

Bond Case Briefs

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IRS Provides Guidance on Refinancings of Tribal Economic Development Bonds - Refinancings of TEDs and Other Targeted Bond Programs Allowed Without Additional Volume Cap Allocation: Holland & Knight

The Internal Revenue Service (IRS) on May 22, 2019, issued much awaited guidance in Notice 2019-39. This Notice allows for refinancings or refundings by Native American tribal governments of Tribal Economic Development bonds and loans (TEDs) without needing to obtain additional allocation of TED volume cap. The new Notice represents an important step in allowing tribes to currently refinance or refund outstanding TEDs without using any of the dwindling amount of TED volume cap from the U.S. Department of Treasury and IRS.

The Notice also applies similar rules to other targeted bond programs such as Gulf Opportunity Zone (GO Zone), Midwestern Disaster Area, Hurricane Ike Disaster Area and Recovery Zone Facility bonds. The Notice was issued in part to eliminate the need for separate program-by-program guidance regarding the volume cap exception for certain current refunding bonds (bonds issued to refund or refinance bonds of a prior issue not more than 90 days before the last expenditure of any proceeds of the refunding issue to pay principal or interest on the prior issue).

Purpose of Tribal Economic Development Bonds

In 2009, Congress enacted a special tax code provision for Tribal Economic Development Bonds - Code Section 7871(f) - to give Native American tribal governments "greater flexibility" to finance economic development projects. The only other opportunity for tribes to seek tax-exempt financing was, and continues to be, Code Section 7871(c), which imposes a restrictive "essential governmental function" test on tribal debt financing. Under the TED program, tribal governments may apply with the Treasury Department and IRS for a TED volume cap allocation to finance on-reservation, nongaming economic development projects with tax-exempt debt. Many tribes have used TEDs to finance such projects and have achieved a lower cost of borrowing since interest on TEDs is federally tax-exempt for the holder of such debt.

Congress limited TEDs to \$2 billion worth of debt and gave the Treasury Department the authority to allocate the \$2 billion volume cap among Native American tribal governments as deemed appropriate by Treasury in consultation with the U.S. Department of the Interior. As of April 1, 2019, no tribe may receive more than \$100 million of TED volume cap, i.e., the greater of 1) 20 percent of the amount of available volume cap of \$182,605,445.95 determined as described in IRS Notice 2012-48, or 2) \$100 million. Tribal governments have been concerned for several years as the available volume cap of TEDs has dwindled with no Congressional relief in sight.

Why the Notice Was Issued

The IRS acknowledged that previously issued guidance for targeted bond programs, such as TEDs and disaster relief bond programs, with volume cap limitations and time restraints, did not address

how refundings and refinancings fit within those programs' limitations. Prior notices relating to TEDs did not address the permissibility of issuing new TEDs in current refunding issues to refund or refinance outstanding TEDs.

As a result, questions have arisen regarding whether original TEDs may be refinanced in current refunding issues without the tribal government seeking additional TED allocation. Under Section 146(i) of the Code, the general rule for tax-exempt private activity bonds subject to volume cap is that current refundings of such bonds are exempt from volume cap to the extent that the amount of the refunding bonds does not exceed the outstanding amount of the refunded bonds. Because no such exception is specifically provided for TEDs, this created an ambiguity that prevented many bond lawyers from opining that TEDs could be refinanced on a tax-exempt basis without a new allocation of volume cap. Further, since TED volume cap is now very limited, many outstanding TEDs would have had to be paid at maturity or refinanced on a taxable basis.

What Does the Notice Say?

Specifically, Notice 2019-39 states that any current refunding issue the proceeds of which are used (directly or indirectly in a series of current refunding issues) to refund original TEDs qualifies for issuance as an issue of tax-exempt TEDs without regard to any bond volume cap or issuance time deadline for the original TEDs if all of the following requirements are met:

1. the original TEDs were issued with any required bond volume cap allocation and before any applicable time deadline for issuance of the original TEDs
 2. the issue price of the new TEDs is no greater than the outstanding stated principal amount of the outstanding TEDs (with certain exceptions for existing TEDs previously issued with more than a de
 3. minimus amount of original issue discount or premium)
- the current refunding issue meets all applicable requirements for the issuance of TEDs

Considerations for Tribal Governments

In summary, Notice 2019-39 clarifies that tribal governments need not seek an additional TED allocation to refinance or refund existing TEDs on a tax-exempt basis. The new Notice is welcome in light of the dwindling amount of nationwide TED bond allocation remaining. Native American tribes should review the Notice carefully as it represents an important opportunity for Native American tribal governments.

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