutes a political subdivision that can issue tax-exempt bonds.

Under longstanding federal law and rules, an entity is a political subdivision that can issue tax-exempt bonds if it has the ability to exercise a substantial amount of at least one of three sovereign powers – taxation, eminent domain and policing.

But Treasury and the IRS, which became concerned that some political subdivisions were controlled by private developers, proposed adding two more requirements to that definition. They said a political subdivision must also be governmentally controlled and serve a governmental purpose "with no more than an incidental private benefit."

"I think that practitioners will be happy to see that rule withdrawn," said Dee Wisor, a lawyer at Butler Snow in Denver. "Practitioners would prefer to go back to what the rule was."

Both the National Association of Bond Lawyers and the American Bar Association's Taxation Section have urged Treasury and the IRS to withdraw the proposed rules. The ABA group warned the proposed rules are over-reaching, ignore congressional intent, run counter to decades of practice, and cast doubt on many legitimate entities that currently issue tax-exempt bonds.

Tom Vander Molen, a lawyer with Dorsey & Whitney in Minneapolis who heads NABL's tax law committee, said the notice on the eight regulations was "a positive development" and that he expects NABL to reiterate its call for Treasury and the IRS to withdraw the proposed rules on political subdivisions. But he cautioned that NABL has not made any decision yet.

John Vahey, managing director of federal policy for Bond Dealers of America, said, "BDA agrees with Treasury's assessment that the proposed political subdivision rule represents an undue increase in both complexity and regulatory burdens. The rule, as proposed, is overly broad and would result in government entities being unnecessarily denied the ability to finance economically beneficial public

projects in the tax-free municipal market and BDA looks forward to submitting additional comments in August."

The Securities Industry and Financial Markets Association also urged the IRS in previous comments to withdraw the proposed rules.

Emily Brock, director of the federal government liaison center for the Government Finance Officers Association, said the group previously recommended withdrawal of the proposed regulations due to the far-reaching scope and potential impact to political subdivisions and the essential public services they provide across the US.

She said also that a coalition of issuers joined together to explain to Treasury and IRS officials that the determination of a subdivision's governmental purpose is made during the consideration of state legislation that authorizes the creation of the political subdivision. The group noted that if a political subdivision does not serve the purpose of the authorizing legislation, it is operating ostensibly against the law of that state and that this is an issue for the state, not the U.S. Treasury.

The list of eight regulations stem from Trump's Executive Order 13789, which was issued on April 21 and directed the Treasury secretary and administrator of the Office of Information and Regulatory Affairs to identify regulations issued as temporary, proposed, or finalized during the almost 16 months that: impose undue financial burdens on U.S. taxpayers; add undue complexity to federal tax laws; or exceed the statutory authority of the IRS.

Treasury said it found 105 regulations during that period, 52 of which were considered to be potentially significant, and identified eight of them as needing a reduction of tax burdens.

The IRS notice asked any commenters that want the rules to be modified rather than withdrawn, to describe the modifications that would "reduce burdens and complexity."

The IRS said that in opposing the proposed political subdivision rules, the "commenters stated that the longstanding 'sovereign powers' standard was settled law and had been endorsed by Congress, and additional limitations were unnecessary."

"Commenters also stated that the proposed regulations would disrupt the status of numerous existing entities and that it would be burdensome and costly for issuers to revise their organizational structures to meet the new requirements of the proposed regulations," the agency said.

The Bond Buyer

By Lynn Hume

Copyright © 2026 Bond Case Briefs | bondcasebriefs.com