Bond Case Briefs

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Update on the Reconciliation Package: Municipal Bonding Priorities

Pullman & Comley's Public Finance tax attorneys are pleased to bring you the latest development on the budget reconciliation front as it relates to municipal bonding. Last Thursday, September 9, 2021, the House Ways and Means Committee kicked off a multiday markup of key elements of $3.5 trillion social spending package. In the evening on Friday, September 10, the House Ways and Means Committee released the remaining tax subtitles for consideration in their portion of the reconciliation package. The proposed legislation, which the Committee will mark up this week, includes the following municipal bond priorities (among others):

- Restoration of Advance Refundings,
- Reinstatement of a Direct Subsidy Bond Program Similar to Build America Bonds, and
- Expansion of Bank Qualified Provisions of the Code.

The Committee's section-by-section summary is below. There are still no firm details on the Senate's tax provisions or on the anticipated schedule for consideration.

Section-By-Section Details for Select Sections of Subtitle F – Infrastructure Financing and Community Development

Sec. 135101. Credit to issuer for certain infrastructure bonds.

Based on the successful Build America Bonds program enacted in the 2009 American Recovery and Reinvestment Act, issuers of qualified infrastructure bonds would receive a tax credit equal to an applicable percentage of the interest, providing direct financing support for infrastructure investments made by state and local governments. The applicable percentage of the credit for interest paid with respect to qualified bonds is determined in the year the bond is issued as follows:

2022 through 2024 – 35%
2025 – 32%
2026 – 30%
2027 and thereafter – 28%

State and local governments may claim this credit for bonds whose interest would otherwise be eligible for tax-exempt status in the Internal Revenue Code, and the entirety of whose net proceeds are used for capital expenditures or the operation and maintenance of capital expenditures.

This provision requires that 100% of the proceeds of a bond issued under this provision meet the requirements in the Davis-Bacon Act. Payments under this section are grossed up in the event of sequestration. This provision applies to qualified infrastructure bonds issued after December 31, 2021.

Sec. 135102. Advance refunding bonds.

Advance refunding refers to a state or local government holding the proceeds of a refunding issue for longer than 90 days before using such proceeds to pay off a refunded issue, allowing state and municipal governments to take advantage of lower interest rates to refinance long-term debt obligations. Prior to repeal in the 2017 Tax Cuts and Jobs Act, interest on advance refunding bonds was exempt from tax. This provision would once again allow interest on advance refunding bonds issued by state and local governments to be exempt from tax. This provision applies to advance refunding bonds issued more than 30 days after date of enactment of this Act.

Sec. 135103. Permanent modification of small issuer exception to tax-exempt interest expense allocation rules for financial institutions.

As a general rule, no deductions are allowed for expenses that are allocable to tax-exempt income, including tax-exempt interest received by holders of certain municipal bonds. The same general rule applies to financial institutions to disallow a deduction for interest expense that is allocable to tax-exempt interest income. However, present law provides an exception for interest expense allocable to certain tax-exempt obligations issued by qualified small issuers, which are defined (in part) as issuers that are not reasonably expected to issue more than $10 million in tax-exempt obligations during a calendar year. This provision revises the definition of qualified small issuers by increasing the $10 million limit to $30 million (indexed annually for inflation). In addition, this provision treats qualified 501(c)(3) bonds as tax-exempt obligations for purposes of the small issuer exception, and makes permanent certain rules related to qualified financings.

Sec. 135104. Modifications to qualified small issue bonds.

This provision expands the definition of eligible manufacturing facilities eligible for financing through qualified small issue bonds to include facilities used for the creation or production of intangible property, and facilities functionally related and subordinate (or directly related and ancillary) to facilities used for the manufacturing, creation, or productions of tangible or intangible property. This provision also raises the aggregate cap for prior issues from $10 million to $30 million, indexed annually for inflation.

Please contact Michael J. Andreana, Sandra D. Dawson or Glenn G. Rybacki with any questions.

by Michael J. Andreana, Sandra D. Dawson and Glenn G. Rybacki

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Pullman & Comley, LLC