Bond Case Briefs

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Tax

Potential Changes for Churches and Charities Regarding Political Campaigning.

A few weeks ago, President Trump announced that he would advocate for the repeal of the prohibition against certain religious organizations (i.e., those exempt from paying federal income taxes under Section 501(c)(3)) from engaging in political campaigning. His statement was made at the National Prayer Breakfast to a group of religious leaders. However, since the prohibition applies to all Section 501(c)(3) entities (e.g., 501(c)(3) universities and hospitals), it seems likely that any such repeal would also apply to all Section 501(c)(3) entities.

To be clear, the prohibition on political campaigning does not apply to religious organizations or other charities per se. Rather, the ban only applies to those entities that have obtained Section 501(c)(3) status. A 501(c)(3) organization is exempt from federal income tax on what would otherwise be its taxable income (aside from taxable income derived from a trade or business that is unrelated to the organization's tax-exempt purpose), and donors to a 501(c)(3) organization may, subject to certain limits, claim a federal income tax deduction for contributions made to the 501(c)(3) organization. In other words, under current law, a Section 501(c)(3) organization has chosen to give up its right to engage in political campaigning in exchange for generous federal income tax benefits. The practical impact of the ban (also known as the Johnson Amendment) is that Congress has decided for the past 60 years that the federal government will not subsidize political campaigning by 501(c)(3) organizations.

Continue reading.

The Public Finance Tax Blog

By Cynthia Mog on March 1, 2017

Squire Patton Boggs

TAX - LOUISIANA

Cameron Parish Police Jury v. All Taxpayers

Court of Appeal of Louisiana, Third Circuit - February 21, 2017 - So.3d - 2017 WL 693927 - 2017-55 (La.App. 3 Cir. 2/21/17)

Parish police jury and school board brought action to validate proposed cooperative endeavor agreement and payment in lieu of taxes (CEA/PILOT) agreement with natural gas liquefaction facility operator.

The District Court entered judgment finding proposed agreement legally invalid. Police jury and school board appealed.

The Court of Appeal held that:

- As a matter of first impression, statutes providing for CEA/PILOT agreements did not authorize police jury to enter into an agreement to reduce or effectively exempt ad valorem taxes for a single taxpayer already operating in the area;
- Proposed agreement violated statutes setting forth procedure for assessing and collecting ad valorem taxes; and
- Proposed agreement violated uniformity provision of constitution.

Statutes providing for public-private partnerships in economic development projects, including through cooperative endeavor agreement and payment in lieu of taxes (CEA/PILOT) agreements and through tax increment or bond financing, did not authorize police jury to enter into an agreement to reduce or effectively exempt ad valorem taxes for a single taxpayer already operating in the area.

Proposed cooperative endeavor agreement and payment in lieu of taxes (CEA/PILOT) agreement, by which police jury would accept fixed annual payments from taxpayer, an operator of a natural gas liquefaction facility, in lieu of ad valorem taxes based upon the facility's fair market value, violated statutes setting forth procedure for assessing and collecting ad valorem taxes, which required assessment at percentage of fair market or use value and prohibited omission of taxable property from assessment list.

Proposed cooperative endeavor agreement and payment in lieu of taxes (CEA/PILOT) agreement, providing for taxing authorities to obligate themselves not to collect ad valorem taxes from taxpayer, which operated a natural gas liquefaction facility, in excess of specified amount and for parish to certify fair market value of facility only in such amount as specified by agreement, violated uniformity provision of state constitution; uniformity provision granted exclusive authority to assessor to assess the facility, while police jury's authority was limited to one of review.

Proposed cooperative endeavor agreement and payment in lieu of taxes (CEA/PILOT) agreement, providing for taxing authorities to obligate themselves not to collect ad valorem taxes from taxpayer, which operated a natural gas liquefaction facility, in excess of specified amount and for parish to certify fair market value of facility only in such amount as specified by agreement, violated constitutional provision forbidding exemptions from ad valorem taxes except in enumerated exceptions; agreement operated as partial exemption of a manufacturer's taxes.

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375 Key Organizations Sign Letter to Save the Muni-Exemption.

Yesterday, the Municipal Bonds for America (MBFA) Coalition sent a letter to House and Senate Leaders, including House Ways and Means and Senate Finance Committee leaders, urging them to retain the current law status on municipal bonds as a part of their ongoing debate on comprehensive tax reform. The letter is signed by 375 organizations from across the United States, representing almost all 50 states. This letter brings continued attention to the value that municipal bonds provide as the strongest and most proven method of financing ongoing infrastructure needs for state and local governments and ultimately, the constituents of all Congressional representatives.

Specifically, the letter highlights:

- State and local governments have financed infrastructure and other community related projects using tax-exempt municipal bonds for over a century
- Reducing or eliminating the tax exemption for municipal bonds could raise infrastructure costs by

10 to 12 percent, with these costs being passed directly to taxpayers
- Preserving the current law status of municipal bonds is essential in rebuilding our nations economy and infrastructure

The letter will remain open for signatures at the MBFA website here. As we continue to grow support and receive additional signatures on the letter, we will update the website with new numbers.

Thanks again to all of those that helped in obtaining signatures for this very important effort. If you have any questions please feel free to reach out to Justin Underwood at justin@munibondsforamerica.org.

MBFA Chair Featured in The Hill: The Case for Tax-Exempt Municipal Bonds for 21st Century America.

Today, Steve Benjamin, Mayor of Columbia, SC and Chair of the Municipal Bonds for America (MBFA) Coalition, contributed an op-ed in The Hill, advocating for why preserving the current law status of municipal bonds is essential in rebuilding our nations economy and infrastructure. You can read the article online here.

Specifically, the article highlights:

- How municipal bonds play a vital economic role in small towns and large cities all across America
- The impact state and local governments may face if the municipal tax-exemption is capped or removed altogether
- How roughly two-thirds of America's core infrastructure is built by state and local governments using tax-exempt municipal bonds

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TAX - PENNSYLVANIA

In re Wilson

United States District Court, E.D. Pennsylvania - December 28, 2016 - B.R. - 2016 WL 7450468

Confirmation hearing was held on Chapter 13 plan proposed by taxpayer whose real property had been sold at prepetition tax foreclosure sale. The Bankruptcy Court entered order confirming plan, which provided for payment of redemption amount with interest over course of plan, and taxing authority appealed.

The District Court held that:

- City, in its capacity as taxing authority, was not "person aggrieved," with standing to appeal bankruptcy court order confirming plan that allowed debtor-taxpayer to redeem real property by paying redemption amount in full with interest over the course of plan, and
- City was not "party in interest" with standing to file objection in bankruptcy court to confirmation of proposed plan.

City, in its capacity as taxing authority, was not "person aggrieved," with standing to appeal bankruptcy court order confirming Chapter 13 plan that allowed debtor-taxpayer to redeem real property that had been sold at prepetition tax foreclosure sale by paying redemption amount in full with interest over the course of his debt adjustment plan, as any injury to city was purely speculative.

City, in its capacity as taxing authority, was not "party in interest" with standing to file objection in bankruptcy court to confirmation of proposed Chapter 13 plan that provided for payment of amount necessary to allow debtor to redeem real property that had been sold at prepetition tax foreclosure sale, with interest, over the course of his debt adjustment plan. Any injury to city was purely speculative and did not qualify as kind of concrete and particularized injury needed to make city a "party in interest."

H.R. 811 Would Treat Stadium Financing as Private Activity Bonds

H.R. 811, the No Tax Subsidies for Stadiums Act, introduced by Rep. Steve Russell, R-Okla., would treat sports stadium financing obligations as private activity bonds if the obligations meet the private business use test.

Bipartisan Bill Reintroduced to Ease Tax Curbs on Small Issuer IDBs.

WASHINGTON – House members have reintroduced a bill that would modernize and ease tax law restrictions for small bond issues used to finance manufacturing facilities.

The Modernizing American Manufacturing Bonds Act (H.R. 1115) was introduced on Friday by Reps. Randy Hultgren, R-Ill., Richard Neal, D-Mass., and Jim Renacci, R-Ohio. Neal is the top Democrat on the House Ways and Means Committee and Renacci is also a committee member.

Qualified small issue manufacturing bonds, also called small issue industrial development bonds (IDBs), are private activity bonds used to finance manufacturing facilities and related projects for small and mid -manufacturers. The federal law governing these bonds has not been updated in nearly 30 years.

The bill would expand the number of projects that are eligible for IDB financing. The three congressmen introduced similar legislation in 2015 but it failed to move forward. Hultgren and Neal offered a bill in 2014 as well.

"Illinois' manufacturers are ready for the challenge of increasing engagement in our global and technology-based economy," Hultgren said in a release. "Unfortunately, decades-old policies governing a key tool that manufacturers used to expand operations no longer address today's challenges, needlessly impeding growth and job creation in the Illinois manufacturing sector.

MAMBA is a bipartisan bill that sensibly reforms these outdated rules without raising taxes."

"It's vitally important that Congress does all it can to support the American manufacturing industry," Neal said. MAMBA "is a commonsense, bipartisan proposal that will ensure the struggling manufacturers in New England and across the country have access to the resources and capital they need to invest in their businesses and hire more workers in their local communities."

The bill would expand the definition of manufacturing facilities to include those that produce intangible property, such as software and patents, as well as tangible property. It would also allow IDBs to be used to finance facilities that are functionally related and subordinate to the production of tangible or intangible property, such as warehouses that temporarily store materials or laboratories that test raw materials. These provisions were in effect in 2009 and 2010 under the American Recovery and Reinvestment Act but expired.

The bill would increase the maximum size of an IDB issue to $30 million from $10 million. It also would increase IDBs' six year capital expenditure limit to $40 million from $20 million.

Currently a manufacturer can only issue IDBs for a project if their capital expenditures, including the bonds proceeds, would not be more than $20 million during six years – three years before the bonds are issued and three years after that.

The bill has the support of the Council of Development Finance Agencies. "We're thrilled that MAMBA has been reintroduced. It's a vital piece of legislation that will help lower the barriers for small manufacturers to access affordable capital," said CDFA president and CEO Toby Rittner.

"Representatives Hultgren, Neal, and Renacci have been great champions of manufacturing bonds and the development finance industry as a whole, and I'm thankful for their commitment to American manufacturing."

The bill, which also has the support of the Illinois Manufacturers' Association, is pending before the House Ways and Means Committee.

The Bond Buyer

By Lynn Hume

February 21, 2017

TIF Jurisdiction, Future Projects Among County Officials' Annexation Concerns.

Officials say existing Monroe County, Ind., tax increment financing districts will remain under the jurisdiction of the Monroe County Redevelopment Commission even if the city annexes areas within them.

County attorney Jeff Cockerill said the areas proposed for annexation touch all of the county's tax increment financing more commonly known as TIF districts. If there is existing debt in a TIF district, it would be treated as if annexation did not occur. That is, the county would still accumulate TIF revenue that could be used to make existing bond payments within the district as well as accumulate funds to use toward projects such as building roads.

However, by state law, if a road is annexed into the city, then it becomes a city road, Cockerill said.

If annexation is approved, the city would also collect revenue due to increased assessed value.

In addition, the city could see increased revenue from other sources as well, such as an increase in road mileage, equating to more motor vehicle highway revenue.

The county has existing debts for its Westside and Bloomington Township/Ind. 46 TIF districts.

For the Westside TIF district, where the commission has concentrated a number of its recent infrastructure projects, its last bond expires in 2040. At this time, there are no projects scheduled for the Bloomington Township/Ind. 46 district.

The Fullerton Pike TIF district is the only area that does not have any current debt. Within it, the county is preparing to begin construction on phase I of the Fullerton Pike project, starting just west of where Gordon Pike and Rhorer Road intersect with South Walnut Street and heading east to just beyond where the road intersects with Walnut Street Pike. Cockerill said the county is still investigating what would happen if the commission decides to issue a new bond for that area.

Barry Lessow, a redevelopment commission member, said knowing this, questions that remain include whether the commission wants to continue making investments in areas that they know would later fall into the city's jurisdiction and whether to invest in areas within the TIF districts that are outside of the areas proposed for annexation.

Jim Shelton, a fellow redevelopment commission member, said such questions are why collaboration with the city is important.

"I don't see we do anything necessarily different except we extend an invitation to the city to participate," Shelton said. "As a community, we can't get hung up whether it is in the city or county or not."

Public Works Director Lisa Ridge said a number of the road projects the redevelopment commission is looking to do within the Westside TIF district were suggested to help all area residents, regardless of jurisdiction. She said such projects for instance, extending Profile Parkway are meant to address connectivity issues and relieve traffic congestion in an area changing due to nearby construction of Interstate 69.

But Lessow agrees conversation with the city is essential to ensure clarity about any actions that might influence the districts later.

Redevelopment commission member Richard Martin said the county board knows the area much better than city officials do, which was very evident from the questions city officials had about the areas proposed for annexation.

"They just don't know enough at this point, and we need to educate them," Martin said.

The Bond Buyer

By Ernest Rollins

February 16, 2017

BlackRock's Carney Says Tax Reform Won't Hurt Munis.

Sean Carney, head of municipal strategy at BlackRock, and Bob Michele, chief investment officer at JPMorgan Asset Management, discuss how U.S. tax reform may impact the tax advantage of municipal bonds. They speak on "Bloomberg Daybreak: Americas."

Watch video.

Bloomberg

February 23, 2017

Bank of America to Trump: Taxing Munis Won't Raise Very Much.

- Bank reckons the tax break costs less than official estimate
- Mayors previously said Trump backs keeping munis tax exempt

If President Donald Trump and Congressional Republicans are looking for revenue to offset planned tax cuts, Bank of America Merrill Lynch analysts say taxing investors' interest on state and local debt wouldn't provide as much as it seems.

The tax break for the $3.8 trillion municipal market — which holds down the expense of financing state and local projects — cost the federal government about $39 billion in 2016, according to the U.S. Treasury Department's figures.

But Bank of America analysts led by Phil Fischer estimate that the revenue raised by repealing it would be much lower. Because taxing the interest would likely cause individual investors to move money elsewhere, many securities would wind up with buyers who don't pay income tax, such as overseas firms or 401(K) plans. Once that's factored in, taxing municipal bonds may only yield about $8.9 billion a year, the analysts reckon.

Moreover, the shift would foist about $7.6 billion of extra costs on state and local governments, assuming yields rise about 0.2 percentage points. That would push up the expense of financing the types of infrastructure projects Trump has vowed to promote.

The bonds have been targeted by previous proposals that stalled in Congress. Former President Barack Obama sought to cap the benefits the wealthiest earners can receive from municipal debt, while a deficit-cutting panel previously suggested eliminating the exemption outright. Lobbyists for state and local-government groups have fiercely opposed any change to the tax treatment of their bonds, given the cost it may impose.

"Hopefully, this helps clarify the point that the attack on the tax-exempt status of municipal bonds from time to time appears to be based more on political calculus than economic analysis," the analysts wrote. "This is becoming more widely recognized and we do not expect that the tax exemption would be targeted in any tax-reform legislation."

The president may agree: A delegation of mayors, after meeting with Trump in December, said he expressed support for keeping the tax break intact.

Bloomberg Markets

by Jordyn Holman

February 27, 2017, 11:30 AM PST February 27, 2017, 1:46 PM PST

[The Countdown to August 18, 2017 – Something You Should Know.]

The IRS has over the past three years issued significant guidance on the safe harbors from private business use for management contracts, and we've been dutifully reporting on this guidance (here, here, here, and here). This guidance has generally been well received, but some issues remain. In addition to questions raised by Bob Eidnier in his post a few weeks ago (link above), the recent spate of IRS guidance raises a concern that is the subject of this post. By correlating the permitted length of management contracts with the economic lives of the managed property, some management contracts that are materially modified after August 18, 2017 might not fit within the New Safe Harbors (defined below) even if the term of the modified contract is unchanged from the prior iteration!! (Tax lawyers use exclamation points to try and keep people awake).

Continue reading.

The Public Finance Tax Blog

By Joel Swearingen on February 25, 2017

Squire Patton Boggs

Senators Call for Tax Relief for Water Conservation Rebates.

Washington—Senators Dianne Feinstein (D-Calif.), Patty Murray (D-Wash.) and Michael Bennet (D-Colo.) today called on Treasury Secretary Jack Lew to confirm tax relief for individuals who receive water conservation and storm water management rebates that also result in energy conservation. These rebates have been treated as income but should qualify under an existing exemption in the tax code for energy conservation measures.

The senators wrote: **"There are many challenges impacting our nation's water supplies, and it is imperative to maintain the effectiveness of incentives for residents to participate in water efficiency and storm water management programs. We would like to request that you clarify that in cases where a public utility can attest to energy savings from water conservation and storm water management measures, such rebates issued by a public utility can be excluded from gross income under Section 136. This is in line with the process many utilities already follow for energy conservation measures."**

The full text of the letter follows:

December 20, 2016

The Honorable Secretary Jacob J. Lew
Department of Treasury
1500 Pennsylvania Avenue NW
Washington, DC 20220

Dear Secretary Lew:

We are writing to follow up on our May 26, 2016, correspondence to request that the Department of the Treasury consider additional information in determining whether water conservation rebates and storm water management rebates, including the installation of green infrastructure, could be excluded from residents' taxable income. Since our initial correspondence to you, we have received additional information showing significant, measurable energy savings that result from water conservation. Given the compelling data we have received, we now have reason to believe that water conservation rebates should be considered exempt from inclusion in gross income under 26 U.S.C. § 136 (Section 136), which provides such an exemption for energy conservation measures.

We have attached a letter from the Director of the Center for Water-Energy Efficiency at the University of California, Davis, which details the Center's findings that water conservation in California in Summer 2015 resulted in energy savings equivalent to those of energy efficiency programs. Notably, their research found that water conservation-related greenhouse gas savings over the Summer of 2015 were equivalent to taking about 50,000 cars off the road for a year. Additionally, The Los Angeles Department of Water and Power has estimated total energy savings of approximately 24,400 MWh for fiscal year 2015/16 from the residential and commercial indoor and outdoor water conservation rebates that it provides. These figures are even higher after including energy savings from hot water heating and other customer end uses. In Colorado, water utilities have also been working to implement conservation programs that have the benefit of saving water and electricity or natural gas, including residential shower head exchange programs. Similar conservation measures are underway at urban utilities throughout the country, including in Arizona, Nevada, and Washington.

Section 136 was added in 1992, when there was a clear line between energy and water conservation. Today, that distinction is largely gone and the nexus between saving water and saving energy has been established. Commissioner Lopez of the Bureau of Reclamation has stated, "[W]ater and energy efficiency are intrinsically linked. When we conserve water, we conserve the energy it takes to move it." Water conservation also results in other energy savings, including reductions in energy use for heating and for treatment. We believe the federal agencies involved in energy and water conservation and the Department of the Treasury currently have the authority to interpret Section 136 more broadly.

It appears that many, if not all, water conservation rebates result in per capita energy savings. The same is true of rebates designed to collect, treat, and use storm water or reduce storm water inflows into combined sewers. There are many challenges impacting our nation's water supplies, and it is imperative to maintain the effectiveness of incentives for residents to participate in water efficiency and storm water management programs. We would like to request that you clarify that in cases where a public utility can attest to energy savings from water conservation and storm water management measures, such rebates issued by a public utility can be excluded from gross income under Section 136. This is in line with the process many utilities already follow for energy conservation measures.

We look forward to working with you to ensure the success of water conservation and water quality efforts in our states.

Sincerely,

Dianne Feinstein
U.S. Senator

Patty Murray
U.S. Senator

Michael Bennet

U.S. Senator

Municipal Bonds May Get Taxed If Border Tax Plan Fails.

Odds that interest on municipal bonds will continue to be exempt from federal taxes decrease if Congress doesn't approve a plan to alter the way imports and exports are taxed.

That's a concern for municipal-bond investors, as well as the state and local governments trying to get investors to buy their debt notes to pay for roads, bridges and other large public projects.

The Republican-controlled Congress is attempting to draft a revenue-neutral tax package to send to President Donald Trump this year, and a question remains as to whether border adjustments, which tax imports and exempt exports, will be included.

A revenue-neutral tax plan enables GOP lawmakers to pass a tax plan by a simple majority vote, without need of support from any Democratic members.

"If the border-adjustability piece, which raises close to a trillion dollars, is not completed, and we've heard mixed views on that, then everything is on the table," including the exemption for municipal-bond interest, Jim Febeo, senior vice president of government relations at Fidelity Investments, said at a Feb. 13 meeting of the National Association of State Treasurers (NAST) in Washington.

Retailers are lobbying against border adjustments, as is Koch Industries Inc., a financial supporter of conservative causes and candidates.

Some senators, including John Cornyn (R-Texas), Mike Lee (R-Utah) and Finance Committee Chairman Orrin G. Hatch (R-Utah), have said they have questions about the proposal, the details of which haven't been fleshed out.

Money for Change

House Speaker Paul D. Ryan (R-Wis.), who put forth the idea, has said the $1 trillion or so raised by border adjustments would allow for sweeping changes to federal taxes.

Without the money, "the municipal-bond exemption will be looked at," Susan Hirschmann, chief executive officer of Williams & Jensen, a Washington-based lobbying firm, said during the NAST event.

"There is a lack of clarity right now as to whether the Senate supports border adjustments, and there is a lack of clarity on whether President Trump supports it," Hirschmann said.

States Will Fight Back

State and local governments, which depend on bonds, will fight for the tax exemption, Charles S. Henck, a Ballard Spahr LLP partner who practices in public finance and tax law, told Bloomberg BNA.

"State and local governments will want to preserve the existing rule for tax exemption of municipal bond interest because to eliminate it would increase the cost of borrowing," Henck said.

Arizona Treasurer Jeff DeWit, who spoke at the NAST meeting, said states shouldn't worry because the exemption is too popular and the potential backlash against congressional members is too great.

“I don’t think the municipal exemption will be on the table,” he said. “Everyone is against doing that. If they really start to play with it, I don’t think that will truly be on the table. Maybe for leverage.”

‘Everything’ on Table

As House and Senate Republicans work on a package that appeals to Trump, elements of a 2014 tax plan offered by then-Rep. Dave Camp (R-Mich.) may give hints to “where we may be headed,” Febeo said. Camp’s plan proposed a 10 percent surtax on municipal-bond interest.

“I wish I had a crystal ball, but everything seems to be on the table right now,” he said.

According to a delegation from the U.S. Conference of Mayors, Trump expressed support for maintaining the tax exemption in the weeks before his inauguration. Others close to him, however, don’t support it.

Trump’s nominee for Commerce secretary, private equity investor Wilbur Ross, has said municipal bonds aren’t an efficient way to pay for public projects. One reason is that a percentage of the money goes to the bondholder. He has suggested private-public partnerships and tax credits to investors and construction companies to finance bridges, roads and other public projects.

Bloomberg BNA Tax Management

By Che Odom

February 17, 2016

To contact the reporter on this story: Che Odom in Washington at COdom@bna.com

To contact the editor responsible for this story: Ryan C. Tuck at rtuck@bna.com

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Tax Guidance to Slow Under Trump. Even More Emphasis on Letter Rulings in Bond Transactions?

As the Trump Administration attempts to substantially reduce the amount of federal regulations, both the Deputy Tax Legislative Counsel of the Treasury Department and an Associate Chief Counsel at the Internal Revenue Service indicated this week that we are likely to see a virtual halt to formal tax law “guidance” for the foreseeable future. Such guidance includes regulations, revenue rulings, and revenue procedures, the principal means by which Treasury and IRS provide interpretations of tax statutes. However, both officials stated that the IRS will continue to provide taxpayer-specific private letter rulings (PLRs).

In addition to more PLRs being requested to resolve ambiguities in connection with particular transactions, the freezing of the formal guidance process could result in PLRs being given more weight than ever in the analysis of other transactions. Not only will bond attorneys have more incentive to read and rely upon the only available tea leaves as to the IRS’s position, but IRS attorneys may write more substantive letter rulings with the expectation that they will guide practice beyond the particular transactions being ruled upon. While officially non-precedential, PLRs have long been of particular importance in the tax-exempt bond practice, where formal guidance is slow and case law is almost nonexistent.

The National Law Review

Wednesday, February 15, 2017

Support for Munis Seen on Capitol Hill; Tax Reform May Be Next Year.

WASHINGTON – Two corporate executives and lobbyists told treasurers meeting here on Monday that they are hearing positive things about municipal bonds from legislative staffers, but a senior tax staffer from the Senate Finance Committee said tax reform may slip into 2018.

Larry Chadwick, vice president of federal government relations for TIAA, said he has found support for munis on Capitol Hill. “We think municipal bonds are a critical funding mechanism for infrastructure,” he said during a tax reform panel at the National Association of State Treasurers 2017 Legislative Conference.

Chadwick and other panelists, including a senior staffer for the Senate Finance Committee, said the key issue for the Trump administration and the Republican-led Congress is economic growth and infrastructure is viewed as the path for job creation and economic growth.

“I don’t think we’ll see tax reform without a serious infrastructure piece,” the tax staffer said.

Chadwick said he would like to see Congress eliminate or ease the proration provision of the federal tax code so life insurance companies could buy more municipal bonds used for infrastructure.

Pierce Scranton, executive director for global relations & public policy at JPMorgan Chase, said, “The municipal bond [interest] exclusion seems to be in pretty good shape.”

But Scranton cautioned, as did the other panelists, that with tax reform, “We’re in an environment where everything is on the table.”

Though a number of House Republicans talk about having tax reform legislation in August, the senior tax staffer said there are a number of obstacles to that and it may be pushed into 2018.

Nothing will happen with tax reform until the Republicans in Congress and the administration follow through with plans to repeal and replace the Affordable Care Act, the senior tax staffer said at the National Association of State Treasurers 2017 Legislative Conference here.

The lawmakers have to resolve the ACA issue, even if they do something less than repeal and replace or decide they can’t do anything and leave it alone, he said.

Legislatively things are already moving slowly, as lawmakers found they could not get support for repeal without some sort of replacement, the tax staffer said. Trump’s cabinet officials are not in place, though Congress confirmed Steve Mnuchin as Treasury Secretary Monday night, with only one Democrat, Sen. Joe Manchin, D-W.Va., voting for him. Given the Democrats’ opposition to

Trump's nominees, including Mnuchin, there may be battles over assistant secretary positions, he said. Treasury's assistant for policy typically quarterbacks tax reform, he said.

Republican lawmakers hope to repeal and replace the ACA, as well as comprehensively reform the federal tax code, through the budget reconciliation process to expedite the legislation and get it through the Senate with only 51 instead of 60 votes. Normal legislation needs 60 votes to limit debate, avoid a filibuster and move forward. But reconciliation is only for legislation that changes spending, revenues and the federal debt limit. And provisions in a reconciliation bill cannot increase the deficit during a second 10-year window – two challenges to using that legislative vehicle.

The budget resolution for fiscal 2017 includes the ACA, but not tax reform. If Congress wants to do comprehensive tax reform through the reconciliation process, it will have to be for fiscal 2018. But it cannot start the process for fiscal 2018 until it finishes reconciliation for fiscal 2017.

Congress must also deal with other potentially controversial issues during the next few months. It will need to increase the federal debt limit on March 15. Also the latest continuing resolution keeping federal spending going in the absence of appropriations bills will expire on April 28, the tax staffer noted.

A "wild card" for any congressional action is April 30 expiration of legislation that temporarily shored up health care and pension benefits for retired miners. Manchin stopped work on the last CR until lawmakers provided the short-term fix. "Keep your eye on that," the tax staffer said.

Key financial issues will also affect how tax reform plays out, the staffer said. If the border adjustment tax envisioned in the Republican blueprint for tax reform doesn't pan out, then the $1 trillion in revenues it was to bring in will have to be found elsewhere. "If it fails, we'll need a whole lot of money from a lot of sources," the tax staffer said.

Medicaid is another issue to watch, he said, adding how it is dealt with in ACA action will also affect revenues for tax reform.

"But don't underestimate the president, the tax staffer said. If Trump decides to throw his weight behind tax reform, he can do a lot to push it forward, he said. The president has promised a phenomenal announcement on tax soon.

The Bond Buyer

By Lynn Hume

February 14, 2017

Membership Substitution Transactions – Why Are They So Misunderstood?

Membership substitution transactions are the most common form of business combination transaction in the nonprofit hospital industry. They are also widely misunderstood and the source of many mistakes. Many large 501(c)(3)s have become more acquisitive as a result of economic pressures of the ACA. Nonprofit health systems have been getting much better at participating in and winning competitive sale processes, resulting in an increased use of this business combination form.

In April 2013, St. Luke's Episcopal Health System announced its sale, via membership substitution, to Catholic Health Initiatives. In responding to a suit from physician owners (a minority faction) of a St. Luke's subsidiary, St. Luke's Sugar Land Hospital, St. Luke's attorney asserted: "the ownership of St. Luke's Sugar Land Hospital is totally unchanged by the Transaction." We have no opinion on this legal debate, but it points out something that repeatedly arises in these transactions – most participants don't really understand them to any depth.

Given the forecasted level of nonprofit hospital M&A activity in the coming years, as well as the increased use of the membership substitution specifically, it is important that these new and often inexperienced participants consider the implications of the structure. This article will explore the membership substitution structure – its history, use, pros, cons, and potential future applications. Issues such the impact on one's credit stature, bond covenants, and the legal handling of consolidating Master Trust Indentures are reviewed.

Description

Fundamentally, there are two means to acquire ownership and control of a company. One can either buy the assets of the business or its stock. Membership substitutions are analogous to a stock sale in corporate finance. A majority of public company mergers are completed via the acquisition of equity. Classic examples include Proctor and Gamble's acquisition of Gillette and Berkshire Hathaway's purchase of Heinz. In these arrangements, the legal entity of the target (Gillette and Heinz) remains intact with a new parent "stepping into Seller's shoes" as sole owner. This transaction structure has several advantages:

- It creates *successorship* for contractual agreements – employment, collective bargaining, management teams and similar operational matters are preserved.
- Business operations are uninterrupted – licensures, working capital, and leases are unchanged.
- The acquisition process is streamlined – timing and due diligence are simplified, regulatory scrutiny can be eased, and often there is no need for wind down corporation.
- Pensions, swaps, and other liabilities continue as a going concern – no need to terminate with the PBGC or unwind costly derivative instruments.
- Debt issues – avoid pre-payment penalties and defeasance costs associated with today's low interest rate environment.
- No need for tail insurance – beneficial if confronted with Stark or compliance issues that cause such coverage to be unattainable or unduly expensive.

It is easy to see that selling the stock of a business has certain advantages to sellers related to simplifying the transaction and costs. Conversely, buyers commonly prefer to acquire assets as it limits real and theoretical future legal obligations.

Asset purchase transactions certainly have merit as well. In industries with significant intellectual property, e.g., technology, this more focused structure can isolate certain attractive assets and exclude other components of the business. For the same reason, divestitures of a subsidiary division within a conglomerate are generally acquired via a purchase of assets.

Governance

In a membership substitution model, typically the buyer will become the sole equity holder (or "membership interest" in nonprofit language) of the seller. As a result, the buyer will achieve full ownership and control of the seller. Think of this relationship much like that of a parent company and subsidiary, where the parent ultimately retains senior controls of the subsidiary. In connection with a member substitution transaction, the bylaws of each of the buyer and seller will be amended and restated in order to reflect the new governance structure and to provide for reserve powers that rest with the buyer. Oftentimes, the seller may negotiate with the Buyer to have a limited minority number of board seats on the buyer's board.

Forms of Consideration

In either a membership substitution or asset sale, there are generally three forms of economic consideration that the buyer provides to the seller of a hospital: (1) a purchase price, (2) assumption of liabilities, and (3) a commitment to spend capital in the future. Together, the sum of these must equate to "fair market value." The mixture of these forms varies based on the capital structure of the target and objectives of the parties. In a nonprofit to nonprofit membership substitution, a purchase price is rarely paid, instead the Seller is relieved of its financial liabilities and secures a commitment to invest capital in the future. In many cases, nonprofit Buyers are now the highest bidders in sale processes due to: (1) the high use of financial leverage, and (2) the strategic importance of growth. So while for-profit conversations were popular a decade ago to extract a purchase price and create a community foundation with the proceeds, today the total economic consideration of a membership substitution transaction is often equal or greater. Evidence of the achievement of "fair market value" is critical to defend the transaction to any critics, notably the state attorney general.

Financial Features

- All assets are conveyed to the buyer.
- All liabilities should be assumed or guaranteed by the buyer.
- Capital expenditures are committed by the buyer for routine and strategic needs in the future.
- Rarely are charitable foundations created, if so it is most always restricted to supporting the hospital.

Liabilities of the new subsidiary either remain in place by being assumed or guaranteed by the new parent company (as part of the obligated group), or are retired via refinancing. Issues associated with assuming the debt can include intercompany loans (potentially with interest), a support or guarantee arrangement, or inclusion or exclusion within the system's obligated group.

Similarly, the handling of balance sheet assets is also customized for each setting. Can the cash be swept to corporate treasury? Who controls the foundation, where is it housed, who gets to select grant donations? Will the capital commitment be infused into the local subsidiary or simply be funded through retained free cash flow?

As a result of the change in the organizational structure, it is important for each party to review its Master Trust Indenture, as well as any and all material documents ancillary to or apart from the Master Trust Indenture between a bondholder and any member of the obligated group. With the assistance of investment bankers and legal counsel, the parties will want to determine whether each Master Trust Indenture may remain in place, and if so, whether this is the desired approach. Alternatively, the parties may determine that it is in the best interests of the combined organization and permitted pursuant to the terms of the Master Trust Indentures to consolidate the debt under one Master Trust Indenture. If consolidation is permitted and desired, then the parties will want to determine under which Master Trust Indenture they wish to proceed post-closing. For example, it may be advantageous to the parties to consolidate the debt under one of the Master Trust Indentures in order to take advantage of less restrictive and less burdensome covenants. In addition, there may be significant savings by capitalizing upon a more favorable cost-of-capital under one Master Trust Indenture over another.

The parties should also have an understanding of how the consolidation may affect the rating of the bonds as a result of the combination, which will require a review of the rating agencies on analysis of pro-forma ratios. As part of the review of the documents, the parties also will want to identify any consents that may be required of the bondholders and develop a timeline for reaching out to and obtaining such consents of the bondholders. Regardless of whether consent is required, there may be other covenants required by the Master Trust Indenture or ancillary documents, such as the delivery of legal opinions, officer's certificates and posting of additional collateral of which the parties should be aware. Finally, the parties will want to understand the terms of any other debt outside the Master Trust Indentures (including any swaps) that may be outstanding to determine if the combination will be in violation of any covenants, and consider whether it is best to obtain consent or alternatively, redeem or pay off such debt.

As a result of the modified structure via a membership substitution, the parties will need to review the contracts to determine whether the change of control will trigger any consent requirements of third parties, any terminations or defaults under any agreements or rights of first refusals. The parties will want to ensure that they abide by the terms of their agreements with third parties. In addition, in the event that the parties are members or partners in a joint venture, there may be transfer and consent requirements that are triggered as a result of the change of controls. Further, the parties will want to carefully review their contracts for non-competition restrictions, non-solicit restrictions and confidentiality provisions to fully understand the implications of the change of control.

Misnomers

Most of the confusion surrounding this structure in the nonprofit world centers on whether the parties acknowledge that a sale is occurring. Often there are incentives to obfuscate reality, namely easing the public relations messaging locally.

Part of the uniqueness of the membership substitution is the nonprofit nature of the partners entering the transaction. While for profit enterprises can access and variety of equity, debt, and synthetic markets to raise capital to finance strategic growth, nonprofit hospital companies are typically limited to the tax-exempt municipal bond market. Buyers of institutional debt are heavily reliant on credit rating (rather than growth prospects in the equity markets) in determination of the cost of capital or required yield. As a result, hospitals, and nonprofits generally tend to be more conservative with capital and have an affinity toward creative relationships to increase market share, revenue, and ultimately profits while not diluting one's rating and thus ability to raise capital.

Sellers are becoming more sophisticated, however, and are questioning what they're getting in return for selling their hospital. The give-away transactions of yesteryear are not likely to be repeated in the era of more commercially oriented partners.

Conclusion

From our standpoint, it seems as though M&A techniques in the nonprofit hospital industry are given too much credit for their uniqueness. Much of this stems from a heartfelt belief that M&A transactions in the nonprofit world are completed on more friendly terms. As the stakes get higher in the increasingly capital intensive, regulated, and complicated hospital industry, however, this is changing. Transactions now seem more adherent to corporate norms – following SEC conventions and Delaware Law. Negotiations surrounding the accounting treatment of financial statements and technical topics such as representations and warranties, escrows, and breakup fees are becoming more common. Overall, it seems like the cottage hospital M&A business is maturing and taking on characteristics of public company transactions.

The Bond Buyer

By Ken Marlow and Rex Burgdorfer and Alex Voss

February 14, 2017

Ken Marlow is a partner and chair of the healthcare department at Waller Lansden Dortch & Davis in Nashville, Tenn. Rex Burgdorfer and Alex Voss are with Juniper Advisory in Chicago, a specialized investment banking firm focused exclusively on hospital M&A. Sources for this research include Waller Lansden and Juniper Advisory's M&A experience, as well as information compiled by The Harvard Business Review, The American Bar Associate, and Latham & Watkins studies.

New Proposed Legislation: PABs for Social Infrastructure and a Ban on Stadium Bonds.

The new Congressional session is heating up, and we'll cover two new pieces of proposed legislation below. For the first time in several years, we can avoid giving the usual disclaimer that any new piece of legislation is "likely going nowhere." Tax reform appears to be a real possibility for the first time in many years, and it will probably involve expansions of some areas of the tax-exempt bond world and contractions of others. The two bills discussed below are an example of each.

The first bill would allow tax-exempt private activity bond financing for public buildings that have too much private involvement. The second bill goes in the other direction, and would forbid governmental bond financing for stadiums, which, as we'll see, would have the effect of preventing tax-exempt financing of any kind for stadiums.

We are continuing to work with our industry-leading public policy group to study the many new legislative developments that are sure to arise, and we will use the blog to provide resources and reactions to them.

Continue reading.

The Public Finance Tax Blog

By Johnny Hutchinson on February 17, 2017

Squire Patton Boggs

BlackRock's Hayes Says Trump Unlikely to End Muni-Bond Tax Break.

- Trump's plans to cut taxes could curb demand for local debt
- Elimination of tax-exemption 'highly unlikely,' Hayes says

Peter Hayes, who oversees municipal-bond investments for BlackRock Inc., the world's largest money manager, doesn't think President Donald Trump and the Republican-led Congress will do away with the tax break given to buyers of state and local government debt.

"The tax exemption of municipal bond interest is a key draw for issuers. And while it may be deemed alterable, we don't see it as dispensable," Hayes said in a blog post on the company's website. "We see the elimination of muni tax exemption as highly unlikely."

Speculation that Washington will move to tax the interest investors receive in the $3.8 trillion municipal market has increased since Trump's election, given that the revenue could help cover the cost of cutting corporate and individual income taxes. Former President Barack Obama proposed capping the benefits the wealthiest earners can receive from municipal bonds, though the plan stalled in Congress, and a deficit-cutting panel once proposed eliminating the tax exemption outright.

Such change would lead investors to demand higher yields on municipal bonds than they do now, an outcome that may be at odds with Trump's other goal of increasing spending on infrastructure projects.

That doesn't mean the municipal market will be spared the effects of any tax changes: Cutting income-tax rates would also lessen the appeal of the securities. But such reductions may not come this year, as lawmakers focus first on overhauling corporate taxes, according to BlackRock's Hayes.

"The individual tax code is very complicated and politically difficult to amend, even under one-party control," he wrote. "Change may well come, but not likely in 2017 as Washington focuses on the comparatively easier task of corporate tax reform."

Bloomberg

by Jordyn Holman

February 14, 2017, 10:48 AM PST

TAX - IOWA

[Acciona Windpower North America, LLC v. City of West Branch, Iowa]

United States Court of Appeals, Eighth Circuit - February 7, 2017 - F.3d - 2017 WL 490412

Wind turbine manufacturer brought action against city, alleging breach of tax increment financing (TIF) development agreement for urban renewal project.

After entry of partial summary judgment in manufacturer's favor, bench trial was held. The United States District Court entered judgment in manufacturer's favor, and city appealed.

The Court of Appeals held that:

- City was obligated by TIF development agreement to pay tax rebate to manufacturer once it paid its taxes for given fiscal year;
- Manufacturer did not make judicial admission that rebates were never appropriated;
- TIF agreement did not impermissibly limit city's ability to decline to pay rebates; and
- District court did not abuse its discretion in permitting manufacturer to change its damages calculation on eve of trial and declining to impose sanctions.

Under Iowa law, city was obligated by tax increment financing (TIF) development agreement to pay tax rebate to wind turbine manufacturer once it paid its taxes for given fiscal year, even though agreement provided that all rebate payments were "subject to annual appropriation of the City

Council," where agreement specified that city was required to annually certify "amount obligated for appropriation for rebate," and that, if city decided to obligate rebate for appropriation, "rebate shall be paid to [manufacturer] within thirty days of receipt by the City of the incremental taxes paid."

In manufacturer's action against city for breach of tax increment financing (TIF) development agreement, manufacturer's statement in its summary judgment papers that it was undisputed that "City did not appropriate the $265,140 rebate" to be paid to it for fiscal year was best read as poorly worded effort to admit that it is undisputed that rebates were never paid, rather than as judicial admission that rebates were never appropriated, where manufacturer had always argued that rebate was appropriated, just not paid.

Under Iowa law, tax increment financing (TIF) development agreement that required city to pay tax rebate to wind turbine manufacturer once it paid its taxes for given fiscal year did not impermissibly limit city's ability to decline to pay rebates. TIF agreements were clearly authorized by state law and were to be liberally construed.

District court did not abuse its discretion in permitting manufacturer to change its damages calculation on eve of trial and declining to impose sanctions in its action against city for breach of tax increment financing (TIF) development agreement, despite city's contention that manufacturer revealed too late that it would seek damages for two fiscal years, where manufacturer sought compensatory damages for multiple fiscal years from beginning of its lawsuit, its pretrial clarification that it would seek compensatory damages for both fiscal years was entirely consistent with theory of damages it articulated at outset of case, and damages calculation used by manufacturer appeared to have been based on information in parties' agreement and documents originally in city's control.

Why Some Bargain Municipal Bonds Aren't Tax Free.

When individuals invest in municipal bonds they expect 100% tax-free income. Right? Well, many may unknowingly be setting themselves up for a tax bill from the IRS. How can this be? After all, we're talking munis.

It's been many years since the municipal bond De Minimis rule was relevant. Here's how it works in plain English: Say you purchase a low coupon municipal bond for a 2%, 2.25%, 2.50%, or even 3% coupon at a discount from the face value in the secondary market. If that discount breaches the IRS De Minimis threshold, then a portion of that discount can be taxed as ordinary income.

It all depends on how deeply the bond price is discounted. The simple formula to compute the De Minimis threshold is:

De Minimis threshold = Lower of par or original issue discount – (.25% X the years to maturity)

The formula basically stipulates that if you purchase a bond at a discount and the discount is equal to or greater than a quarter of a point per year until maturity, then your gain at redemption is taxed at your ordinary income tax rate rather than the more favorable capital gains rate, which are as low as 15%.

If this sounds like IRS gobbledygook, you are right. The law was created to prevent taxpayers from converting ordinary income into capital gains. Remember the only IRS rule you should commit to memory is: Whatever is best for the government and worst for the taxpayer is the correct rule interpretation .

Here's an example: Assume you purchased 50 XYZ Unified School District municipals, 2.00% coupon maturing September 1, 2028 originally issued at par, 100. If you purchased the bonds in the secondary market today at 90.288 for a 3.00% yield-to-maturity because rates rose since issuance, you will owe $2,107.50 in tax on $50,000 face value of the bonds.

The market discount cutoff price was $97.25. Okay—paying $2,107.50 in tax on 50 munis isn't the end of the world. Still, it could blindside you if your weren't aware of the De Minimis rule.
Your rule of thumb for purchasing municipal bonds should now be: If you want all your return to be tax free then invest in higher coupon bonds at par or a slight premium.

Stay away from market discounted munis. If you're doing business with a retail broker ask them to run the analytics on Bloomberg. That will quickly compute your tax liability if purchasing at a discounted price.

One caution: If interest rates rise significantly, high coupon premium bonds can decline and breach the De Minimis threshold too.

The De Minimis rule also has a significant impact on your bond price. Should you decide to sell a bond subject to the De Minimis rule your sale of the bond will be at an even deeper discount. The buyer will demand compensation for that portion of their [now] taxable return.

The reason we have not been plagued until recently with the De Minimis rule is that issuers weren't issuing many 2%, 2.25%, 2.50%, or 3% municipal bonds until 2016 when yields touched such low levels. Then post-election muni yields rose and prices declined.

If you buy munis online and your platform does not supply a De Minimis calculator better get out your pencil and paper for hand computations. There are numerous articles online written by Piper Jaffray, Pimco, Schwab, RBC and others explaining the formulas and with grids showing allowable market discounts before treatment as ordinary income kicks in.

Let this column be a red flag warning: The De Minimis rule can bite the incautious. Oh…and if you think no one will notice the discounted price you paid, the 1099s issued by the brokerage industry are extremely accurate in their reporting to the IRS.

FORBES

by MARILYN COHEN

FEB 7, 2017 @ 11:48 AM

Marilyn Cohen is founder and CEO of Envision Capital Management, a Los Angeles fixed-income money manager.

Heller, Nelson, Kelly and Blumenauer Re-Introduce Bipartisan Public-Private Partnership Bill.

(Washington, DC) – Today, U.S. Senators Dean Heller (R-NV), Bill Nelson (D-FL), Congressman Mike Kelly (R-PA), and Earl Blumenauer (D-OR) released the following statements after re-introducing the

"Public Buildings Renewal Act." The bill enables communities to establish public-private partnerships (P3s) for needed public infrastructure improvements, such as in schools or public universities, by creating $5 billion in new private activity bonds for public buildings.

"In the past, P3 investment has produced enormous benefits across the nation in the form of transportation and infrastructure improvements. I want to see the same results right here in the Silver State, especially for Nevada's schools. Now is the time to use the success of P3s in the infrastructure industry as a financing model for Nevada's public buildings to repair cornerstones in our communities like public schools and libraries. This commonsense idea helps our public schools and universities do even more. By empowering the private sector to address these issues, innovation ensures these projects are completed in a more cost efficient manner," said Senator Dean Heller.

"This bill will help local governments build schools, libraries, fire stations and other public buildings that serve as the foundation of our communities," said Senator Bill Nelson.

"Our country's public buildings are in a historic state of disrepair and in need of a bold solution. That's where the Public Buildings Renewal Act can come to the rescue. This legislation became more urgent than ever for me after I visited several of our district's schools last year and saw the unacceptable damage up close. When public places like schools, hospitals, and court houses are allowed to crumble, the people they serve suffer, especially students. Our bill will channel a new stream of P3 financing into local communities for the ultimate goal of restoring public infrastructure from coast to cast. It will take advantage of private sector efficiency to create jobs and save taxpayer money by streamlining the delivery, design, and construction of these projects. I thank my colleagues in both chambers for supporting this commonsense solution and look forward to helping them advance it swiftly," said Congressman Mike Kelly

"Congress has failed to display the political courage necessary to adequately invest in infrastructure—from roads and light rail to schools and courthouses. Our nation is literally falling apart and falling behind. We need an 'all of the above' approach to infrastructure funding, and simple fixes to lower investment barriers are steps in the right direction," said Congressman Earl Blumenauer (OR-03)

Background:

These newly created private activity bonds mentioned above would provide much-needed financing to cash-strapped states to construct government-owned buildings such as public schools, state colleges, post offices, libraries, prisons and courthouses. Currently, the use of P3s to deliver public buildings is extremely limited because unlike the transportation sector, public buildings are not eligible for private activity bonds. This inhibits public building P3s from combining tax exempt financing with private financing, resulting in an increased cost of financing. Nearly every U.S. transportation P3 project that has moved forward has utilized federal financing, 75% of which have accessed Private Activity Bonds. Over $36 billion in transportation P3 projects have been undertaken since 2010 with a cost savings of nearly 20 percent for each project.

This bill will catalyze the use of P3s in public buildings just as PABs have for transportation. By empowering the private sector to tackle these projects, the bill would make these projects more cost effective, stretching every public dollar further. Additionally, the bill is a fiscally conservative solution to overhauling these public projects with an estimated cost from JCT of less than $50 million over ten years.

The House companion bill is HR 960.

Senator Heller was recently named Chairman of the Senate Committee on Finance's Subcommittee on Energy, Natural Resources, and Infrastructure. This role will give him the ability to promote infrastructure projects in Nevada like Interstate 11.

Bills Would Allow States, Localities to Issue up to $5B of PABs for Public Buildings.

WASHINGTON – House and Senate members have reintroduced companion bills that would allow state and local governments to issue up to $5 billion of private activity bonds to finance the repair or construction of schools and other public buildings under public-private partnership arrangements.

The "Public Buildings Renewal Act" was introduced in the House on Feb. 7 as H.R. 960 by Rep. Mike Kelly, R-Pa., and eight cosponsors, including six members of the House Ways and Means Committee such as Rep. Earl Blumenauer, D-Ore.

The measure in the Senate, which has not been assigned a number yet, is being introduced by Sens. Dean Heller, R-Nev., and Bill Nelson, D-Fla., both of whom sit on the Senate Finance Committee.

The bills they introduced last session were H.R. 5361 and S. 3177.

The legislation would create a new category of tax-exempt PABs that would allow states and localities to construct or renovate government-owned buildings such as public schools, state colleges, post offices, libraries, prisons and courthouses with private parties.

These kinds of projects cannot currently be financed with tax-exempt P3s because there is not a specific qualified PAB category for bonds for public buildings.

"Our country's public buildings are in a historic state of disrepair and in need of a bold solution," Kelly said. "That's where the Public Buildings Renewal Act can come to the rescue."

"Congress has failed to display the political courage to adequately invest in infrastructure – from roads to light rail to schools and courthouses," said Blumenauer. "Our nation is literally falling apart and falling behind. We need an 'all of the above' approach to infrastructure funding and simple fixes to lower investment barriers are steps in the right direction."

The Bond Buyer

By Lynn Hume

February 8, 2017

Senate Panel Told P3s Won't Work for Rural Areas, Tax-Exempts Are Key.

WASHINGTON – Municipal bonds are a "crucial component" of any infrastructure plan and their tax-exempt status must be preserved, a county official from Oklahoma representing the National Association of Counties told members of a Senate committee on Wednesday.

Transportation officials from rural states said during the hearing held by the Senate Environment and Public Works Committee that public-private partnerships won't work for them. The hearing was on "Modernizing our Nation's Infrastructure."

The comments were not exactly an endorsement of President Trump's $1 trillion infrastructure plan to bring in private investment to help finance the repair and development the nation's roads, bridges, and other infrastructure projects.

Cindy Bobbitt, a commissioner of Grant County, Okla., who was representing NACo, told committee members that, "Between 2003 and 2012, counties, states and other localities invested $3.2 trillion in infrastructure through long-term, tax-exempt municipal bonds, 2.5 times more than the federal investment."

Bobbitt, who noted that munis have low default rates and are often approved by both legislatures and the voters, said, "Simply stated, the tax exemption of municipal bond interest from the federal income tax represents one of the best examples of the federal-state-local partnership."

She pointed out that two thirds of the nation's 3,069 counties are considered rural with a combined population of 60 million and face challenges such as declining populations and a limited ability to raise revenue for capital projects.

Among her recommendations were that Congress should make federal highway dollars available for locally owned infrastructure. Local governments own 78% of the nation's road miles, including 43% of federal-aid highways and 50% of the National Bridge Inventory, she said.

Committee chairman Sen. John Barrasso, R-Wyo., asked Bill Panos, the director and CEO of the Wyoming Department of Transportation who also testified, whether rural or smaller states could use Build America Bonds for infrastructure, though they would have to be reauthorized.

"Wyoming has never borrowed for transportation" because its "high cost per capita … discourages borrowing," Panos said. But he later said the state has issued grant anticipation revenue vehicles, or Garvees.

Barrasso said data from the U.S. Treasury Department shows rural states issued a lot of BABs in 2009 and 2010 when they were authorized by the American Recovery and Reinvestment Act. BABs are taxable bonds for which Treasury makes subsidy payments to issuers equal to roughly 35% of their interest costs.

Panos, who was also speaking on behalf of the transportation departments in Idaho, Montana, North Dakota, and South Dakota, some of which issued BABs, told committee members that P3s and other approaches to infrastructure investment that depend on positive revenue streams from projects "are not a surface transportation infrastructure solution for rural states."

P3s would be unlikely to attract investors even with tax credits, he said. Part of the problem is that roads in rural states tend to have relatively low traffic volumes, he said.

Panos said Congress must strengthen the Highway Trust Fund, which will no longer be able to support surface transportation programs after 2020, when funding from the Fixing America's Surface Transportation Act (FAST) ends.

He also said certainty is important for transportation planners. He applauded the FAST Act's providing several years of transportation funding, but said Congress' track record of passing continuing resolutions, restricting funds to the previous years' levels, instead of annual appropriations bills, creates uncertainty.

Sen. Deb Fischer, R-Neb., a committee member, said she's proposed legislation (S. 271) to shore up the Highway Trust Fund and to provide states with more flexibility in how federal funding is spent on infrastructure projects. "I think it's really important to look at a federal revenue source without raising taxes," she said during the hearing. Her bill would transfer revenues from U.S. Customs and Border Protection to the HTF.

"If we have certainty we can make better plans" and that will lead to lower costs, said Shailen Bhatt, executive director of the Colorado Department of Transportation, who also testified.

Most of the witnesses agreed with the current funding formulas that divide federal funds between highway and transit programs and urged that they be continued.

While the committee paid particular attention to the needs of rural areas, Bobbitt pointed out that farms and businesses in agricultural-based rural areas need roads and bridges to deliver products to urban areas. "It's not rural vs. urban," she said, adding, "We're all in this together."

The Bond Buyer

By Lynn Hume

February 8, 2017

The Timeline of Tax Reform and the Danger For Munis.

AUSTIN – Federal tax reform efforts will accelerate in just a few weeks, and municipal market participants need to be pushing hard to protect the muni interest exemption right now, lawyers told attendees at a conference here Thursday.

Speaking at The Bond Buyer's Texas Public Finance Conference luncheon, Bracewell attorneys Curtis Beaulieu and Charles Almond warned that the exemption could be in danger very soon despite President Donald Trump's apparent support for leaving that part of the tax code unchanged. Republicans have been pushing to lower corporate and individual income tax rates, a goal that puts the muni exemption in danger of being limited or eliminated.

The momentum will pick up about six weeks from now, Beaulieu said, when House Ways and Means Committee chair Kevin Brady, R-Texas, releases the first draft of tax reform legislation. This draft, called the "chairman's mark," is crucial for the future of the muni exemption, said Almond. If the mark comes out and does not include a tax exemption for municipal bond interest, the lawyer warned, that means someone on the committee will then have to work to get it in.

"You really want things taken care of in the chairman's mark," Almond said, urging conference attendees to begin lobbying their representatives now if they hadn't already, warning them against waiting weeks to do so. Almond said that the "House blueprint" for tax reform that has already been publicly circulated could already be interpreted as limiting the tax exemption, and proposed eliminating "special-interest" deductions and credits.

A September estimate released by the Treasury pegs federal "tax expenditures" for tax-exempt bonds issued by state and local governments at about $565 billion over the 10-year period from 2017-2026. While that ranks only 15th on Treasury's list of tax expenditures, Almond said it still provides lawmakers with a potentially appealing way of helping to lower tax rates without adding to the deficit.

“To get those rates down, they’re going to go searching for other places to raise revenues,” said Almond.

Beaulieu said that even if the tax exemption is on the table, legislation would still be very unlikely to include a retroactive change to the status of outstanding tax-exempt bonds.

“Republicans typically do not support retroactive tax increases,” Beaulieu said. “So there’s probably no chance.”

Almond downplayed the comfort that market participants can take in then President-Elect Trump’s comments to the U.S. Conference of Mayors in December, during which Trump spoke about his proposed $1 trillion ten-year infrastructure plan and said that he plans to maintain the tax-exempt standing of municipal bonds.

“I don’t think you can rely on anything until it’s Tweeted,” joked Almond.

Beaulieu said that Republicans can pass tax reform legislation on a partisan basis in the House, where they GOP maintains a sizeable majority. But when the discussion moves over to the Senate, he said, Republicans will likely need to abandon their partisan approach and get some Democrats on board. Republicans control 52 Senate seats, but the upper chamber’s rules essentially require 60 votes to pass a bill because of the ability of Senators to filibuster and more easily amend bills they dislike.

“Everything slows down in the Senate,” said Beaulieu.

The Bracewell lawyers’ estimated timeline includes consideration of tax reform legislation by the full House by August. The full Senate could consider it by the end of 2017, and a conference report could produce a joint product by spring 2018.

The Bond Buyer

By Kyle Glazier

February 9, 2017

TAX - CONNECTICUT
Kettle Brook Realty, LLC v. Town of East Windsor
Supreme Court of Connecticut - January 24, 2017 - A.3d - 324 Conn. 544 - 2017 WL 194255

Property owner filed municipal tax appeal seeking reduction in property’s assessed value.

The Superior Court granted town’s motion to dismiss. Property owner appealed. The Appellate Court affirmed. Property filed petition for certification to appeal, which was granted.

The Supreme Court of Connecticut held that appeal was commenced when property owner served appeal documents on municipality, which was outside of two-month deadline, and not when appeal documents were filed with Superior Court, which was within two-month deadline, and thus appeal was untimely.

TAX - NEW HAMPSHIRE

Bishop of Protestant Episcopal Diocese in New Hampshire v. Town of Durham

Supreme Court of New Hampshire - December 9, 2016 - A.3d - 2016 WL 7177763

Church appealed town's assessment of property tax on 24 spaces in church parking lot that church leased to state university students. The Superior Court, Strafford County, Houran, J., entered summary judgment for town, and church appealed.

The Supreme Court of New Hampshire held that spaces in church's parking lot leased to state university students were not exempt from property tax.

Spaces in church's parking lot leased to state university students were not "used and occupied directly for religious purposes," within meaning of statutory exemption from property tax for "houses of public worship, buildings, and the lands appertaining to them owned, used and occupied directly for religious training or for other religious purposes by any regularly recognized and constituted denomination"; university students were using parking spaces for their own private and secular purposes, i.e., parking for about six hours each week, plus special event days and during snow plowing and repair operations, and church did not argue that leasing spaces to university students was reasonably necessary to carry out its mission.

Mayors Fight to Keep Municipal Bonds Tax Free.

Mayors present and past swear by the value of municipal bonds, while also swearing by the tax deduction for investing in them.

Hence their ongoing battle to preserve that tax benefit as Congress considers changes that could cut the deduction or trim it back in some way as part of an overall tax overhaul, despite some whispered assurance that the century-old exemption won't get touched.

Advocates don't want to take anything for granted.

Still, it doesn't hurt that they have easy allies on the House Ways and Means Committee, where legislative changes to the U.S. tax code begin. Multiple GOP members are former mayors who are fighting opposition to the tax break.

"As we go through the tax reform debate, I will be a voice in that camp," said Rep. Tom Reed (R-N.Y.), who ran City Hall in Corning, N.Y., in 2008 and 2009.

Municipal bonding is critical to building infrastructure such as roads, he told Bloomberg BNA, adding that no financing alternatives exist. That echoes a point raised by members of the U.S. Conference of Mayors in an effort to keep the tax benefit.

The group recently launched a formal campaign to ensure the status quo.

Local and state governments financed nearly $1.7 trillion in infrastructure projects through tax-exempt municipal bonds from 2003 to 2012, but would have paid nearly $500 billion more if investors couldn't use the deduction over that decade, according to data from the mayors' group.

That kind of impact would have caused higher taxes and job losses, a number of mayors argued at a recent gathering in Washington for their 85th winter meeting.

$195 Billion

The tax benefit for municipal bonds adds up to an estimated $195 billion in lost revenue from the 2016 federal fiscal year through 2020, according to an analysis released Jan. 30 by the Joint Committee on Taxation.

That federal subsidy for state and local outlays represents wasteful spending that accrues to top-income taxpayers, said Chris Edwards, director of tax policy studies at the libertarian Cato Institute. He has recommended repealing the provision because it favors government infrastructure over the private sector.

“It’s a distortion because it discourages state and local governments from making privatization reforms,” Edwards told Bloomberg BNA, repeating a message he has delivered directly to Ways and Means Chairman Kevin Brady (R-Texas) and committee staff.

Private ownership of airports, seaports and highways is much more common in countries like Canada and the U.K., Edwards said, adding that it is more efficient than government-run infrastructure.

But new water and sewer infrastructure would be imperiled without municipal bond financing in South Carolina’s state capital, Columbia, said its mayor, Steve Benjamin.

The project, which he said should service 300,000 people in the region when completed, hasn’t required higher taxes. In fact, the city hasn’t raised taxes in a decade and has ended five of the last six years with a budget surplus, Benjamin said.

“We don’t need rate increases simply based on the unavailability of additional capital,” he told Bloomberg BNA. “That’s the concern here. Certain cities will always be able to access the market. But if in fact we saw the tax exemption go away, or any other jolts to the muni market, there are several cities that wouldn’t be able to access markets.”

Trump Support

President Donald Trump agrees with keeping the tax benefit, according to Benjamin, who in December met with Trump in New York along with New Orleans Mayor Mitch Landrieu and Oklahoma City Mayor Mick Cornett, president of the U.S. Conference of Mayors.

Behind the scenes, some Ways and Means Republicans don’t expect change, according to two sources close to the talks who spoke on condition of anonymity so they could speak freely about the ongoing discussions, but the tax exemption’s defenders don’t feel safe.

“That alarms us because we know that that cuts directly into the amount of infrastructure that we’re able to finance in our nation’s cities,” Cornett said at a news conference during the group’s Washington meeting.

Several mayors had meetings with Ways and Means members and staff, Benjamin said, without providing specifics. He stayed in town through Trump’s inauguration, but didn’t have another meeting with the president.

“I can tell you it’s one of the potential things to look at as far as replacing and simplifying the tax code,” said Rep. James B. Renacci (R-Ohio), another former mayor among Ways and Means’ GOP roster.

Committee members are being petitioned on a host of tax benefits that could be on the chopping block as part of tax reform, for which legislation is being developed based on the loose framework released in June by Brady and House Speaker Paul D. Ryan (R-Wis.).

“Being on the front line of that debate previously, I think mayors—and myself included—tend to understand the need for municipal bonding, and if you don’t have it, how difficult it would be to meet the needs of local communities,” Reed said.

Still Waiting

Renacci has pushed back against the opposition, and like Reed, would prefer to maintain the tax exemption. But the former mayor of Wadsworth, Ohio, admitted that such decisions remain out of his hands for now.

“We don’t know what’s in or what’s out; we haven’t seen the bill in writing,” Renacci told Bloomberg BNA. “It’s the same old answer—we just have to continue to wait and see what the committee staff puts in writing and we’ll have a better answer.”

Other former mayors on Ways and Means include Reps. Kenny Marchant (R-Texas), who said bonding was an essential ingredient to funding municipal projects during his tenure running Carrollton, Texas.

Ways and Means ranking member Richard E. Neal (D-Mass.), the former mayor of Springfield, Mass., said bonds’ guarantees are essential for communities and investors, and that he couldn’t imagine changing tax policy to alter their attractiveness.

“It’s a public good,” Neal told Bloomberg BNA. “I don’t think that’s a difficult one.”

But the tax overhaul blueprint needs revenue to minimize more red ink on the federal ledger, something Brady has pledged to ensure when estimating economic upside that would come from the myriad tax cuts involved in the plan.

Both Reed and Renacci cautioned that changes to tax-exempt municipal bonds remain a possibility. But Reed said he won’t hold back his opinions.

“To me, it’s a tool that’s worked for years and years and years,” he said. “And as we go through tax reform I’m about fixing the broken parts of the tax code, but for the provisions that work, we’re a voice to say let’s continue that.”

Bloomberg BNA

By Aaron E. Lorenzo

February 6, 2016

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2017 – What lies ahead?

The year 2017 promises, and threatens, to be a potentially momentous one for public finance in the United States. The Trump Administration and the 115th Congress may put in place tax reforms and infrastructure programs that will have transformative consequences for the financing of public projects in all sectors and at all levels. These are only a few of the issues that state and local officials and public finance professionals will be following closely in the coming year:

- Will income tax rates be reduced and, if so, will lower rates reduce the relative attractiveness of tax-exempt municipal bonds?
- Will new restrictions be placed on the purposes for which tax-exempt bonds may be issued or on the manner in which they may be sold, or how their proceeds may be invested?
- Will the new Administration pursue the trillion-dollar, ten-year infrastructure program that President Trump proposed during the campaign? Will Congress approve it? If so, which categories of infrastructure improvements will be given priority?
- How will any major infrastructure program be paid for? As a candidate, President Trump indicated that he would propose new tax credits as a funding method. If enacted, would those tax credits enhance or undermine traditional municipal bond financing?
- Will the Alternative Minimum Tax be eliminated and, if so, will that increase the relative attractiveness of "AMT Bonds" (e.g., exempt facility bonds) commonly issued to finance certain types of large infrastructure projects?

Continue reading.

Squire Patton Boggs

The Public Finance Tax Blog

By Joel Swearingen, Johnny Hutchinson and Bob Eidnier on February 3, 2017

IRS Opens Probe Into Financing for Statler Redevelopment.

The Internal Revenue Service is investigating a deal that raised millions of dollars for the redevelopment of the Statler Hotel and Dallas Central Library, according to lawyers involved in the financing.

The *Dallas Morning News* recently signed a lease agreement to move into the old library building once it has been renovated. The library and 19-story hotel are on Commerce Street across from the Main Street Garden Park.

The IRS is examining a complex financing that raised $26.5 million for the $221 million project. Mehrdad Moayedi, a real estate developer known for building residential communities in North Texas, is spearheading the project though Commerce Statler Development LLC.

The financing to help pay for the redevelopment involved tax-exempt bonds, which are regulated by the IRS.

The bonds were sold by an agency in Wisconsin and were backed by future tax grants to the project from the city of Dallas. Local experts called that structure unusual when it was announced in August.

Lawyers involved in the tax-exempt bond sale published a notice Monday telling investors that the IRS is examining the deal because of concerns "that the debt issuance may fail one or more provisions" of the tax code. The notice said the concerns may have been raised by "external sources."

The agency did not respond to requests for comment Monday night.

The Public Finance Authority in Wisconsin "believes the bonds complied with all applicable provisions of the Internal Revenue Code," according to the law firm that posted the disclosure, Orrick, Herring & Sutcliffe. The firm declined to comment to *The News*.

The city of Dallas approved the bond sale based on the future payout of the tax incentives.

Moayedi's spokeswoman referred questions about the IRS inquiry to Kirk Wilson, a financial consultant for the project. Noting that the developer has not received any information directly from the agency, he said that the IRS is simply asking for more information in a routine audit.

The bonds are backed by so-called tax-increment financing, in which the city promises to give developers tax breaks over time for developing in designated areas. City representatives did not immediately respond to requests for comment.

The Dallas Morning News

by Terri Langford

Miles Moffeit contributed to this story

CDFA Agenda Includes Pushing for Bond Bills, Supporting Tax Exemption.

WASHINGTON – The Council of Development Finance Agencies this year will work to obtain separate bills that would ease certain tax restrictions for manufacturing bonds and remove water and sewer bonds from the private activity bond volume cap.

The goals are in the 2017 policy agenda the group is circulating to its members.

The CDFA also will work to preserve and strengthen tax-exempt bonds in general, obtain increased funding for the Water Infrastructure Finance and Innovation Act (WIFIA) and promote the launching of a federal urban tax increment finance program, among other things.

"The bond issues outlined in our agenda are our primary focus in 2017, said Toby Rittner, CDFA's president and chief executive officer. "Working with our partners in Congress to get MAMBA passed would be a great victory for issuers, and for our industry as a whole. Our efforts to protect the tax-exempt status of municipal and private activity bonds are also important. With tax reform likely coming this year, it's essential that we make sure members of Congress are fully aware of the importance of the tax exemption, and that they protect it at all costs."

MAMBA is the acronym for "Modernizing American Manufacturing Bonds Act," companion bills introduced by House and Senate members last year and the year before that would have loosened tax law restrictions for qualified small issue manufacturing bonds. These bonds are used to finance facilities for small and mid-sized manufacturers. They are also called industrial development bonds (IDBs). The bill (S. 3416) in the Senate was offered on Sept. 28 of last year by Sens. Sherrod Brown, D-Ohio, and David Perdue, R-Ga., The one (H.R. 2890) in the House was introduced on June 25, 2015 by Reps. Randy Hultgren, R-Ill., Richard Neal, D-Mass., and James Renacci, R-Ohio. Neal is now the top Democrat on the House Ways and Means Committee. The two congressmen had offered the bill the previous year as well.

The House and Senate bills would have made two tax law changes that had been put into effect in 2009 and 2010 under the American Recovery and Reinvestment Act. They would have expanded the definition of manufacturing facility to include intangible property, such as software, as well as tangible facility. The bills also would have allowed IDBs to be used to finance facilities that are functionally related and subordinate to the production of tangible or intangible property, such as warehouses that temporarily store materials and laboratories that test raw materials.

Additionally, the measures would have made two other tax law changes. They would have increased the maximum size of an IDB issue to $30 million from $10 million. The limit hasn't increased since 1979 and hasn't ever been indexed to inflation.

They also would have increased the capital expenditure limitation for IDBs. Currently, a manufacturer can only issue IDBs if their capital expenditures, including the bond proceeds, are not more than $20 million in the six-year period beginning three years before the date of the proposed new issue and ending three years after that date. Under the bills, that capital expenditure limitation would have increased to $40 million.

On tax-exempt financing in general, CDFA's agenda said, "The administration must commit to preserving and protecting tax-exempt bonds under any and all circumstances. The restriction, capping, and/or eliminating of the tax-exempt status for municipal and private activity bonds should be dismissed outright."

In addition, the group said, any tax reform measures considered by Congress should take into account the importance of private-sector led investment and "the critical role that tax-exempt bonds play in generating private investment."

CDFA also wants to push for the reintroduction of legislation that would remove PAB volume caps for water and sewer bonds. A bill (S. 2606) was introduced in the Senate on Feb. 29 last year by Sens. Robert Menendez, D-N.J. and Mike Crapo, R-Idaho. The one (H.R. 499) in the House was introduced by Reps. John Duncan, Jr., R-Tenn., and Bill Pascrell, DN.J., the year before in January.

In addition, the group wants increased funding for WIFIA, which provides credit assistance in the form of loans for large water infrastructure projects.

The group's agenda also calls for the launch of a Federal Urban Tax Increment Finance Program that would allow local governments to redirect specific estimated tax revenue to finance urban revitalization efforts. Currently state and local governments set up TIF districts and use the revenue to back tax exempt bonds.

CDFA called for the creation of a State Clean Energy Finance Initiative (SCEFI) pilot program with the Treasury Department that would be authorized for five years with a onetime $5 billion appropriation. The program would leverage an additional $50 billion of private investment nationally for clean energy projects.

The two-plus-page agenda calls for other initiatives as well.

The Bond Buyer

By Lynn Hume

February 2, 2017

Making the Case for the High Efficiency of the Tax Exemption - It's in the Numbers.

As tax reform takes shape, a key challenge for the municipal market in maintaining full access to the tax exemption stems from a factually flawed methodology utilized by the Joint Committee on Taxation.

Over a long period of time, we have been told, “don’t try arguing with Joint Tax methodology, their methodology is accepted by Congress, the Administration and staff as being gospel.” However, what if the problems with the Joint Tax analysis stem not primarily from methodology, but from factual inaccuracies in the data underpinning the analysis?

Under its analysis, the JCT comes to three conclusions:

1. That municipal yields as a percentage of taxable yields are high;
2. That this high ratio results in the marginal tax rate of the marginal investor in municipals being low; and,
3. That, as a consequence, everyone in a higher tax bracket received a “windfall”—a higher yield than would be needed to needed to attract them to buy municipals.

Under their methodology, long-term municipal yields as a percentage of corporate yields are indeed quite high – roughly 94% on long-term A1/A+-rated paper. However, the high ratio vanishes when two simple but essential adjustments are made to the calculation: The first adjustment is to compare municipals to corporate bonds that are actually similar, which the Joint Tax report demonstrably did not. We stress that this adjustment does not reflect a change in methodology relative to the JCT. It simply makes sure that the analysis involves an “apples vs. apples” comparison.

The second adjustment is to increase municipal yields to the levels that would be needed to clear the market if these municipals came as taxable bonds. That is a higher yield than that which would show on corporate indices, because as currently constructed, municipals have certain disadvantages that would force them to pay a higher yield than corporate bond indices suggest, if they came in the taxable market. These disadvantages include weaker call provisions, lower liquidity on smaller maturities, and a weaker disclosure regime than on corporate bonds. Having shown how these two adjustments would look, we then discuss two other factors, which provide important pieces of evidence that the conclusions of Joint Tax are incorrect—the functioning of the market for “Private Activity Bonds” subject to the Alternative Minimum Tax, and the pattern during the second half of 2009 and 2010, when taxable “Build America Bonds” were available as an alternative to tax-exempts.

The bottom line is that in our view, the 2012 report out of Joint Tax on their methodology for determining the efficiency of the tax-exemption was severely factually flawed:

- Triple-A corporates were compared to A1/A+ municipals using the Bond Buyer 20-Bond Index (BBI);

- The fact that the BBI severely overstates actual borrowing costs in the municipal bond market was ignored;
- The fact that municipals with shorter maturities compare much more favorably than longer bonds in comparison with taxable bonds was ignored; and,
- The more favorable structure of corporate bonds with respect to call provisions, liquidity and disclosure, which reduces their borrowing cost relative to the likely cost of fully taxable municipals was ignored.

All of the above factors create an illusion the JCT analysis that muni yields as a percentage of corporate bond yields are much higher than they are in the real world.

Finally, the underlying assumption that, if tax-exempts did not exist, investors would only buy fully-taxed corporates as an alternative, is simply incorrect, as Joseph Poterba at MIT has shown. At the maximum 40% tax rate on corporate bond interest, a vast number of investors would, if they could not buy tax exempts, seek out an alternative with a lower Federal tax rate, such as the 20% maximum rate on dividends and capital gains.

Working Through the Numbers

In our analysis, we start with the yield ratio we would expect JCT to derive using its flawed data. Using this starting point, we would have a tripleA corporate bond index of roughly 3.50%, and a yield on the Bond Buyer 20-bond Index of roughly 3.87%. This provides a starting point ratio of roughly 107%.

Adjusting for the factual inaccuracies in the data as shown by JCT in its own analysis works out as follows:

1. Currently, municipal yields are inflated to a degree by tax risk fears. In our estimation, long-term municipal yields would be at least 30 basis points lower under “normal” conditions. Since the election, investors have become reticent to put cash to work in the municipal market as a result of fears that tax reform would damage the value of municipals by sharply cutting tax rates or putting a cap on the value of the tax-exemption. Pressures on the municipal market are shown in municipal bond fund flows, which have been a whopping negative $15 billion since the election. Adjusting for tax risk fears, and the ratio declines to 3.57% vs. 3.50%, or 102%.
2. Different quality bonds are being compared. A Triple-A rated Corporate Bond index is compared to the A1/A+ Bond Buyer Index. Use of comparably rated bonds would reduce the ratio on municipal yields to corporate yields considerably. (3.57% /3.60% would become 3.57%/4.10%). The yield ratio would thus move down from 102% to 87% – still very high, but wait…
3. The greatly inflated yield on the BBI. The Bond Buyer Index utilized by the JCT in their analysis ALWAYS yields considerably more than actual municipal bonds, as it did over the entire time period included in the JCT report. During their measurement period, the difference typically ran 80120 basis points. Now, with lower yields in all sectors, the difference still runs 50 basis points for similarly rated bonds due in 20 years. So, the 3.57% to 4.10% comparison above becomes 3.07% to 4.10% when real-world yield levels are used instead of the massively inflated BBI, and the ratio declines to 75%.
4. Differences in call provisions, liquidity and disclosure between A1/A+ corporates and A1/A+ municipals are ignored. To be sold in the taxable market without corporate-like attributes, we estimate that municipals would have to have roughly 40-basis-point higher yields than like-rated corporates, and 60 basis points more for smaller, less liquid issues. Differences include the lack of call risk on corporate bonds versus the ten-year call on nearly all municipals, stronger liquidity resulting from higher per-maturity issue size, and stronger disclosure requirements. So, the comparable ratios become 3.37% to 4.50%, and 3.37% to 4.70%, or the 74.9% to 73% range.

5. A focus on long maturities. As we discuss below, municipal yields as a percentage of taxable yields tend to be dramatically lower on bonds 11 years and shorter than they are on longer-maturity paper. By our estimate, the ratio in the 10year range would be at least 7 percentage points lower in 10years than it is in the 20-year bonds used in the JCT analysis, and on 5year paper would be another 7 percentage points lower. Using an average of a 10 percentage point drop for paper inside 10 years, and the ratio declines to from 64.9% to 63%.
6. Evidence for a very high clearing marginal tax rate on shorter maturities comes from BABs. During the period from mid-2009 through the end of 2010, nearly 40% of new issues came as Build America Bonds – fully taxable to the investor, but with a 35% subsidy provided to the issuer. Issuers thus had a choice: accept the reduced yield provided by access to the tax exemption, or accept a 35% subsidy. The two choices would essentially be break even when munis yielded exactly 65% as much as taxable BABs. In terms of measuring the efficiency of the tax exemption, here is the interesting result: during that period, a very large proportion of bonds with a maturity longer than roughly 11 years came as BABs, but nearly all bonds with a maturity inside 11 years came in the tax-exempt market. As far as the efficiency of the tax exemption is concerned, the implications are clear: inside roughly 11year maturities, municipal bonds were clearing with a ratio to taxable bonds lower than 65%. This compares with the implied tax rate for municipals during 2009 in the Joint Tax analysis of 13.2%. We estimate that the ratio actually stayed above 30% as far out as roughly 15 year maturities, a sizable component of the entire municipal market – roughly 60%-70%.
7. Thus, simply comparing apples to apples—similarly rated and structured municipals and corporates under current conditions takes the clearing marginal tax rate up from 8% to 34%-38.5%. However, even this purely factual analysis based upon current market conditions ignores an important invalid assumption in the Joint Tax Analysis: That investors who could no longer buy tax exempts would only buy taxable bonds taxed at their maximum income tax rate as an alternative. The problems with the assumption that taxable bonds are the only alternative in the absence of tax-exempts, is shown in the work of Joseph Poterba and teammates at MIT. (Example: *Portfolio Substitution and the Revenue Cost of the Federal Income Tax Exemption for State and Local Government Bonds*, Poterba, James M. and Verdugo, Arturo Ramírez, National Tax Journal, June 2011.)

It's Not Just Municipals vs Taxable Bonds

Having adjusted the yield comparison to provide an apples-versus-apples comparison, we arrive at an adjusted yield ratio of municipal yields to corporate yields, at various spots along the yield curve. While this adjustment suggests a marginal tax rate for the marginal buyer that is vastly higher than the JCT suggests, we then explain why the assumption that this ratio represents a complete comparison of the two markets is highly flawed. This assumption has been deconstructed by Poterba at MIT, among others.

In reality, in the absence of a tax-exemption, most investors would not buy taxable bonds taxed at their maximum marginal rate; they would hold more cash/nearcash (they currently hold 6X as much cash as the do municipals), or they would buy investments with a lower effective tax rate. Currently, dividends and capital gains are taxed at a maximum rate of 20%. With longterm corporate yields around 4.25%, investors in roughly the 40% tax bracket would earn roughly 2.50%, after-tax. As Drs. Poterba and Verdugo note, lacking access to tax-exempts, many of these investors would choose dividend paying stocks, or invest for a longterm capital gain, rather than buying fully taxable bonds. The idea that the difference between the ratio of municipal yields to corporate yields and investors' maximum tax brackets represents a "windfall" to the high bracket investor is simply incorrect, because investors have other choices.

Impact of a Cap on the Tax Exemption—Evidence From the Market for Bonds Subject to the AMT

Our message in the above is that, when comparisons between munis and corporates are measured properly, municipal yields as a percentage of taxable yields are vastly lower than that shown in the Joint Tax analysis. Quite simply, the low marginal efficiency of the tax-exempt market described by Joint Tax in its analysis results from inaccurate data. We do not attack the methodology, we simply show that the clearing marginal tax rate for municipals, properly measured, is quite high under most market conditions.

In addition, the question has come up as to what the impact would be of a 28% cap on the tax-exemption.

In our view there is already evidence of the impact from the functioning of the market for PABs subject to the AMT.

These bonds are subject to a "surtax" on the interest, but only for investors who pay the AMT. For other investors, the AMT has no effect. Even with this limited target for the surtax, bonds subject to the AMT cost issuers roughly 30 basis points more than nonAMT paper. To investors who do not pay the AMT, the extra yield is a "windfall" that provides no tax revenue to the Treasury. Now consider what would occur if all municipals were subject to a surtax in the form of a 28% cap: we would expect the cost of borrowing in the municipal market to rise substantially more than 30 basis points. In our estimate, the impact would range from 50 basis points to 75 basis points or more for the entire market. Please note that when municipals and corporates are compared properly, the clearing ratio of yields generally put the marginal tax rate above 28%. As a consequence, in our view, a 28% cap would be quite damaging the in the form of higher borrowing costs.

The Bottom Line

Decision makers often cite the Joint Tax methodology in explaining why they believe the tax exemption to be an inefficient subsidy. To a very significant degree, we believe that the JCT analysis is flawed, not because its methodology is incorrect, but because its data is wrong: its comparison is a clear "apples to oranges" comparison. When the data is adjusted to compare similar bonds in both sectors, we discover that muni yields as a percentage of corporate bonds actually provide a marginal tax rate that is impressively high. In addition, we site one comparison from the work of Joseph Poterba et al at MIT: we believe, as he does, that if the tax-exemption were eliminated, many investors would substitute other investments with a tax rate roughly half of that on full taxable bond interest. Given all of this, the premise that the muni market clears through investors with a low marginal tax rate—thereby giving a windfall to high bracket investors – is simply incorrect.

The Bond Buyer

By George Friedlander

February 1, 2017

George Friedlander is a managing partner at Court Street Group Research.

Despite Budget Shortfalls, Some Governors Call for Tax Cuts.

About half of the states are facing budget shortfalls this fiscal year, but many governors are still pushing to cut taxes in their proposed 2018 budgets.

The proposals vary in scope but generally fall within two categories: comprehensive and targeted.

Nebraska Gov. Pete Ricketts' proposal is of the comprehensive variety and may be the most aggressive call for tax cuts so far. He is asking for property and personal income tax cuts to be phased in beginning in 2019 — even as the state faces a $900 million budget gap. Property taxes would be reduced via a new valuation formula and income tax breaks would kick in incrementally and only in years when state revenue grows by more than 3.5 percent.

On the whole, most of the comprehensive proposals are part of ongoing efforts.

"Many of these ideas are either follow-ons to things they've already done," said John Hicks, the National Association of Budget Officer's executive director. "Or they are things they hoped to do and haven't been able to yet."

For instance, Maine Gov. Paul LePage is again proposing to expand the state's sales tax on services as a way to pay for income tax cuts. In the latest version, LePage has extended his sales tax proposal to include streaming services like Netflix and rental platforms like Airbnb.

South Carolina Gov. Nikki Haley, who, if approved, will be vacating her office to take over as the United Nations ambassador for the Trump administration, is pushing for a pared-down version of a previous income and corporate tax cut proposal.

In Alaska, which faces a $3 billion budget shortfall, Gov. Bill Walker has toned down his previous efforts to overhaul the state's finances. He still wants to reduce citizens' annual bonus checks from the Alaska Permanent Fund and divert some of the fund's investment earnings into the state budget each year. But he has backed off previous proposals for a new state income tax, instead leaving a $900 million budget gap in his proposal for the legislature to fill.

Meanwhile, some governors are taking a more targeted approach.

Indiana Gov. Eric Holcomb wants to exempt veterans' pensions from the income tax; Arkansas Gov. Asa Hutchinson would cut taxes for low-income workers; and New York Gov. Andrew Cuomo wants to preserve planned tax cuts for the middle class.

Cuomo is renewing his proposal for a millionaire's tax hike, which would help pay for that state's $3.5 billion budget deficit. In Montana, which is also facing a shortfall, Gov. Steve Bullock has proposed a tax hike on his state's wealthiest residents. And Washington Gov. Jay Inslee is proposing a new tax on capital gains to help pay for the state's court-mandated education funding increases.

Outside of raising income taxes, some states are looking to excise or sin taxes to fill needs or budget deficits.

Governors in California, Indiana and Tennessee have floated raising the gas tax to fund transportation projects. In recent years, roughly 20 other states have approved gas tax hikes to raise sorely needed money for infrastructure and overdue maintenance. Governors in Colorado and Nevada have pitched raising marijuana taxes, while Kansas Gov. Sam Brownback is proposing an alcohol and cigarette tax hike.

In both Colorado and Kansas, the tax increases would help cover projected budget deficits. That can be a dangerous habit, said Meg Wiehe of the progressive-leaning Institute on Taxation and Economic

Policy, because such tax increases tend to discourage consumption.

"Politically speaking they're low-hanging fruit," she said. "The problem in relying on this is it is a very unsustainable increase. When you increase taxes on cigarettes, smoking declines. If the motivation is for public health, then that's a different story. But if you're looking to address a short, medium or long-term budget hole … it's a bad proposition."

GOVERNING.COM

BY LIZ FARMER | JANUARY 25, 2017

TAX - ILLINOIS

[Oswald v. Hamer]

Appellate Court of Illinois, First District, Fourth Division - December 22, 2016 - N.E.3d - 2016 IL App (1st) 152691 - 2016 WL 7436113

Real property taxpayer brought action against Department of Revenue and the Director of Revenue, seeking declaration that statute governing property tax exemptions related to access to hospital and health care services was facially unconstitutional for granting a property tax exemption to a hospital applicant without regard to whether property was used exclusively for charitable purposes.

The Circuit Court granted summary judgment for defendants. Taxpayer appealed.

The Appellate Court held that statute was facially constitutional.

Statute governing property tax exemptions related to access to hospital and health care services was facially constitutional under state constitution's provision permitting exemption from taxation for properties used exclusively for charitable purposes. Statute's use of term "shall" was directory, rather than mandatory, and, thus, did not require an exemption without regard to whether property at issue was used exclusively for charitable purposes, General Assembly did not intend for satisfaction of statute to ipso facto warrant an exemption, but intended for requirements of the statute to considered on a case-by-case basis, and absence of exclusivity language in statute did not mean the statute was to be read separately from constitutional requirements.

TAX - NEW YORK

[Congregation Ateres Yisroel v. Town of Ramapo]

Supreme Court, Appellate Division, Second Department, New York - January 18, 2017 - N.Y.S.3d - 2017 WL 189197 - 2017 N.Y. Slip Op. 00287

Landowner, a religious not-for-profit corporation, brought action against town, town assessor, and Board of Assessment review, seeking declaration that owner's real property was exempt from real property taxes.

The Supreme Court, Rockland County, granted defendants' motion for summary judgment.

The Supreme Court, Appellate Division, held that landowner's use of real property violated town zoning law, and thus landowner was prohibited from receiving real property tax exemption.

Use of real property owned by landowner, a religious not-for-profit corporation, violated town zoning law, and thus landowner was prohibited from receiving a real property tax exemption. Landowner had illegally erected two trailers on property without obtaining proper permits, and had used primary structure on property as a dormitory and living quarters for over 20 students in contravention of its certificate of occupancy.

TAX - ILLINOIS

Hertz Corporation v. City of Chicago

Supreme Court of Illinois - January 20, 2017 - N.E.3d - 2017 IL 119945 - 2017 WL 243395

Car rental companies brought declaratory judgment actions against city, asserting that ruling by city's department of revenue as to tax on use of vehicles leased by city residents was unconstitutional.

The Circuit Court declared ruling facially unconstitutional and entered permanent injunction. City appealed. The Appellate Court reversed. Companies sought to appeal, which was allowed.

The Supreme Court of Illinois held that city department of revenue ruling regarding applicability of personal property tax to cars rented from agencies outside of city violated home rule article of state constitution.

Ruling had an extraterritorial effect, and therefore city department of revenue ruling determining that suburban car rental agencies located within three miles of city were responsible for paying tax on use of personal property within city borders unless lessee was exempt from paying tax based upon use of leased vehicle outside of city violated home rule article of state constitution. No part of the transactions took place within city's borders, and 100 percent of the cost of a car's rental was taxed even though ruling required that the car be driven in city for only 50 percent of the time to be subject to the tax.

Revenue Procedure 2017-13: Management Contracts – Still Trying To Get It Right.

For the third time in less than three years, the IRS has issued major guidance – Revenue Procedure 2017-13 — on the safe harbor rules for management or service contracts to avoid private business use. The new revenue procedure follows closely behind the total rewrite of the safe harbor rules that the IRS issued as Rev. Proc. 2016-44 in August 2016, which was the subject of several of our posts (here, here, and here). A cynic might think the IRS was just looking for an excuse to renumber the management contract revenue procedure as 97-13 plus 20 years. But in fact there are some important modifications in the new revenue procedure.

Continue reading.

By Bob Eidnier on January 25, 2017

Squire Patton Boggs

IRS: Unspent Proceeds, Refunding Will Not Cause Loss of BABs' Subsidy.

WASHINGTON – Unspent proceeds at the time of a current refunding will not cause Build America Bonds to lose their qualified status for Treasury subsidy payments, the Internal Revenue Service recently found in a recent private letter ruling.

The private letter ruling (PLR) was written in response to a BAB issuer that sought a ruling on whether a proposed current refunding would cause the bonds to fail to meet a requirement that 100% of the proceeds, beyond those put into a reasonably required reserve, be used for capital expenditures.

In a current refunding, the issuer refunds previously issued bonds within 90 days from the issuance of the refunding bonds. The IRS concluded in the ruling that, based on the issuer's representations, "the existence of the unspent proceeds on the redemption date of the bonds will not retroactively cause the bonds to lose their status as 'qualified bonds.'"

Because of this, the IRS said, the issuer would not lose any credit under Section 6431 of the Internal Revenue Code for the bonds for the period prior to the date of redemption. IRS officials said the ruling is contingent on the issuer not spending any of the unspent proceeds for anything other than capital expenditures.

The four-page PLR, signed by IRS senior counsel Timothy Jones, states that the bonds in question were used to finance certain capital projects for an unidentified city. The bonds were to be treated as direct-pay BABs, and the issuer agreed to spend 100% of project proceeds of the bonds for capital expenditures. By an unspecified date, a percentage of the available project proceeds of the bonds remained unspent.

The names of all parties involved in the issuance were withheld in the PLR, which was released on Jan. 13. Both the issuer and city intended to refinance the BABs by issuing tax-exempt bonds.

The IRS also stated in the PLR that it was not expressing any opinion about whether the BABs could be considered reissued upon the deposit of the refunding bond proceeds into an escrow fund to pay principal and interest on the bonds at redemption.

Linda Schakel, a partner with Ballard Spahr in Washington, said she agrees with the ruling, especially considering that the BAB legislation was different than other tax credit subsidy bonds, which required proceeds be spent within three years of the issue date on permitted costs.

"I think this is definitely a very reasonable approach to the question of what happens when you have unspent proceeds at the time you do a refunding, particularly unspent proceeds more than three years after the bonds are issued," she said.

However, Schakel said the ruling does not provide details regarding what might have delayed expenditure or what factors confirm the issuer still expects to expend proceeds.

"I take [this] to mean that the ruling is not conditioned as being extraordinary circumstances justifying the outcome," Schakel said.

Tom Vander Molen, a partner at Dorsey and Whitney in Minneapolis, said he believes that the ruling is correct. He said that although he is not aware of this particular request for a PLR, this issue has come up in different contexts.

“Sometimes in audits, the IRS says maybe it’s a problem if you don’t spend proceeds before you refund,” Vander Molen said. “My position has always been it doesn’t matter as long as you use the proceeds you were going to in the time you were going to.”

“I think this is very consistent with that,” he said. “I think this ruling is exactly right.”

Created under the American Recovery and Reinvestment Act, roughly $181 million of BABs were issued to finance infrastructure during 2009 and 2010 before the program expired for new issuances.

The Bond Buyer

By Evan Fallor

January 19, 2017

IRS Modifies Safe Harbor Guidance and Deadlines for Section 45 and 48 Energy Credits: Grant Thornton

The IRS has issued new guidance (Notice 2017-04) updating and modifying deadlines and rules for the safe harbors for establishing that construction has begun and is continuous on projects qualifying for the renewable electricity production tax credit (PTC) under Section 45 and the energy investment tax credit (ITC) under Section 48.

The guidance extends the date by which a project can be placed in service and qualify for the continuity safe harbor, adds an effective date to a restriction on combining begin-construction safe harbor methods, and clarifies which expenses from a retrofitted facility are included in the 5% safe harbor calculation.

The Protecting Americans from Tax Hikes (PATH) Act of 2015 extended both the PTC and ITC credits. Under the bill, construction on qualified PTC projects must now have begun before the end of 2016 to be eligible for the full credit. The PTC will also be available at reduced rates for wind facilities if construction begins in 2017 (80% of normal credit), 2018 (60%) or 2019 (40%). Taxpayers may also elect to take the ITC in lieu of the PTC, but any PTC rate reductions will apply to the ITC.

In addition, the 30% ITC for commercial solar projects was extended. The rate was set to fall to 10% if construction began after 2016, but the full 30% rate will now be available if construction begins by the end of 2019. A 26% credit is available if construction begins in 2020, and a 22% credit is available if construction begins in 2021 and the facility is placed in service by the end of 2023. The credit is otherwise 10%.

Under guidance issued previously (Notices 2013-29, 2013-60, 2014-46, and 2016-31) the IRS said that taxpayers can establish that construction has begun by either satisfying a test showing “physical work of a significant nature” has begun or by incurring 5% or more of the total cost of the facility under a safe harbor. Taxpayers can aggregate multiple facilities based on the relevant facts and circumstances, but then disaggregate them for applying the placed-in-service deadline for the continuity safe harbor.

However, Notice 2016-31, issued last year, does not allow taxpayers to use two different beginning construction tests in alternate years to establish construction has begun in different years for the purpose of the separate begin-construction and continuity deadlines. Newly issued Notice 2017-04 limits this restriction only to projects that began after June 6, 2016 (the day Notice 2016-31 was issued).

Notice 2016-31 also provided that a retrofitted energy project can qualify if the used property represents less than 20% of the value. Notice 2017-04 clarifies that only costs related to new construction in these projects are included in the calculation for the 5% safe harbor.

Once construction is considered to have begun, taxpayers must make continual progress toward completion. The IRS created a continuity safe harbor to satisfy this standard, last modifying it under Notice 2016-31. Taxpayers are generally considered to have made continual progress toward completion if a facility is placed in service within four calendar years of the calendar year in which construction began. Notice 2017-04 now provides that a taxpayer will also fall under this safe harbor if the project is completed before Dec. 31, 2018, even if this more than four years after construction began.

Taxpayers who don't use the continuity safe harbor must generally use a facts-and-circumstances analysis to determine if construction is continual. Notice 2017-04 does not update the nonexclusive list of allowable disruptions. The following disruptions remain excusable:

- Severe weather conditions
- Natural disasters
- Certain licensing and permitting delays
- Delays at the written request of government for safety, security or similar concerns
- Transmission interconnection issues
- Labor stoppages
- Supply shortages
- Delays in manufacturing custom components
- Inability to obtain specialized equipment
- Financing delays
- The presence of endangered species

Notice 2017-04 also does not update the list of preliminary activities under Notices 2013-29 and 2016-31 that don't qualify as physical work of a significant nature. The following preliminary activities do not qualify:

- Planning or designing
- Securing financing
- Exploring
- Researching
- Conducting geologic mapping and modeling
- Obtaining permits and licenses
- Conducting geophysical, gravity, magnetic, seismic and resistivity surveys
- Conducing environmental and engineering studies
- Performing activities to develop a geothermal deposit prior to discovery
- Clearing a site
- Test drilling of a geothermal deposit
- Test drilling to determine soil condition
- Excavation to change the contour of the land (as distinguished from excavation for footings and foundations)
- Removing existing turbines, towers, panels or other components

Last Updated: January 24 2017

Article by Dustin Stamper

Grant Thornton LLP

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.

IRS Clarifies New Management Contract Safe Harbors.

In August, 2016, the IRS issued Revenue Procedure 2016-44, the first comprehensive revision of its management contract safe harbors since Revenue Procedure 97-13. Rev. Proc. 2016-44 built upon and amplified principles laid out in private letter rulings issued over many years and in Notice 2014-67. Now, less than six months later, the IRS has published Revenue Procedure 2017-13, which clarifies and supersedes Rev. Proc. 2016-44 but does not materially change the safe harbors described therein. The clarifications are in response to questions received with respect to certain types of compensation protected under earlier safe harbors, incentive compensation, timing of payments, treatment of land when determining useful life, and approval of rates.

Tuesday, January 24, 2017

Should Tax Collectors Be Loan Collectors?

Investors love a federal green-energy program for property owners. But if there's a backlash, localities could be caught in the middle.

As proof that no good deed goes unpunished, a well-intentioned federal green-energy program has put local governments into a new alliance with finance companies, sparking a small frenzy on the bond market and turning county tax collectors into de facto home-loan servicers in 34 states and the District of Columbia.

Property Assessed Clean Energy (PACE) is an Obama-era Department of Energy program designed to help residential and commercial property owners finance renewable-energy systems and energy-efficiency improvements. PACE, according to The Wall Street Journal, has become the nation's fastest-growing loan category. Along the way, the property-tax assessment and payment system has morphed into a home equity loan repayment process, posing new perils for property owners and localities alike.

PACE works like this: Contractors offer special home-equity loans to homeowners to go green. Once the green upgrades are completed and the loan documents are signed, the loans are packaged with thousands of similar loans and sold to investors in the form of bonds. Any observer of the last great boom-and-bust cycle — along with any fan of the 2015 film "The Big Short" — will recognize the process.

But here's the rub: PACE loans aren't repaid like a car loan or a mortgage. Instead, localities serve as the middlemen by collecting payments once or twice a year as an assessment in the property owner's tax bill. Localities earn a fee and then forward the proceeds to finance companies.

The premise is a good one, at least in theory. It incentivizes property owners to make environmental upgrades, requiring no cash up front. The *Harvard Business Review* named the concept as one of 10 "Breakthrough Ideas for 2010," and *Scientific American* profiled the concept's creator.

Institutional investors are devouring the bonds because of their high credit ratings and green status. The first PACE program bond, structured by Deutsche Bank and issued in 2014, was awarded an AA credit rating by the Kroll Bond Rating Agency. The interest rate — the "coupon" in bond-speak — was 4.75 percent.

Recently the largest ever PACE bond was issued. It contained 13,432 assessments on homes in 31 California counties. The assessments had an average balance of about $24,400, an average interest rate of 7.96 percent and an average term of 14.95 years. This suggests an additional annual tax-bill payment averaging about $3,200 per property owner.

Critics in the banking industry argue that the PACE model gives these assessments priority lien status over mortgages. To placate lenders in California, which has been a laboratory for the concept and where PACE loans are known as HERO loans, a $10 million mortgage-loss reserve was established in 2014. Still, the banks don't like it.

Other critics contend that the program has been developed as fodder for the bond market and that environmental aims are secondary. PACE financing has been used to purchase everything from furnaces to pool covers to artificial turf. The National Consumer Law Center has reported abuses with the program, including some in which elderly homeowners were victimized.

From a public-policy standpoint, proponents see little difference between PACE and a locality paving a street and then assessing homeowners for the cost. PACENation, an industry group, argues that the increased investment has created stable work for local contractors — often family-owned businesses that have served their communities' needs for heating, air-conditioning, plumbing, roofing and landscaping for decades.

In the middle of all of this are participating localities, which sometimes deal with reports of abuse by contractors selling the loans with scant oversight, and homeowners, some of whom are shocked when their tax bills double or triple.

Even worse, localities fear that, if the home market goes bust again, they may be forced into wide-scale foreclosure proceedings, possibly leaving taxpayers on the hook to cover resulting loan-repayment shortfalls. And if and when a backlash comes from taxpayers or investors, it's likely to be local governments, the middlemen in all of this, that will have to deal with it.

GOVERNING.COM

BY JEREMY BAGOTT | JANUARY 25, 2017

Coming Soon to 6 States: Online Sales Taxes From Amazon.

Online retail giant Amazon will begin collecting sales tax in Missouri next month, as it does in dozens of other states.

The collection of state sales tax in Missouri will begin Feb. 1, Amazon spokeswoman Jill Kerr said in an email to the Post-Dispatch. The state sales tax rate in Missouri is 4.225 percent.

Items sold by Seattle-based Amazon.com and its subsidiaries already are subject to sales tax for merchandise shipped to more than 30 states. Amazon will also begin collecting sales tax on Feb. 1 in Mississippi, Rhode Island, South Dakota and Vermont, and in Wyoming in March.

Amazon does not yet have facilities in the state of Missouri, and online retailers aren't required to collect sales tax where they don't have a physical presence. Amazon charges sales tax in Illinois, where it has multiple distribution facilities, including in Edwardsville.

Amazon announced this month that it planned to hire 100,000 fulfillment employees nationwide over the next 18 months, leading to speculation that the company will open distribution facilities in Missouri. Amazon declined to comment on its distribution facility expansion plans.

"I gather they will be expanding in Missouri because there is a lot of warehouse space here," said David Overfelt, president of the Missouri Retailers Association, a Jefferson City-based trade group that supports requiring online retailers to charge sales tax.

"This is going to be good for Missouri and good for our communities because we provide a lot of services and finding resources is getting tougher and tougher," Overfelt said of Amazon's collection of sales tax. "This is a long time coming. We can't continue down the way we are without hurting Main Street businesses."

Several states and retail groups have pushed for years for Amazon to begin charging sales tax, arguing brick-and-mortar retailers that must charge sales tax are unfairly disadvantaged.

In 2013, a new tax law in Missouri required online retailers to collect sales tax if the company received business referrals from an affiliate in Missouri. After the law was passed, Amazon ended its Associates Program in Missouri that paid advertising fees to web entrepreneurs for customers referred to Amazon.com

Stephen Weiss, owner and president of Creve Coeur Camera, said he welcomed Amazon's announcement that it would begin charging sales tax. Shoppers often come to his eight stores to look at equipment but buy on Amazon because no sales tax is collected, making the purchase $50 or even more than $100 cheaper than buying at his stores, a practice retailers call "showrooming."

"It makes a huge difference," Weiss said about competing against Amazon's prices that don't include sales tax, which he said is an unfair disadvantage. "It kills us."

Creve Coeur Camera, a St. Louis County-based chain, is closing its Edwardsville store at the end of this month and is considering shuttering another store in part due to lost sales that Weiss blames on Amazon. Up until four months ago, Creve Coeur Camera sold some lenses through Amazon, but Amazon recently went directly to the manufacturer to supply the lenses, Weiss said.

Adding sales tax to goods sold in Missouri will help level the playing field for retailers, he said. "I think it'll help, no question."

A Missouri Department of Revenue spokeswoman did not immediately respond to requests for comment about the amount of new tax revenue that will be generated.

Carl Davis, research director for the Washington, D.C.-based think tank Institute on Taxation and Economic Policy, estimated the state of Missouri could collect between $30 million and $34 million annually from Amazon sales, based on an analysis of revenue generated in other states.

“We’re supporters of sales tax being collected on online purchases in the same way they’re collected at brick-and-mortar stores,” Davis said.

Some Missouri Amazon customers criticized the decision on social media Wednesday, saying it could make merchandise more expensive.

Judith Stallmann, a professor at the University of Missouri who studies state and local public finance and rural and economic development, said the change may prompt cost-conscious shoppers to shift their buying habits.

“This means you’re going to be paying sales tax on things you didn’t before,” Stallmann said. “There may be some people for whom paying sales taxes could weigh on their decision.”

BY TRIBUNE NEWS SERVICE | JANUARY 27, 2017

By Lisa Brown

How San Diego's Taxpayer Won by Letting the Chargers Bolt.

- Moody’s: voters’ rejection of new stadium credit positive
- Largest city-owned site could be redeveloped in better deal

The departure of a professional football team from San Diego means the city may not need to pay out $11.7 million annually from its general fund on the stadium for much longer.

The National Football League’s Chargers are decamping for a new Los Angeles area stadium after voters in November rejected a measure that would have pledged $1.1 billion in public backing for a new arena. Not only did residents dodge a debt burden, they now have a chance to see redevelopment of the city’s largest piece of real estate available. One proposal would bring a soccer franchise without public subsidies.

The ballot proposal, pushed by the Chargers, would have increased hotel taxes to 16.5 percent from 10.5 percent to pay for a new stadium and a convention center expansion. But analysis by consultants highlighted the uncertainty of the $1.8 billion price tag. Since the city would have borne any cost overruns and infrastructure improvements, the rejection of the measure by 56 percent of the voters was a credit positive, Moody’s Investors Service said.

“We’ve had a history of bad deals as a city,” said City Councilman Chris Cate, who opposed the ballot measure. “I firmly believe that taxpayers paying for a stadium has no economic benefit whatsoever to the city or the region.”

San Diego still owes $38 million in municipal bonds on the stadium, data provided by the city show. Debt service next year through 2027 will total about $4.7 million annually, which won’t be covered by the team’s $12.5 million payment to the city for breaking its lease. Still, it would be a “minimal” impact to the city’s general fund, said Kristina Alagar Cordero, a Moody’s analyst.

Investors in the city’s debt don’t appear to be put off by the loss of the football team. A San Diego

5.25 percent coupon 2040 revenue bond, callable in 2020, is trading at a 31 basis point spread to the BVAL AA Muni 5-Year Revenue Curve, compared to 28 basis points just before Election Day and 52 basis points on the day the Chargers made their departure official on Jan. 12.

Thanks to rebate agreements and legal settlements, San Diego actually ended up paying the Chargers to play for the past decade. "If anything, there will likely be a cost savings to the city by not having to provide public safety services" during games, said Craig Gustafson, a spokesman for Mayor Kevin Faulconer, in an e-mail.

The Chargers, who ended the season last in its division and with a home attendance that was second-worst in the league, will join the Rams in a new stadium in Inglewood, outside of Los Angeles, when it opens in 2019. Until then the team, renamed the Los Angeles Chargers, will play in a smaller complex in Carson.

Other leases, such as with San Diego State University, oblige the city to keep the stadium open through 2018. After then, it's up in the air. Since the facility is costing the general fund and also needs $90 million in upgrades, municipal officials are evaluating "the financial feasibility of continuing stadium operations beyond that point," Gustafson said.

The departure could yield a chance for long-term positive impact if the 166-acre site is redeveloped. "It does provide the city an opportunity," Cordero said.

Bloomberg Technology

by Romy Varghese

January 27, 2017, 2:00 AM PST

–With assistance from Eben Novy-Williams.

The Economy's Expanding. So Why Aren't Tax Revenues?

There are a couple of major reasons that the frustration is likely to continue for revenue estimators and policymakers.

It may still not feel like it to everyone, but we are at or near the top of the business cycle. By all definitions, we have been in expansion for nearly eight years, the third-longest period of expansion in modern American history. Gross Domestic Product growth is tracking at more than 2 percent, the unemployment rate is under 5 percent, and wage gains have finally begun to accelerate. But if you work for a state or a local government, you may not have noticed.

The same GDP reports that have shown such progress recently also show that states and local governments have subtracted from the pace of real economic growth in three of the past four quarters, and it doesn't take much detective work to find out why. That same year of strengthening growth coincides with five consecutive quarters of weak state tax-revenue growth, including an outright year-over-year decline in the second quarter of 2016. Combined, state tax revenues were unable to clear the pace of inflation in the past year, their worst performance since the Great Recession.

How can state taxes be in recession when the rest of the economy is in expansion? This has been the biggest puzzle for policymakers this year, and the leading cause of subnational budget weakness throughout the country. The growing disconnect is twofold and attributable to both structural and one-time factors.

The first source of frustration for revenue estimators and policymakers is temporary and has to do with prices. This is particularly relevant to sales taxes, which have been the largest underperformer for most states over the past year and a half. Price levels impact sales taxes because sales taxes are levied as a percentage of overall taxable value. Thus, even though consumers may have more money in their pockets and are buying a greater number of goods, the value of those goods may not be growing in line with expectations. In fact, the taxable value may be declining.

Typically, at this point in the business cycle, low unemployment and rising wages push prices — and therefore tax collections — higher. However, the extraordinary strength of the U.S. dollar and the energy bust are holding prices well below expansionary levels. Headline consumer prices are increasing in line with the business cycle at around 1.7 percent annually, but the components of the Consumer Price Index tell a more nuanced story. Looking solely at goods prices, which make up the lion's share of all taxable sales, we actually still see deflationary pressures weakening sales-tax collections.

Take homebuilding as an example. Housing construction is a major driver of sales taxes because of the large durable-goods purchases that go into building and furnishing a new home. Last year the number of housing starts increased significantly, which should have resulted in stronger sales-tax collections. However, the prices of most goods used in new-home construction declined significantly. Lumber prices, for example, were down by more than 10 percent at one point in 2016. So even though more housing units were being built, the sales-tax collections from each unit were much less than the year before.

With inflation expectations rising, this dynamic will only prove temporary. However, a second and more structural consideration will continue to give revenue estimators fits for some time to come.

Over time, state tax revenues have generally grown more disconnected from the underlying economies upon which they're levied. A study we performed several years ago found that state tax revenues in the first decade of the 2000s had become three times more volatile than the underlying economy. This was orders of magnitude larger than anything states had experienced before, and it led to state tax revenues underperforming nominal GDP for the first time since records have been kept.

This dynamic has progressed in line with two growing influences on state taxation over the past few decades. First, states have become increasingly reliant on highly progressive personal income taxes. This isn't necessarily a bad thing — an efficient tax structure should have at least some progressivity — but a side effect is increased volatility. By making their tax structures more progressive, states are relying on a smaller set of higher-income taxpayers for a larger portion of their revenues. This set of taxpayers typically has some of the most volatile incomes. A taxpayer in the top 1 percent of the income distribution can make $10 million one year and very easily lose $10 million the next. It is no anomaly then that some of the states with the biggest income-tax surprises are also those with some of the most progressive tax codes.

Adding to this disconnect is the growing number of targeted tax incentives being put to use by state and local governments for economic development. This isn't necessarily a bad thing either, as these incentives can be effective at spurring local growth. But these rarely tracked incentives can also create a scenario in which the fastest-growing parts of an economy are growing tax-free. This distorts the relationship between broad-based economic statistics and tax revenues, making life very difficult on revenue estimators.

As a result, revenues become more unpredictable and policymakers have to become more cautious. Unfortunately, it looks like that dynamic is here to stay.

GOVERNING.COM

BY DAN WHITE | JANUARY 19, 2017

Neal: Tax Reform Should Preserve Tax Exemption, Reinstate BABs.

WASHINGTON – Tax reform legislation should preserve the tax exemption for municipal bonds and reinstate Build America Bonds for infrastructure financing, Rep. Richard Neal, the top Democrat on the House Ways and Means Committee, told reporters Thursday.

But tax reform may have to wait until Republicans complete their repeal and replacement of the Affordable Care Act as they have proposed, the Massachusetts Democrat said.

Speaking at a news conference at the National Press Club here, Neal said he is "skeptical" that Congress can simultaneously tackle two projects of the magnitude of tax reform and the ACA.

Republican leaders in Congress as well as President-elect Donald Trump and Vice President-elect Mike Pence have made repealing and replacing Obamacare the top priority at the start of the new administration.

Neal said he met with House Ways and Means Committee Chairman Rep. Kevin Brady, R-Texas, last week, who told him that the GOP blueprint for tax reform released last June would be rolled out as formal legislation this year. Neal said he could not provide a more specific timeframe, but added that Brady made it clear he wants to get through tax reform "vigorously."

He said he hopes the blueprint, which does not mention munis directly but proposes to generally repeal deductions, maintains the tax-exempt standing.

The former Springfield, Mass. mayor and longtime advocate of munis cited his municipal experience, calling himself a "pro-growth believer."

"My DNA is in the mayor's office and I know how we used tax-exempt bond financing," said Neal, who was named ranking minority member of the House Ways and Means Committee in December. "It worked quite well."

Although roads, bridges and other public use projects "beg" for a large infrastructure program, Neal said, infrastructure spending is not as easy to pass as it once was. That could mean reintroducing BABs, which were a "stunning success" when they were created and used in 2009 and 2010.

Neal introduced the Build America Bonds Act of 2015 two years ago, which would have permanently reinstated and expanded the BAB program.

About $181 billion of BABs were issued before the bonds expired at the end of 2010.

"I think investing in those sorts of initiatives can return us to a connection with … the middle class," he said.

Neal also opposes the Republicans' plan to concentrate tax cuts at the top, a move that could raise taxes on the middle class. Although tax policy is complicated and consequential, he said, he suggested bipartisan efforts should be made, similar to those of former Michigan Republican Rep. Dave Camp several years ago when he included Democratic suggestions in his tax reform proposal.

"There could be an appetite here for some common ground on tax reform," Neal said, adding that the current system is underproductive and inefficient. "It's stuck in the eighties. It's a rotary phone in a smartphone world."

However, he is critical of what he believes are GOP tax cuts that could increase the federal budget deficit.

"All of this is being done without deficits in mind," Neal said. "I want our Republican friends to hold their party and president-elect to the same standard they held Barack Obama. Do deficits only count when there is a Democrat in office?"

Meanwhile, Brady and Neal have announced the tax policy subcommittee members for the 115th Congress. The Republicans include: Reps. Peter Roskam from Illinois; Dave Reichert from Washington State; Pat Tiber from Ohio; Tom Reed from New York; Mike Kelly from Pennsylvania; Jim Renacci from Ohio; Kristi Noem from South Dakota; George Holding from North Carolina; and Kenny Marchant from Texas.

Democrats on the subcommittee include ranking member Lloyd Doggett from Texas, as well as: Reps. John Larson from Connecticut; Linda Sanchez from California; Mike Thompson from California; Suzan DelBene from Washington State; and Earl Blumenauer from Oregon.

The Bond Buyer

By Evan Fallor

January 12, 2017

A Tax Credit Turns 30.

The low-income housing tax credit (LIHTC) has helped house millions, and it remains a vital driver of development. The 30-year track record of the LIHTC offers compelling evidence that affordable housing is good business, a stable asset class, and a strong driver of economic activity and neighborhood improvement.

Among the myriad ways the U.S. Internal Revenue Code affects commercial real estate is through a federal tax incentive that has become the most important tool to develop and rehabilitate affordable housing: the LIHTC. Since 1986, it has attracted enough private equity to produce nearly 3 million apartments for working-class families, seniors, and formerly homeless individuals. When one looks back over a generation of housing tax credit activity, several themes of importance to the entire real estate industry emerge:

Affordable housing can be a smart real estate investment. A 2015 survey of the housing credit throughout its history by New York City–based professional services firm CohnReznick found that equity investors have realized 98 percent of their anticipated federal tax credits (dollar-for-dollar reductions in federal income taxes owed) through calendar year 2014. The report also noted that yields on housing credit fund investments have maintained a healthy premium over yields on ten-year Treasuries, "with an approximate 400-basis-point buffer since 2011."

Affordable housing can be a viable development opportunity. Contrary to popular perception, most LIHTC-supported and other affordable developments are delivered by for-profit firms. According to a 2016 paper from Harvard University's Joint Center for Housing Studies, for-profit companies among the largest 50 developers were responsible for 79 percent of all affordable housing starts between 2009 and 2014. Nonprofit developers also are important players in LIHTC-supported development. Various studies have shown that both for-profit and nonprofit sponsors execute LIHTC-supported developments of similarly high quality and financial performance.

Affordable housing is a significant driver of overall multifamily construction activity. The housing tax credit drives the creation of roughly 50,000 new units per year—a significant share of overall multifamily development activity even during the current boom in new apartment construction. The LIHTC also supports the rehabilitation of another 50,000 existing units. The Washington, D.C.–based National Association of Home Builders estimates that the LIHTC annually generates 95,700 jobs; $3.5 billion in federal, state, and local tax revenue; and $9.1 billion in wage and business income.

Affordable housing development can strengthen struggling areas. Housing credit properties are found in many types of neighborhoods and usually—if not always—provide higher-quality housing than their residents could otherwise afford or access. A working paper from the National Bureau of Economic Research found that LIHTC-supported development delivers significant impact at the community level as well: each LIHTC-supported development in a low-income area generates aggregate benefit in the neighborhood of $116 million, increasing surrounding home prices by 6.5 percent (which boosts the local tax base) and lowering crime rates.

Housing credit development and management face challenges, however. Industry participants agree that total development costs for LIHTC-supported properties in some markets are high in relation to existing affordable units, and even some market-rate homes, for reasons that include higher construction quality and excessive state and local regulatory requirements.

The CohnReznick report found that 17 percent of LIHTC-supported properties operated below breakeven (a debt-coverage ratio less than one), but noted that this percentage is way down from ten years prior and that "the great majority of properties that did not achieve breakeven operations in 2014 failed to do so by relatively modest amounts." Analysis by certified public accountants Novogradac & Company, based in Bethesda, Maryland, has shown that net operating income as a percentage of total rental income had declined annually from 2010 through 2013 for LIHTC-supported units, with a small upward rebound in 2014, which slightly reversed a negative trend.

The biggest challenge facing the housing tax credit, though, is the overwhelming demand for the housing it enables developers to produce, which vastly exceeds the amount of tax credit authority available to states every year. In a broader housing market where supply is probably 3 million units short of demand, according to industry estimates, low-income renters—including millions filling critical jobs in the workforce such as teachers, nurses, firefighters, and police officers—are paying half or more of their income for housing, living in substandard units, and sacrificing on other basic needs to pay their rent.

An expanded LIHTC would help ease that crunch. Senators Maria Cantwell (D-Washington) and Orrin Hatch (R-Utah) have introduced a bill to increase credit authority by 50 percent. The proposed legislation would help create or preserve approximately 1.3 million affordable homes over a ten-year period—an increase of 400,000 more units than is possible with current authority. Efforts expected by Congress next year to reform the tax code could create an opportunity to enact the proposal. Tax reform could also endanger the credit or weaken its effectiveness, according to industry experts.

The 30-year track record of the LIHTC offers compelling evidence that affordable housing is good business, a stable asset class, and a strong driver of economic activity and neighborhood improvement. Regrettably, it is also a basic foundation for family success that a growing number of Americans cannot access.

Urban Land Institute

By Stockton Williams

December 13, 2016

Stockton Williams *is the executive director of the ULI Terwilliger Center for Housing.*

IRS Releases Interesting Private Letter Ruling on Build America Bonds.

On January 13, 2017, the Internal Revenue Service released Private Letter Ruling 201702009. The IRS held in this private letter ruling that the existence of unspent "available project proceeds" would not cause an issue of Build America Bonds ("BABs") to lose their status retroactively when they are redeemed with the proceeds of tax-exempt bonds.[1] The IRS further held that the issuer of the BABs would not lose any subsidy paid to it in respect of the BABs for the period that ends on the BABs' redemption date. This private letter ruling is most interesting for an opinion that the IRS expressly said that it was not giving but that is unavoidably implicit in the holding of the private letter ruling.

Continue Reading

By Michael Cullers on January 18, 2017

Squire Patton Boggs

Breaking News: Rev. Proc. 2017-13 Released

The IRS has released Rev. Proc. 2017-13, which provides updated safe harbors from private business use for management contracts. Click here for a copy; we will have more on this soon.

By Alexios Hadji on January 17, 2017

Squire Patton Boggs

US Mayors Raise Concerns Over Threats to Municipal Bonds.

US mayors have reiterated the importance of federal infrastructure investment and their concerns over the threat of municipal bonds losing their tax-exempt status, as Donald Trump takes office.

Three hundred mayors gathered in Washington DC at the US Conference of Mayors Winter Meeting with some using the platform to express their fears that the new administration will remove the exemption on one of the most important tools for funding infrastructure.

“We are fighting to protect [the tax exemption] so that we can build schools, roads, hospitals and protect jobs without costing middle-class taxpayers billions of dollars that they cannot afford,” said Steve Benjamin, Mayor of Columbia, and Second Vice President of the US Conference of Mayors.

Other concerns discussed over the three days of the conference included immigration reform, policing, and the repeal of the Affordable Healthcare Act, otherwise known as Obamacare.

Mitch Landrieu, Mayor of New Orleans and Vice President of the US Conference of Mayors, spoke out against any new plans for immigration reform that would force cities to become a “deportation force for federal government”.

“Everyone is welcome in our cities–they are not the dark foreboding places that people have talked about,” said Landrieu. “The President-elect paints with too broad a brush.”

Playing on Trump’s campaign slogan, Landrieu added: “Investment needs to take place in policing for safety and infrastructure for jobs. We need to make America safe again.”

But while the mayors are keen to air their views on what works best for US cities, they are looking to establish consensus with the new administration. Last month, Mick Cornett, Mayor of Oklahoma City and President of the US Conference of Mayors, took comfort in the fact that President-elect Trump expressed his support for continuing the tax-exempt status of municipal bonds when they met in Trump Tower.

Mike Pence, the Vice President-elect of the US joined a lunch meeting this week, the first time a Vice President-elect has attended a US Conference of Mayors meeting before being sworn in.

Although short on detail, Pence emphasised the importance of infrastructure, public safety and education.

“This administration is going to be a friend to America’s mayors,” he added saying that he and “Donald Trump are going to work in partnership with city halls all across America”.

Earlier Cornett had added that relations with the incoming Trump administration were “so far so good” and paid tribute to treatment received from the outgoing Obama administration over the past eight years.

“Although many of us mayors may differ on some of the policies of the administration we had good access to the executive branch and we were treated well and respected.”

CitiesToday

by Jonathan Andrews

17th January 2017

Pirates in the Desert: Oakland Raiders Charging Toward Biggest Taxpayer Subsidy in NFL History.

If the relocation is approved, a Las Vegas hotel tax hike would fund nearly 40 percent of the Raiders' new stadium

The Oakland Raiders moved one step closer this week to leaving the San Francisco Bay Area for Las Vegas. If the relocation deal is approved, a hotel-room tax increase at the nation's gambling hub would help pay for a shiny new $1.9 billion stadium.

The team filed its paperwork to win approval for the move from the National Football League, the NFL announced Thursday.

"The application will be reviewed in the coming weeks by league staff and the stadium and financing committees," the league said in a statement. The deal also requires the support from at least 24 of the 32 NFL team owners in a vote that would take place during a meeting in Phoenix on March 26-29.

If the relocation is approved (and Bay Area investors fail to entice the team to stay), then the new home of the Las Vegas Raiders would become the largest taxpayer-subsidized stadium deal in NFL history, blowing past the $600 million in public money used to build the Atlanta Falcons' $1.5 billion Mercedes-Benz Stadium and the nearly $500 million the public is picking up for the U.S. Bank Stadium in Minneapolis, the future $1.06 billion home of the Minnesota Vikings.

State officials have said the team would bring more tourists to Las Vegas, but critics question whether the benefits outweigh the costs.

"The big carrot being held out to Vegas residents is that it will bring in new tourism that will help pay for the hotel-tax increase," Neil deMause, co-author of the book "Field of Schemes," told Salon in an email. "The notion that there are currently tourists who aren't going to Vegas but will start to do so once there are Raiders games to be seen is, let's say, unproven at best — it's far more likely that existing visitors will just reschedule their planned trips around what NFL games they want to see, but the NFL boosters don't want to hear that."

With the help of Goldman Sachs, the NFL and Raiders owner Mark Davis would arrange $500 million in financing to fund the new Vegas stadium. Another $650 million would come from billionaire casino magnate and major Republican Party donor Sheldon Adelson, one of the richest men in America. The rest, $750 million, would come from a lodging tax paid primarily by tourists that was approved by state lawmakers in October. The subsidy deal explicitly excludes the public from sharing in the future profits from the stadium and would lock in the hotel tax even if the project comes in under budget, according to the San Francisco Chronicle.

Local officials and team backers often argue that deals like this ultimately benefit the public by creating jobs and generating peripheral economic activity and tax revenue. Yet the immense wealth of team owners and stakeholders has critics questioning why public funds are needed when the primary individual beneficiaries are private citizens with enough financial clout to fund and build these projects on their own. Adelson's net worth is estimated to be about $31 billion, according to Forbes, and Davis, who inherited the Raiders from his father, is worth an estimated $500 million.

The biggest issue for critics like DeMause is the sheer amount of public money going to stadium projects. Pitching in a few tens of millions of dollars on a big project that would benefit private investors might be justifiable if there’s a proven net increase in jobs and tax revenue to help fund truly public projects like road maintenance and schools.

But evidence is scant about the long-term benefits (not just temporary spikes in construction jobs and other project-related economic activity) and the so-called multiplier effect, the claim that publicly-subsidized megaprojects increase incomes and therefore create more spending and economic activity. A study by economists Roger Noll and Andrew Zimbalist in the late ’90s concluded that backers of these types of deals often radically overstate the long-term benefits.

“A new sports facility has an extremely small (perhaps even negative) effect on overall economic activity and employment,” the authors wrote. “No recent facility appears to have earned anything approaching a reasonable return on investment.”

Bay Area proponents of keeping the Raiders in Oakland are offering a new $1.25 billion stadium, but so far that proposal would be privately funded, and smaller. If business executives like Adelson believe in the magic of capitalism, perhaps they should play ball on a level playing field by declining handouts to subsidize their investments.

SALON.COM

ANGELO YOUNG

SUNDAY, JAN 22, 2017 06:00 AM PST

TAX - OREGON

[Village at Main Street Phase II, LLC v. Department of Revenue]

Supreme Court of Oregon, En Banc. - December 30, 2016 - P.3d - 360 Or. 738 - 2016 WL 7488855

Taxpayers challenged county assessor’s real market value of improvements on their real property.

Assessor sought preliminary ruling that it had statutory right to pursue counterclaims alleged in its proposed amended answers challenging value of taxpayers’ land.

The Tax Court granted preliminary ruling in favor of taxpayers. Department of Revenue and assessor appealed. The Supreme Court reversed and remanded. After taxpayers served notices of voluntary dismissal before assessor could file amended answers, the Tax Court entered judgment of dismissal, over assessor’s objection, and denied subsequent motions for relief from judgment filed by Department and assessor. Department and assessor appealed.

The Supreme Court of Oregon held that as matter of apparent first impression, Supreme Court’s remand following its determination that assessor had statutory right to pursue counterclaims required Tax Court to allow pending amended answers to be entered before turning to taxpayers’ subsequently filed notices of dismissal.

Supreme Court’s remand, which followed its determination that county assessor had statutory right to pursue counterclaims alleged in its proposed amended answers challenging value of taxpayers’ land, required Tax Court to allow pending amended answers to be entered before turning to taxpayers’ subsequently filed notices of dismissal of property tax appeals challenging assessor’s value of improvements on their land. Although remand made no statement about Tax Court’s dismissal rule, Tax Court's dismissal failed to implement Supreme Court's decision, which reversed Tax Court's only basis for denying entry of amended answers, and action was remanded for "further proceedings," which included implied directive to enter assessor's answers

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TAX SALES - UTAH

Jordan v. Jensen

Supreme Court of Utah - January 10, 2017 - P.3d - 2017 WL 104642 - 2017 UT 1

Purported owners of severed mineral interest brought quiet title action against successors to purchaser of real property at tax sale, and successors counterclaimed to quiet title and brought third-party complaint against lessor.

The Eighth District Court granted summary judgment to owners and lessor. Successors appealed.

The Supreme Court of Utah held that four-year statute of limitations could not be applied after tax sale was conducted in violation of owners' due process rights, overruling *Hansen v. Morris*, 3 Utah 2d 310, 283 P.2d 884.

Four-year statute of limitations applicable to challenges to tax titles could not be applied to bar quiet title action brought by mineral interest owners after tax sale was conducted in violation of owners' due process rights, despite contention that constructive notice of tax sale was sufficient to trigger statute of limitations without violating due process. Statute was not self-executing time bar, but was limitations period that was triggered by county's adversarial action and sale of property at tax sale, and names and addresses of owners were reasonably ascertainable, rendering constructive notice insufficient; overruling *Hansen v. Morris*, 3 Utah 2d 310, 283 P.2d 884.

GOP Expected to Take Aim at Local Tax Deductions.

State and local governments are fighting to avoid becoming big losers in tax reform — and they hope President-elect Donald Trump will be an ally.

Trump and congressional Republicans are aiming to pass tax-reform legislation this year that lowers rates and curbs and eliminates tax breaks.

In the process, two key preferences important to state and local governments, the deduction for state and local taxes and the tax exemption for municipal bonds, may be on the chopping block.

The two preferences are among the most expensive provisions in the tax code. They are also viewed as disproportionately benefiting upper-income people.

Of the two, the state and local tax deduction, which tends to benefit areas that lean Democratic, looks to be more endangered.

A 2015 paper from the Tax Foundation found that the 10 counties that benefit the most from the deduction are located in New York, New Jersey, California and Connecticut.

House Republicans are currently drafting a bill based on a tax-reform blueprint they released in June. That plan would eliminate the state and local tax deduction, since it does away with all itemized deductions except those for mortgage interest and charitable giving.

House Ways and Means Committee Chairman Kevin Brady (R-Texas) said at a Heritage Foundation event in December that he thinks there's "merit" to eliminating the deduction while also lowering rates.

"The added benefit here is that the federal tax code will no longer subsidize higher taxes at the local level," he said. Brady acknowledged that eliminating the deduction would be a big change and asked the public to look at his plan and provide feedback.

The tax plan Trump released in September did not specifically mention the deduction but would cap itemized deductions at $100,000 for individuals and $200,000 for married couples.

Groups representing state and local governments are concerned about the elimination of the deduction because it could reduce the government's flexibility to make tax changes.

"We're big proponents of federalism and we feel this strikes at the heart of it," said Brett Bolton, principal associate for federal advocacy at National League of Cities.

Emily Brock, director of the Government Finance Officers Association's federal liaison center, said her group is asking Congress "to honor the commitment they've made which is the partnership between the federal government and state and local governments."

Max Behlke, director of budget and tax policy at the National Conference of State Legislatures, said states with high income taxes are "very wary" about the deduction being eliminated. If the deduction is eliminated, the states could face pressure to lower their taxes.

It's "definitely possible" that Trump could be sympathetic to keeping the deduction because he's from a state with a high income tax. However, Trump may defer to Congress on taxes, Behlke said.

The municipal bond tax exemption is more likely to be preserved than the state and local tax deduction, and its preservation is the top tax reform priority for state and local governments.

The exemption allows state and local governments to have lower borrowing costs when they issue debt to finance infrastructure projects.

The House Republicans' tax-reform blueprint and Trump's tax plan are both silent on the municipal bond tax exemption, though the blueprint discusses eliminating tax breaks that benefit special interests.

But during a meeting at Trump Tower last month, Trump told a group of mayors that he supports the tax exemption.

While state and local governments are encouraged by Trump's comments, they are still concerned that changes to the tax exemption will be made. Many of the details about what will be included in tax-reform legislation is unknown, and many of the policy positions of the incoming administration are not firm.

"It's positive, but again, tax reform still has to go through Congress," said David Parkhurst, general counsel of the National Governors Association.

Groups held a briefing for Capitol Hill staff on the municipal bond exemption in late November, and they are meeting with lawmakers on the Hill to educate them about the importance of the exemption.

On Tuesday, groups in a public-finance network sent lawmakers a letter in support of tax-exempt bonds.

“They are the best way to implement the infrastructure needs of each community effectively, as the decision to issue bonds for various projects is determined and approved by either the citizens themselves through bond referenda or their elected legislative bodies,” the groups said.

The exemption does have support on Capitol Hill, including from some Republicans. Last year, Reps. Randy Hultgren (R-Ill.) and Dutch Ruppersberger (D-Md.) launched a municipal finance caucus.

“Tax reform is complex and wrought with many pressures,” Hultgren said in a statement. “I hope to see this key financial tool, which has worked for more than a century, maintained in a much-needed comprehensive tax reform package.”

THE HILL

BY NAOMI JAGODA – 01/10/17

The Case Against Tax Money for Stadiums, Movies.

The Tampa Bay Rowdies owner has pledged to privately finance an $80 million renovation of Al Lang Stadium, envisioned above. If the Rowdies and other teams like the Orlando soccer team can pay for stadium renovations, why can’t NFL teams?

Florida’s state legislators from both political parties have resisted corporate welfare schemes in recent years, and taxpayers should celebrate.

Corporate welfare gives a select few industries special handouts at the expense of everyone else. Supporters of corporate welfare claim that such programs create jobs, but the facts demonstrate that’s rarely the case. Even when jobs are created, each job comes at a tremendous cost to Floridians.

Take Enterprise Florida, for example, a public-private partnership that promised to create 200,000 jobs by 2005. After $1.7 billion in incentives, it had reached only slightly more than half of its goal as of 2013. And while the program was intended to be funded equally between public and private funds, an estimated 90 percent of its funding came from the taxpayers.

Some claim that while Enterprise Florida was a failure, other programs are still worth the taxpayer’s dime. In fact, the Tampa Bay Times editorial board cited sports and tax film credits as worthy programs to keep intact, albeit with appropriate reforms.

But the facts tell another story.

When it comes to sports stadiums financed through Florida’s Professional Sports Facilities Incentive Program, according to the state’s own economists, for every dollar invested in sports renovation projects, the state sees only 30 cents returned in economic activity — a far cry from a sound investment.

What’s more, plenty of sports owners can afford to renovate without a special taxpayer-funded deal.

Case in point: The Orlando City Soccer Club is building its own stadium. And while the Orlando team originally asked for $30 million from the state, it announced it would self-fund the stadium after citizens and lawmakers opposed state funding.

In St. Petersburg, Tampa Bay Rowdies owner Bill Edwards has pledged to privately finance an $80 million renovation of Al Lang Stadium in order to bring a Major League Soccer team to the region.

If these sports teams can renovate on their own, why do other teams such as the NFL's Tampa Bay Buccaneers, Miami Dolphins or Jacksonville Jaguars deserve taxpayer money?

As for film production handouts, they too have a storied past. The state's economists find that the film subsidy program only produces up to 43 cents for every dollar invested.

The program hurts taxpayers, while often going to projects that don't produce any long-term jobs in the Sunshine State. Of course, the film industry lobbying for the special favor alleges the program produces more revenue, but the estimates don't pass muster in comparison to the state estimates.

What's more, state after state that has gone down the road of film tax credits has paid the price of doing so. The University of Southern California conducted a national study on state programs, finding that since 1999 tax credits have created close to zero jobs, even in states like California and New York. Taxpayers, on the other hand, are still on the hook for over $10 billion to Hollywood producers and movie stars.

Floridians have enough legitimate demands on their tax dollars, such as education and transportation expenses. It's not our responsibility to ensure that Ben Affleck's new movie is profitable or that sports executives have enough extra cushion to ensure fans will flock to their fields.

For the past several years, lawmakers have rightly rejected some of these efforts to boost special interests — now is not the time to reserve course. Instead, lawmakers should keep fighting against all forms of corporate welfare so that everyone has a chance to succeed.

Tampa Bay Times

By Chris Hudson

Wednesday, January 11, 2017 3:09pm

Chris Hudson is the Florida state director of Americans for Prosperity, a conservative political advocacy group.

Munis Are Critical for Infrastructure, Groups Tell Lawmakers.

WASHINGTON – State and local groups told members of Congress that tax-exempt bonds are the cornerstone of infrastructure financing, as the lawmakers consider how to increase spending on roads and bridges as well as tax reforms that could entail restrictions on tax exemption.

Tax-exempt bonds are used by more than 50,000 state and local governments, and nearly 75% of infrastructure funding comes from munis, the 29 groups said in a joint letter to House and Senate members.

“We welcome the chance to work with you to develop new tools as a complement to tax-exempt municipal bonds,” the groups wrote. “We would note that even new ideas – including variations of public-private partnership models – will likely rely on municipal bonds.”

The two-page letter was signed by representatives of the Government Finance Officers Association, the National Governors Association, the U.S. Conference of Mayors (USCM), the National Association of State Treasurers, and the National Association of Counties (NACo) and other groups.

The organizations comprise the Public Finance Network, a coalition of state, local and utility issuers and stakeholders. While the GOP blueprint for tax reform released last year does not mention the muni exemption directly, its intention of repealing unnamed deductions have made state and local groups uneasy of a cap or repeal.

House Ways and Means Committee Republicans said Tuesday that they are “moving forward aggressively” to turn the blueprint into formal legislation that would eliminate special interest provisions they said keep rates high and “increase confusion.”

Michael Belarmino, NACo’s associate legislative director and associate general counsel, said the letter is meant to be a “refresher” for lawmakers as the 115th Congress kicks off.

“I’m hoping that this message continues to resonate with them,” Belarmino said. “It seems pretty clear that there are many things on their agenda at this point and where tax reform is going to fall is anybody’s guess.”

The coalition stressed that issuers save on average roughly two percentage points on borrowing costs to finance infrastructure investments through munis, which they said equates to “substantial” savings for taxpayers.

Munis have financed more than $2 trillion in new infrastructure over the past decade, and are on track to finance another $2 trillion over the next ten years, the coalition wrote.

“As the new administration and Congress seek ways to increase infrastructure investments, we would note an incredibly powerful tool already in hand – tax-exempt municipal bonds,” it wrote.

The groups argued that munis are the most effective method to finance community infrastructure, as bond issuances are determined and approved through citizen referenda or by elected legislative bodies.

Several state and local groups have told The Bond Buyer that they set their sights on Congress after President-elect Donald Trump told the USCM in December that he supports maintaining the muni exemption.

The Public Finance Network also cited as good resources on munis Reps. Randy Hultgren, RIll., and Dutch Ruppersberger, DMd., two major allies of the muni exemption who chair the bipartisan Municipal Finance Caucus in Congress.

The Bond Buyer

By Evan Fallor

January 10, 2017

Trio of Lawmakers to Seek Tax Reform Revenues for Infrastructure.

DALLAS – A bipartisan trio of lawmakers intends to file a pair of House bills that would use revenues from international tax reform to fund infrastructure projects.

Rep. John Delaney, DMd., said Monday that he and Rep. Rodney Davis, RIll., will propose the Partnership to Build America Act that would create the American Infrastructure Fund to finance local and state projects.

As part of the effort, Delaney and Rep. Ted Yoho, RFla., will sponsor the Infrastructure 2.0 Act that would dedicate additional revenues through repatriation of corporate overseas earnings to stabilize and expand the federal Highway Trust Fund.

The proposals would provide an incentive for corporations to bring into the U.S. an estimated $2 trillion in overseas earnings, Delaney said, spurring private sector reinvestment and growth.

Delaney proposed similar measures in 2014 and again in 2015 with significant bipartisan support, but neither gained traction in Congress.

His third attempt at linking the repatriation of overseas earnings by U.S. corporations could be the answer to calls for more infrastructure funding, Delaney said.

"If the next President and leaders in Congress want to rebuild America in a fiscally responsible way that has deep bipartisan support, we've given them a blueprint," he said. "A bold infrastructure-tax deal that combines legitimate support for new projects and progrowth reform would be transformative for the country, for our economy and our quality of life."

However, Rep. Kevin Brady, RTexas, chairman of the House Ways and Means Committee, has said any revenue resulting from corporate tax reform should be used for overall tax reforms rather than just dedicated to infrastructure.

House Speaker Paul Ryan, RWis., and other House Republicans support Brady's stance, but Senate Republicans seem to be more open to the idea of linking tax reform with infrastructure funding.

"I think there's an interest among our members, in both the House and the Senate in doing something on infrastructure, but my guess is if that gets done, it probably hitches a ride on tax reform," said Sen. John Thune, RS.D., chairman of the Senate Commerce Committee and third ranking Republican in the Senate.

"I don't know that just an infrastructure bill on its own, a standalone, would go anywhere,"

Thune told reporters last week. "I think it would have to be coupled with something that we view to be really advantageous in terms of stimulating the economy."

The Partnership to Build America Act would capitalize the infrastructure fund with $50 billion of proceeds from the sale of 50year, 1% fixed rate bonds that would be purchased by companies willing to bring back overseas earnings.

These bonds are not intended to be a good investment on their own but would be transferable, Delaney said.

For every $1 invested in the bonds, the companies would be allowed to bring back an estimated $4 of foreign profits without paying any U.S. tax. The ratio would be set through a reverse Dutch auction, which Delaney said would allow the market to set final rates of return.

Local governments could use low-interest loans from the AIF for transportation, communications, education, and water projects.

At least 25% of the projects financed through the AIF must be public-private partnerships with at least 20% of project financing coming from private capital.

The Infrastructure 2.0 Act would provide six years of Highway Trust Fund solvency by supplementing revenues from federal fuel taxes and other dedicated fees, Delaney said.

The measure would levy a mandatory onetime tax of 8.75% on existing overseas corporate profits to replace the current rate of 35% on earnings brought into the U.S.

The tax proposal would generate $120 billion for the HTF and $25 million for a pilot program of regional infrastructure planning groups, according to Delaney.

The legislation also would create a bipartisan House and Senate joint commission tasked with developing a solution for permanent solvency of the HTF, he said.

The Bond Buyer

By Jim Watts

January 10, 2017

Slowing of Muni Tax Regs Seen in 2017, But Three Projects Watched.

WASHINGTON – Municipal market participants see a slowing of Treasury Department and Internal Revenue Service guidance and rules in 2017, but plan to closely watch rules on political subdivisions, tweaks to management contract guidance, and rules for public approval of private activity bonds.

“The change in the White House to a Trump administration will certainly put a severe damper on any regulatory activities for most of [2017],” said Matthias Edrich, a tax partner with Kutak Rock in Denver. “Not just for public finance but for any regulatory efforts.”

Emily Brock, director of the Government Finance Officers Association’s (GFOA) federal liaison center, agreed. “I think what we will see is a bit of a calming down of the priority list,” Brock said. “One thing that drew our attention … is the political subdivision definition. We’ll continue to keep an eye on that.”

John Cross, Treasury’s associate tax legislative counsel, said that while he can’t comment on regulatory priorities that will be set by the incoming policymakers for the new administration, Treasury’s two most active existing muni projects at the staff level are The Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) public rules for private activity bonds (PABs) and bond reissuance regulations.

He also said the staff has been considering some discrete, clarifying changes to the recent more flexible management contract safe harbors under Rev. Proc. 2016-44, which was issued last year.

In October, the Treasury and IRS released their final 2016-2017 priority guidance plan, which included seven projects for tax-exempt bonds. Three projects were completed in 2016 – final issue price rules, guidance on management contracts, and final rules on arbitrage investment restrictions. The remaining ones are bond reissuance rules, guidance on remedial actions for tax-advantaged bonds, final regulations for public approval of PABs, and a new definition of political subdivisions for this year.

TEFRA Regulations

Perhaps no other pending regulatory measure is as long-awaited as the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), which originally date back nearly 35 years.

Bond attorneys and other market participants have long clamored for a clarification of public approval requirements for private PABs, which were written in temporary form in 1983 by Treasury and the IRS.

In 2008, proposed regulations, which were well received by market participants, were released, but have yet to be finalized.

Officials from the National Association of Bond Lawyers (NABL) have previously told The Bond Buyer they believe, and hope, the TEFRA rules will finally be completed in 2017.

NABL has called for a clarification of the TEFRA public approval requirements for PABs, which it said were burdensome. The group has recommended regulators broaden the allowance for PAB proceeds to be used for working capital without the public notice specifically mentioning that purpose.

In order to be tax exempt, PABs must be approved by the issuer and, in some cases, the governmental entity that has jurisdiction over the area where the bond-financed facility will be located. The bonds can be approved by voter referendum or by elected officials following a public hearing.

Ed Oswald, a partner with Orrick, Herrington, and Sutcliffe in Washington, said he will be tracking TEFRA developments closely, which he said are long overdue.

“The original regulations came out in 1983 and are very antiquated,” Oswald said. “I think the muni market would love to have the TEFRA regulations in final form.”

Stefano Taverna, an attorney with McCall, Parkhurst & Horton in Dallas, and the chair of the American Bar Association’s tax-exempt financing committee, was cautiously optimistic about final regs in 2017.

“TEFRA regs have been active for quite some time so hopefully they get that out and publish something later this year,” Taverna said.

Edrich said that the release of final issue price rules last month may indicate the agency is trying to “clear the deck” of its highest priority guidance projects, but warned that the TEFRA regulations could be stalled during the first year of the Trump presidency.

Taverna said he expects market participants to spend the coming months trying to determine the issue price regulations’ impact on certain transactions, particularly competitive sales, since they do not become effective until June of this year.

The issue price regs contain special allowances for competitive sales and establish that the issue price for competitive sales will be the reasonably expected initial offering price under certain conditions.

The final rules are meant to be more flexible and workable, Cross said.

Political Subdivisions

Several muni market participants also said they will be watching developments on definition of a political subdivision for purposes of tax-exempt, tax credit and direct pay bond provisions — another project outlined in the guidance plan.

Most muni market participants felt the political subdivision rules proposed in February of last year by Treasury and the IRS were overly restrictive and could jeopardize the tax-exempt status of some outstanding bonds.

John Vahey, managing director of federal policy for Bond Dealers of America (BDA), said his group is hoping for more clarification for incidental private benefit rules that he feels raise more questions than answers. Vahey said BDA has questions tied to community development projects and how land purchases, for example, impact incidental private benefit.

The proposed rules say, among other things, that political subdivisions must serve a governmental purpose "with no more than an incidental private benefit."

"We're hoping for more clarification for incidental private benefit," Vahey said. "There's a few points that we've raised and that's one of the biggest ones."

The tax regulators began writing rules on political subdivisons after the IRS issued a technical advice memorandum in 2013 that found the Village Center Community Development District in Florida was not a political subdivision and could not have issued tax-exempt bonds because its board was developer-controlled rather than by publicly elected officials.

Bond lawyers complained the IRS was trying to change standards through the enforcement process rather than through public rulemaking, which would allow for public input.

The Treasury and IRS proposed rules on the definition of a political subdivision last February.

Under the current definition, an entity is a political subdivision that can issue tax-exempt bonds if it has a right to exercise a substantial amount of at least one of three recognized sovereign powers of a state or local governmental unit: eminent domain, taxation or police. The proposed rules would add two new requirements: that a political subdivision serve a governmental purpose "with no more than an incidental private benefit" and that it be governmentally controlled.

The agencies received many comments on the proposed rules, most of them critical, saying they were unworkable and could upend the muni market. They asked the rules be reproposed, at a minimum, or simply withdrawn.

Edrich, meanwhile, said that any efforts to "fix uncertainties" in the market created by the proposed regulations relating to the definition of a political subdivision may be stalled during Trump's first year.

Management Contracts

Another regulatory issue for the bond community in 2017 is guidance pertaining to management contracts.

In August, the IRS released Rev. Proc. 2016-44, which extended terms of long-term management contracts to up to 30 years from the previous 15-year limit, and also removed the formulaic fixed fee requirements for manager compensation.

Bond lawyers initially lauded the new management contract safe harbors, which they found to be more liberal than restrictive safe harbors established under Rev. Proc. 97-13 released in 2013.

But questions and concerns soon arose regarding the guidance, which was meant to allow for more incentive compensation, bond-financed infrastructure projects, and public-private partnerships.

NABL said the guidance is confusing and could limit the usefulness of safe harbors in short-term contracts. Concerns were also raised about how the guidance should be implemented.

Questions also surfaced regarding whether the term of a contract is retested when one is modified or a new one is entered into.

Taverna while the guidance made strides in liberalizing management contract guidelines, he hopes comments submitted to Treasury in November will lead to clearer guidance in the coming year.

The guidance "liberalized a lot of guidelines but in that process, it left open some questions," Taverna said. "Particularly what it means to have sharing of land losses and sharing of net profits."

"The purpose of the comments is to ask Treasury for more narrow guidance in respect to the revenue procedure and to provide more certainty to the corners of that guidance," he added. "Other than that I think they've done a very good job with the guidance plan."

Oswald agreed. "We're hoping for some additional guidance or amplification regarding the guidance which is otherwise helpful," Oswald said. "This would fill the void that other practitioners have observed in terms of details."

The safe harbors under Rev. Proc. 2016-44 apply to any management contract entered into on or after Aug. 22, but issuers can also apply the safe harbors to management contracts entered into before that date.

The guidance created three provisions containing limits ensuring no private ownership or leases: a state or local government "must exercise a significant degree of control of the managed property," the state or local government must bear the risk loss for damage of managed property, and the private party must agree not to take any tax position that is inconsistent with being a service provider.

Both Oswald and Taverna said they will also be tracking bond reissuance regulations, another Treasury guidance plan item that has not moved forward.

"The reason they're important is that the rules had been put out over years, somewhat on an ad hoc basis, and a lot were issued during the 2008 downturn when the market needed relief," Oswald said. "The reissuance guidelines need to be reformatted and reorganized."

Taverna said a common concern he has heard in the industry is what type of effect the Trump administration could have on published regs.

“What I find interesting and what a lot of folks are wondering is if the new administration will have an effect on the types of regulations published,” Taverna said. “[Donald] Trump said that for all new regulations that come out you’ll have to take two out. I don’t know if that will have an impact on the streamlining of regs.”

TEB

All eyes for the time being will be on Imraan Khakoo, the acting director of the IRS’ Office of Tax Exempt Bonds (TEB) who replaced Rebecca Harrigal late last year.

Khakoo had been Harrigal’s acting assistant. IRS officials did not specify how long Khakoo will be acting director of TEB.

Mark Scott, a former director of TEB who now has a private practice focused on representing whistleblowers, said he believes Khakoo’s lack of muni tax law knowledge, an area where agents are struggling to apply tax law and where enforcement is lacking, “doesn’t help anything.”

“Efficiency in TEB has gone down and it is getting worse at identifying good cases,” Scott said. “Even when they are identified, [TEB] is struggling to get agents to complete cases. The cases are there and the work can be done. Still, I anticipate this trend continuing.”

The number of agents doing audit work is roughly 60-65 overall, which is lower than the 70-75 agents Scott said he had in his peak when he served as TEB head.

According to IRS spokesman Dean Patterson, TEB closed 570 audits in fiscal 2016 and entered into 18 closing agreements in the same period.

TEB entered into 61 settlements under the voluntary closing agreement program (VCAP), a substantial drop from the 105 VCAP settlements reached during the prior fiscal year.

The 570 closed audits were two more than TEB closed in fiscal 2015, while the 18 closing agreements were one less compared to the prior fiscal period.

The total dollar amount from audit settlements in fiscal 2016, which ended on Sept. 30, was $10.72 million, and $11.68 million for VCAP settlements.

Patterson also noted that TEB does not have any webcasts planned for 2017.

Scott speculated that a reason VCAP figures have been dropping is due to a decrease in refundings, which had spiked several years ago. This trend may continue, he said, due to over-auditing in some areas, and allocating resources inefficiently.

“When you have a strong enforcement program, the voluntary closing agreement program motivates issuers to identify a problem before enforcers come in.,” Scott said. “When an audit program weakens, this motivation is reduced, and the impact of this will eventually be reflected in a lower number of requests for voluntary closing agreements.”

The IRS provided numbers, but not comments for this story.

The Bond Buyer

By Evan Fallor

January 12, 2017

[GFOA and Issuer Groups' Message to Congress: Munis Build Infrastructure.]

On January 10, 2017, GFOA and 28 other issuer groups, including our state and local sister organizations, sent a message to the entire Congress in support of the preservation of the tax exemption of municipal bond interest. The message reiterated that the municipal bond is the only infrastructure financing tool that is accessible to jurisdictions of all sizes to effectively access the capital markets. We emphasize that the municipal bond is the best way to effectively implement the infrastructure needs of each community because decision making is made at the local level. Read our letter.

Will you join the effort? Tell us your story!

GFOA continues to develop information for distribution to Congress about the tax exemption on municipal bond interest, including data showing the costs local governments may incur should the tax exemption come under review in comprehensive tax reform.

But the most effective communication comes from you.

What have municipal bonds built in your jurisdiction? Will you share pictures of the projects built by bonds? Jump on the hashtag #BuiltByBonds and @GFOA along with your Congressional representatives. Please let the Federal Liaison Center know of any communication heading up to your senator or representative, or let us know how we can help your efforts. Contact Emily S. Brock.

New Year, New Action on Marketplace Fairness.

On January 3, 2017, the City of Roanoke, Virginia, passed a resolution urging the U.S. Congress to act on legislation that will enable state and local governments to collect revenues due to local government. Congressional inaction over the past several years has resulted in an increase in the Virginia state sales tax from to 5.3%, from 5%, and has placed significant limitations on the jurisdiction.

The resolution asks the new Congress to act on legislation this year that would collect and remit sales taxes structured on a system of collection based upon the purchaser's location. Passing this legislation during the 115th Congress would "send the clear and unequivocal message to states and localities that the United States Congress supports small business women and men who create jobs, produce revenues to support essential infrastructure improvements, and create a stronger and more resilient economy for the benefit of all Americans," as stated in the resolution, which the City of Roanoke's City Council passed unanimously at its first meeting of 2017.

This resolution sends a clear message not only Roanoke's representative, Bob Goodlatte, Chairman of the House Judiciary Committee, but also to the state legislature and its governor, Terry McAuliffe, who has recently proposed a collection on certain out-of-state online retailers to collect sales taxes.

GFOA's Federal Liaison Center is working with our colleagues at the National League of Cities, U.S. Conference of Mayors, and National Association of Counties to distribute a template of this resolution and work toward a solution that would give marketplace fairness the chance to be considered and passed this year. Stay tuned for more details on this grassroots movement.

Read the resolution here.

Thursday, January 5, 2017

Why Texas Is Cheering a Tax Lawsuit Loss.

As gloomy government budget news stacks up in Austin, a state appeals court ruling issued Friday appears to erase a huge worry about the state's business franchise tax.

The parent company of AMC movie theaters sued the state over what it is allowed to include in non-taxable cost of goods sold. An initial ruling in the company's favor in May 2015 contained what the state thought was an overly broad definition of "costs" — one that Comptroller Glenn Hegar feared could require $6 billion in tax refunds to various businesses and a $1.5 billion annual reduction in state franchise taxes.

Friday's ruling from the 3rd Court of Appeals leaves the company's victory in place, but uses a narrower definition of costs of goods that apparently won't apply to most other taxpayers.

The difference could be worth billions to the state, allowing it to continue to collect franchise taxes much the way it does now.

The case turns on a legal definition in the state's tax code? of "tangible personal property" that includes "personal property that can be seen, weighed, measured, felt or touched, or that is perceptible to the senses in any other manner."

AMC takes "perceptible to the senses" to include movies and contends all of its costs for space should be included in its cost of goods sold. The comptroller argued that AMC is selling intangible property or a service and that it shouldn't be considered tangible personal property.

To compute its franchise taxes, the movie chain (like other businesses) subtracts its cost of goods sold from its total revenue and pays taxes based on the difference. Increasing the costs lowers the amount being taxed. The court ruled that AMC can include costs of exhibiting films in that calculation — a decision that means the theater chain will get $1.1 million in refunds for taxes it already paid.

The new ruling relies on a less encompassing definition that includes "films, sound recordings, videotapes, live and prerecorded television and radio programs, books, and other similar property embodying words, ideas, concepts, images, or sound, without regard to the means or methods of distribution or the medium in which the property is embodied…"

The state still lost the case, but according to Lauren Willis, a spokeswoman for the comptroller, this ruling doesn't present the kind of threat to other franchise revenue that the earlier ruling did.

The state will have to refund $1.2 million, plus interest and penalties, to AMC. But other taxpayers looking for the same treatment will have to fit within the narrower definition of tangible personal property to get refunds.

AMC's case is one of two lawsuits that threatened to knock big holes in the state's pocketbook. The other big tax case with potentially large implications — involving Midland-based Southwest Royalties — went to the Texas Supreme Court, with Hegar worrying publicly that an adverse ruling would cost the state as much as $4.4 billion. The state won that one in June.

On Monday, a day before the legislative session begins, Hegar will unveil his official revenue estimate which will tell lawmakers how much money will be available for them to write the next two-year budget. Money is expected to be tight, but it won't be because the state lost in court.

THE TEXAS TRIBUNE | JANUARY 9, 2017

By Ross Ramsey

2016 Year-End Review: Squire Patton Boggs

Despite an increase in the federal funds rate by the Federal Open Market Committee in December, municipal bond interest rates throughout 2016 were (and still are) extremely low when compared to historic rates. As a result, the volume of municipal bond issues reached an all-time high in 2016.

As discussed below, the Treasury Department released a number of highly anticipated and significant proposed and final regulations during 2016. In addition, to accommodate public-private partnerships, Treasury issued Revenue Procedure 2016-44, which allows issuers to enter into longer-term management contracts without resulting in private business use.

Continue reading.

The Public Finance Tax Blog

By Joel Swearingen on January 9, 2017

Squire Patton Boggs

States Will Have Increase in PAB Capacity in 2017.

WASHINGTON – States will have a modest increase in their capacity to issue private activity bonds in 2017 due to population increases and higher cap space allowed by the Internal Revenue Service.

The 50 states, the District of Columbia and the Commonwealth of Puerto Rico will have a total of roughly $35.69 billion of new capacity in 2017, an increase of 9.84% from the $32.49 billion in 2016.

Click here to see PAB chart

The 9.84% increase is more than nine percentage points higher than the increase heading into 2016, which was a 0.76% increase from the prior year.

The increase is due to the higher minimum amount of cap allowed by the Internal Revenue Service as well as population gains across the board. The PAB volume cap limit is based on the latest state population estimates released by the U.S. Census Bureau on Dec. 20 and a revised PAB cap formula published by the Internal Revenue Service in October.

The 2017 PAB volume cap for each state is the greater of $305.32 million or $100 per capita for each state for 2017. That's a slight change from the 2016 cap formula, which had the same per capita amount but a lower minimum of $302.88 million. The 2016 U.S. population as of July 1, 2016 was 326.54 million, up from the 324.37 million revised estimate for 2015.

A total of nine states will have PAB volume caps of $1 billion or greater in 2017. California, the nation's most populous state, will have a $3.93 billion cap in 2017, followed by Texas at $2.79 billion and Florida at $2.06 billion.

The remaining states with a cap of greater than $1 billion are Georgia, Illinois, New York, North Carolina, Ohio, and Pennsylvania. All had populations of 10 million or greater in 2016.

All but six states or territories will see increases in their new capacity to issue PABs in 2017.

Florida, at 1.68%, will have the biggest percentage increase in cap in 2017 compared with 2016. The Sunshine State had a $2.03 billion volume cap in 2016. Washington State is next, with a 1.64% increase in cap to $728.80 million, followed by Oregon with a 1.60% gain in cap to $409.35 million.

Connecticut, Illinois, New Jersey, New York, Pennsylvania, and Puerto Rico will all have decreased PAB volume caps next year compared with 2016. All but New Jersey experienced population decreases between 2015 and 2016.

Puerto Rico, at 1.81% to $341.13 million, will have the biggest drop in capacity for the coming year, followed by Illinois, with a 0.45% decrease to $1.28 billion, and Connecticut, with a 0.40% reduction to $357.65 million.

A total of 21 states and the District of Columbia will use the minimum amount of $305.32 million in 2017.

Private activity bonds are used by state and local governments to provide low-cost financing for projects that provide some kind of public purpose but include some private involvement.

Qualified PABs subject to the volume cap are exempt facility bonds such as water and sewage facilities, hazardous waste facilities and other utility facilities, as well as qualified mortgage revenue bonds, small issue bonds, student loan bonds and redevelopment bonds.

Qualified PABs not subject to the volume cap include exempt facility bonds such as airports, docks and wharves, as well as qualified veterans' mortgage revenue bonds and qualified 501(c) (3) bonds.

No states or territories will have an increase or decrease of 2% or higher in 2017; nine will have a fluctuation of greater than 1%.

The Bond Buyer

By Evan Fallor

December 23, 2016

Will Trump's Lower Income Tax Rates Really Hurt Muni Bonds?

There was some paranoia a couple years back surrounding the muni market. Those fears are cropping up again, but infrastructure momentum could make munis a safe bet.

It feels like deja vu all over again in the municipal bond market.

All the chatter of how President-elect Trump's lower income tax rates may hurt munis reminds us of the Meredith Whitney scare back in 2011.

She went on CBS's 60 Minutes program and claimed that more than 100 American cities could go bankrupt.

Oops.

O.K., we'll give her Puerto Rico and Detroit, but other than that, the muni market basically has been just fine.

Until recently. Remember, the income on a municipal bond is generally tax-free. As a result, lower income tax rates decrease a muni's attractiveness, at least on the tax front. So there are a bunch of naysayers, channeling their inner Meredith Whitney and claiming the sky may fall again in the muni world.

"And just the potential for lower tax rates immediately hit the bond market and brought municipal bond returns [yields] up and values [prices] down," says Bernie Kent, tax expert and Chairman, Schechter Investment Advisors, in Birmingham, Mich. (Remember, a bond's price moves in the opposite direction of its yield.)

But let's not panic.

We don't know when (or even if) tax rates will officially change, and history has shown it can take a while.

"Don't forget that both Reagan and Bush took a full year to get a tax cut in place," reminds Jim Robinson, bond expert and founder of Robinson Capital in Grosse Pointe, Mich.

Plus, there are some other variables to consider.

Granted, Lower Rates Could Make a Difference

The top federal tax rate for those making $500,000 or more, realistically could be over 44% these days. The top federal tax rate is currently 39.6%. Then you have to throw in the 3.8% Obamacare surtax and this pesky stealth surtax on high net worth individuals, says Kent. Without getting into the weeds of the calculation (it's called the Pease tax), you could find yourself taxed at 44%.

So if the top bracket drops to 33%, as both Trump and Paul Ryan suggest, the tax benefits of a municipal bond decrease.

A quick calculation shows you why.

In really simple terms, divide the municipal bond rate by (1 minus your tax rate).

Let's say the muni is yielding 5% and your tax rate is 40%. So the equation looks like this: 5/(1-0.40)

= 8.3%.

Consider that your cut-off when choosing between a corporate bond and a municipal one. If you find a corporate bond yielding more than 8.3% (good luck with that), take it, because you may be better off with that bond even if you have to pay taxes on the income.

But let’s say your rate drops to 33%, 7.46% becomes your cut-off. Granted it’s lower, but it’s still tough to beat in the corporate world.

The decision is never based on just one factor, though. Don’t forget about the quality of the bond, the duration, fees etc., says Kent.

But Trump Is a Big Infrastructure Guy

So he’s not going to want to kill the funding.

Remember, muni bonds are debt obligations issued by states, cities, counties and other governmental entities to raise money for schools, highways, hospitals or other public projects.

So when you buy a muni, you’re essentially lending money to the project in return for your money back and some additional interest. And as we mentioned, a bigger perk is that the income is often federal and state tax free.

And while we don’t have details, Trump may promote policies that actually help these bonds, says Mark Luscombe, principal analyst at Wolters Kluwer, a tax and accounting services company.

We know that some Trump’s infrastructure proposals may include tax incentives to create private-public partnerships for infrastructure. He also has signaled that he’d consider Build America Bonds.

And We Know There Will Be Interest Rate Increases

But even that is hedged into the calculation, says Robinson.

Short-term debt is already the optimal choice compared to longer-term bonds, because no one really knows what the interest-rate future looks like either.

There is Talk of Decreasing the Tax on Interest Income

One potential tax change that could benefit corporate bonds is if the tax on interest income is reduced. Bonds pay interest to their holders (usually) semi-annually. Currently that interest is taxed at the ordinary income rates, which could be as high as 44%, as we mentioned above.

“There is talk of implementing a cap at 16.5%,” says Robinson, (which is basically 50% of the highest proposed rate of 33%).

“If that happens, we’ll see a rally in corporate bonds as opposed to munis getting beaten up,” Robinson adds.

So What Should You Do?

Rates have gone up and down over the years and munis have managed to beat out their taxable counterparts. And even with all this noise, the relationship between munis and corporates is about the same as it was 12 months ago, notes Robinson.

If you are a high-net worth individual, you probably still will need municipal bonds in your portfolio regardless of what happens.

And many will argue that now's a good time to buy them. Especially with variables like market volatility and the Fed and Trump presidency.

To boot, municipalities may have to increase their yields to keep investors coming, which will only help investors.

So don't overreact like the market did. Just take advantage of it.

TheStreet

by Tracy Byrnes

Jan 3, 2017 1:33 PM EST

TAX - WASHINGTON

City of Snoqualmie v. King County Executive Dow Constantine

Supreme Court of Washington, En Banc - December 22, 2016 - P.3d - 2016 WL 7421401

City brought action challenging the constitutionality of statutory provision, which required Indian tribes taking advantage of property tax exemption for tribal property to make payment in lieu of leasehold excise taxes if property was not leased.

The Superior Court granted partial summary judgment in favor of the city. Department of Revenue appealed to Supreme Court, and Supreme Court retained the case for review.

The Supreme Court of Washington held that:

- City had direct standing to challenge constitutionality of statutory provision under more liberal standing requirements for cases of public importance, and
- Payment in lieu of leasehold excise taxes was not a "tax," and thus, payment was not subject to State Constitution's tax requirements.

City had direct standing to challenge constitutionality of statutory provision, which required Indian tribes taking advantage of property tax exemption for tribal property to make payment in lieu of leasehold excise taxes if property was not leased, under more liberal standing requirements for cases of public importance. Issue of whether payment in lieu of taxes was a tax would impact Indian tribes throughout the state, and several other tribes would be directly affected by invalidation of exemption and accompanying payment in lieu of taxes.

City had representative standing on behalf of its residents to challenge constitutionality of statutory provision, which required Indian tribes taking advantage of property tax exemption for tribal property to make payment in lieu of leasehold excise taxes if property was not leased. Residents had been subjected to tax shift, payment in lieu of taxes could not compensate for the total loss, and residents suffered injury from the exemption and payment in lieu of taxes.

Payment to county by Indian tribes, which took advantage of property tax exemption for tribal property, in lieu of leasehold excise taxes was not a "tax," and thus, payment was not subject to

State Constitution's tax requirements. Purpose of payment was to offset the burden created by property tax exemption in order to compensate county for services that tribal exempt land required, payment was essentially reimbursement or prospective payment for municipal services rendered, and payment was made because of municipal services the land received, as evidenced by negotiation process between tribe and county.

TAX - CONNECTICUT

[Nutmeg Housing Development Corporation v. Town of Colchester]

Supreme Court of Connecticut - December 27, 2016 - A.3d - 324 Conn. 1 - 2016 WL 7374650

Taxpayer sought judicial review of decision of town's board of assessment appeals upholding town's valuation, for property tax purposes, of taxpayer's land, on which age and income restricted apartment complex was located.

The Superior Court rendered judgment for town. Taxpayer appealed.

On transfer from the Appellate Court, the Supreme Court of Connecticut held that:

- Clear error standard governed review, and
- Taxpayer failed to demonstrate aggrievement, as initial burden in obtaining relief from town's valuation.

Supreme Court would review under the deferential clear error standard the trial court's decision rejecting taxpayer's challenge to town's valuation of taxpayer's land for property tax purposes, where trial court's rejection of taxpayer's valuation was based on court's credibility determination in light of flaws it perceived in the data used by taxpayer's appraiser, rather than a determination as to the proper standards governing the valuation.

Taxpayer failed to demonstrate aggrievement, as initial burden in obtaining relief from town's valuation, for property tax purposes, of taxpayer's parcel, on which age and income restricted apartment complex was located. Valuation of taxpayer's appraiser relied on unrestricted market properties to determine reasonable income and expense figures, town's appraiser testified that adjustments were required given the age and income restrictions, and taxpayer provided no testimony to support its calculation under statute providing capitalized value of net rental income as basis for property valuation.

TAX - VIRGINIA

[Western Refining Yorktown, Inc. v. County of York]

Supreme Court of Virginia - December 15, 2016 - S.E.2d - 2016 WL 7242276

Taxpayer challenged county's valuation of refinery's machinery and tools for purposes of levying machinery and tools tax.

The Circuit Court upheld valuation. Taxpayer appealed.

The Supreme Court of Virginia held that:

- Evidence supported finding that tax assessor did not overvalue refinery's machinery and tools by valuing them at a static 25% of original cost;
- County commissioner of the revenue adequately considered appraisal submitted by taxpayer's expert;
- Evidence supported finding that commissioner adequately considered market conditions; and
- County did not impermissibly assume inconsistent positions by arriving at higher value of machinery and tools than value it had determined for refinery in separate real estate litigation.

Evidence supported finding that tax assessor did not overvalue refinery's machinery and tools by valuing them at a static 25% of original cost, regardless of age or value, in levying machinery and tools tax. Legislature had authorized assessment of machinery and tools based on percentage of original cost, county commissioner of the revenue testified that methodology tended to approximate fair market value over time, refinery was regularly upgraded and maintained, and taxpayer's need for cash could have had dampening effect on price of sale of refinery that occurred shortly after relevant period.

In assessing refinery's machinery and tools when levying machinery and tools tax, county commissioner of the revenue adequately considered appraisal submitted by taxpayer's expert. Record established that commissioner reviewed appraisal and conducted additional research to determine whether it was well-founded, commissioner issued detailed written explanation for why she rejected expert's appraisal, and commissioner concluded that cost approach would yield unknown result due to lack of information about cost to restart refinery.

Evidence supported finding that county commissioner of the revenue, in levying machinery and tools tax, adequately considered market conditions in valuing refinery's machinery and tools. Taxpayer had told its shareholders through securities filings and state through tax returns that refinery was worth a great deal more than commissioner's assessment, and taxpayer made a business decision to sell refinery at low value due at least in part to its need for cash and to gain tax advantage.

In levying machinery and tools tax on refinery, county did not impermissibly assume inconsistent positions by arriving at higher value of machinery and tools than value it had determined for refinery in separate real estate litigation. Expert had no occasion to value machinery and tools in real estate litigation and had expressly stated that he was valuing real property only, there was evidence that equipment could have been returned to use when market conditions improved and that equipment did not have "salvage" value only, and taxpayer had sold refinery when it found itself short of cash and decided to sell refinery when entire refining industry was in slump.

Muni Investors: Beware Of The De Minimis Tax Rule.

- The recent rise in interest rates has exposed certain municipal bonds priced at a market discount to the de minimis tax rule.
- This rule causes the accretion of the bond discount to be taxed at the marginal income tax rate.
- Muni investors unaware of the de minimis rule could buy a bond at a seemingly attractive yield to later find out the effective yield is much lower.

The recent rise in interest rates has created a situation where tax-exempt municipal bonds trading at a discount could be subject to what is known as the "de minimis" tax rule. The rule applies to bonds purchased at a market discount below a threshold determined by the IRS.

This is a problem because most investors choose municipal bonds for tax-free income. Giving up a portion of your return to the IRS is not something any investor wants to do.

Your broker or bond salesman should advise you if a bond you are considering purchasing or selling qualifies for the de minimis tax. Don't rely on your broker. Become an informed investor by learning about the rule for yourself.

Continue reading.

Seeking Alpha

Joshua Hudson, CFA

Jan. 1.17

TAX - WISCONSIN

Regency West Apartments LLC v. City of Racine

Supreme Court of Wisconsin - December 22, 2016 - N.W.2d - 2016 WL 7407487 - 2016 WI 99

Owner of apartment complex subject to low income housing tax credits brought actions against city to recover refunds from claimed excessive taxation.

The Circuit Court dismissed the claims. Owner appealed, and the Court of Appeals affirmed. The Supreme Court granted owner's petition for review.

The Supreme Court of Wisconsin held that:

- Income approach required calculation of net operating income based on income and expenses specifically projected for the complex;
- Appraiser could not derive the capitalization rate from market-rate properties;
- Sales of three properties were not "reasonably comparable" arms-length sales as required for assessor to rely on the sales when assessing apartment complex; and
- Evidence was sufficient to meet burden of showing that city's assessed value of $4,169,000 was excessive.

Using best information available, income approach to valuing apartment complex property required calculation of net operating income based on income and expenses specifically projected for the subject property, rather than calculation of net operating income through mass appraisal techniques.

An appraiser must not value federally regulated housing as if it were market-rate property, as doing so causes the assessor to pretend that the subject property is not hindered by federal restrictions. The restrictions and underlying agreements implicit in federally regulated housing will affect the property's value.

Sales of three properties were not "reasonably comparable" arms-length sales as required for assessor to rely on the sales when assessing apartment complex. While subject complex was built using tax credit program, one comparable sale property was mostly market-rate rentals, while others used Section 8 rent subsidy credits, and rents at subject property were not subsidized by the government.

Apartment complex owner's evidence in tax refund action was sufficient to meet burden of showing that city's assessed value of $4,169,000 was excessive. Complex used third tier direct capitalization of income appraisal which employed actual expenses and income for the property upon which the net income was calculated, appraisal derived its capitalization rate from a market for tax credit properties, and appraisal determined that the property's value was $2,730,000.

Tax-Exempt Bonds Already Pinched by Proposed Trump Tax Cuts.

Investors pulled another $2 billion from U.S. municipal bond funds in the latest week, underscoring fears that potential sweeping tax changes under President-elect Donald Trump and a Republican Congress will undermine the tax-exempt debt market.

Trump's plans to cut taxes and increase fiscal spending have already boosted inflation expectations. As a result fixed-income markets, already weighed down by forecasts for tighter U.S. monetary policy, have see prices slump while stocks have reached record highs.

Since the Nov. 8 election, munis suffered more than any other fixed-income sector with a negative total return of 3.229 percent, according to Bank of America Merrill Lynch indices.

Trump wants to reduce the current seven tax brackets to three: 12 percent, 25 percent and 33 percent. This mirrors a June tax proposal by U.S. House Republicans but the House proposal would also allow taxpayers to deduct 50 percent of their capital gains, dividends and interest income, shrinking overall taxes even further.

"It just seems that municipals would have to readjust in terms of yield, a little bit higher yield, to bring itself back into parity proportionately with other asset classes to remain competitive," said Jim Colby, chief municipal strategist at VanEck.

Tax-exempt bonds, which outperformed other fixed-income assets in 2015, are on track to have the only negative return, albeit a small one, for all of 2016.

As of last Wednesday, munis returned a negative 0.078 percent versus positive returns of 0.551 percent for Treasuries and 5.158 percent for corporate bonds, BAML reported.

The corporate tax rate, as envisioned by Trump, would fall to 15 percent from 35 percent, making muni bonds less attractive for tax-exempt debt buyers like banks and property and casualty insurance companies.

Wealthy investors subject to federal income tax rates currently as high as 39.6 percent are traditional buyers of tax-free bonds sold by states, cities, schools, nonprofits and other issuers.

Investors are fleeing from muni bond funds. The net outflows have grown for six straight weeks to $13.5 billion since the U.S. election, according to Thomson Reuters Lipper service. The muni market is $3.7 trillion overall and until recently was the beneficiary of 54 straight weeks of fund net inflows.

DO TAX RATES MATTER TO MUNIS?

While there is talk of a tax reform bill moving through the House relatively quickly, past history indicates a vote by the August recess, setting up a Senate vote in the fall and potential signing by Trump before year-end. If progress stalls, tax reform could lay dormant during 2018's election year.

Some question the tax impact on the municipal bond market though.

Philip Fischer, municipal research strategist at BAML, said tax rates are no longer the driving force behind muni purchases and that tax-sheltered investment vehicles have replaced competition from other fixed-income assets.

“What is going on is that munis have to yield enough so they are competitive with other tax sheltered instruments like 401k’s,” he said.

The tax-exempt market should have some time to adjust before the first major U.S. tax changes materialize since 1986’s massive reform law.

“We really believe if it really does happen it’s more of a 2018 event not a 2017,” said Dan Heckman, national investment consultant at US Bank.

Meanwhile, muni issuers are facing higher borrowing costs than just six months ago.

A rise in yields on Municipal Market Data’s benchmark triple-A scale from record lows reached this summer accelerated after the election.

The yield on top-rated 30-year bonds ended Friday at 3.11 percent, which is 118 basis points up from its 1.93 percent low. For 10-year bonds, Friday’s 2.39 percent yield was 110 basis points over the all-time low of 1.29 percent.

Issuers took advantage of historic low rates to refund old debt and sell new bonds, pushing 2016 issuance to $423.5 billion as of Friday, just short of 2010’s record $430.35 billion supply, according to Thomson Reuters data.

“We could envision a market totaling $350 billion (in 2017), about $100 billion less than this year, but this of course depends heavily on how the proposals play out,” Natalie Cohen, a senior analyst at Wells Fargo, said in a December report on potential tax changes.

Refundings of existing bonds, which accounted for about 61 percent of 2016 issuance, would not screech to a halt given the impending 10-year call on hefty amounts of debt issued in 2007, she added.

Reuters

By Karen Pierog

Tue Dec 27, 2016 | 7:00am EST

(Reporting By Karen Pierog, additional reporting by David Morgan in Washington; Editing by Daniel Bases)

[IRS Issus New Guidance On The Beginning Of Construction Safe Harbor For Renewable Energy Projects: Foley & Lardner]

The IRS recently issued Notice 2017-4 (the “Notice”) which makes two important changes to its “beginning of construction” rules for taxpayers seeking to take advantage of the section 45 renewable electricity production tax credit (PTC) for wind and other renewable energy facilities including geothermal, biomass, landfill gas and certain hydropower and marine hydrokinetic energy projects. Under prior IRS guidance, including Notice 2016-31 discussed in our blog post here, taxpayers have two ways to establish that they started construction. They can either show that they began physical construction of a significant nature (the “Physical Work Test”), or incurred at least 5% of the total cost of the eligible facility (the “5% Safe Harbor”). However, once construction has begun or cost have been paid or incurred, the IRS requires taxpayers to make continuous progress towards completion to satisfy both the Physical Work Test and the 5% Safe Harbor (“Continuous Construction Requirement”). Taxpayers are deemed to satisfy the Continuous Construction Test provided they began construction on the facility prior to January 1, 2015, and place it in service prior to January 1, 2017 (the “Continuity Safe Harbor”).

The Notice now permits taxpayers to fall within the Continuity Safe Harbor provided that they place the facility in service by the later of (1) a calendar year that is no more than four calendar years after the construction of the facility began or (2) December 31, 2018. This provides additional time for developers that have satisfied the Physical Work Test or 5% Safe Harbor to complete construction and place the facility in service without having to demonstrate that the Continuous Construction Requirement was satisfied. For example, if construction begins on January 15, 2013, and the facility is placed in service by December 31, 2018, the facility will meet the Continuity Safe Harbor.

The Notice also provides that the prohibition on taxpayers using both the Physical Work Test and 5% Safe Harbor methods in alternating years to push forward the facility’s placed in service deadline does not apply to taxpayers that began construction on a project under either test prior to June 6, 2016. (The date that Notice 2016-31, which established this rule, was published.) Accordingly, taxpayers that began construction before this deadline can show that they have made continuous progress towards construction by relying on the Physical Work Test in one year and then relying on the 5% Safe Harbor the following year after they have paid enough costs to meet the 5% threshold. This is helpful because taxpayers acquiring projects may not have been satisfied with the manner in which the prior developer demonstrated the commencement of construction. The new rule permits them to “requalify” the project under a different method.

Last, the Notice provides guidance for developers using the 5% Safe Harbor for repowering and retrofitting existing projects. In order to take advantage of the tax credit, the facility must be “new” as determined by the 80/20 rule, which means that the cost of new parts must be four times the value of the used parts. The Notice clarifies that for purposes of satisfying the 5% Safe Harbor, the cost of the new property includes all costs properly included in depreciable basis, meaning that indirect costs that are allocated to the new property’s depreciable basis should count towards the 5% Safe Harbor.

Last Updated: December 28 2016

Article by John A. Eliason, David B. Weisblat and Kurt R. Rempe

Foley & Lardner

The New Issue Price Regulations – "Bought Deals," Bored Bidders, and Other Problems.

As you have heard, and as we noted last week, Treasury and the IRS recently released final regulations that tell issuers how to calculate the "issue price" of tax-advantaged bonds that are issued for money. The regulations don't take effect until June 7, 2017, so we can spend some time luxuriating in their nuances and preparing for the new order of things until the appointed hour arrives. As ever, though the new regulations seem to carve out some discrete rules, interesting [sic] questions lurk in the margins.

Continue reading.

By Johnny Hutchinson on December 22, 2016

The Public Finance Tax Blog

Squire Patton Boggs

TAX - CALIFORNIA

In re Transient Occupancy Tax Cases

Supreme Court of California, California - December 12, 2016 - P.3d - 2016 WL 7187624

Online travel companies petitioned for writ of mandate challenging city's determination that companies were responsible for paying transient occupancy tax on their service fees.

The Superior Court granted writ of mandate. City appealed, and the Court of Appeal affirmed. The Supreme Court granted review, superseding the opinion of the Court of Appeal.

The Supreme Court of California held that tax was not payable on amounts retained by travel companies above the amounts remitted to hotels as the agreed wholesale costs of room rentals plus the hotel-determined markup.

City transient occupancy tax, which was charged as percentage "of the Rent charged by the Operator," was not payable on amounts retained by online travel companies above the amounts remitted to hotels as the agreed wholesale costs of room rentals plus the hotel-determined markup. Travel companies were not "operators" under the ordinance and did not act as agents for purposes of setting and collecting additional markups from room occupants, and contractual provisions between hotels and travel companies apportioning tax responsibility did not create tax liability.

MBFA: Sign Our Letter to Save the Muni-Exemption.

Municipal Bonds For America will be sending a letter to all House and Senate Leadership, House Ways & Means and Senate Finance Committee Members urging them to retain current law on municipal bonds as a part of their upcoming legislative debate.

The letter was intentionally drafted to be short and simply focuses on urging Members to oppose any efforts to limit or repeal the exemption.

The intent of the letter is not to get Members to focus on its content, but to get them to focus on who signed the letter from their state or district.

MBFA's goal is to collect a minimum of 300 signatures for this letter.

We strongly encourage each of you and your organizations to immediately take the following action:

1. Obtain sign-off from your parent organization to have your organization's name affixed to the letter–and follow the instructions (below) to make that happen.
2. Alert your organization's individual members regarding the opportunity to join with other like-minded organizations in supporting municipal bonds. MBFA wants to include the signatures from as many airports, hospitals, education entities, transportation authorities, mayors, broker/dealers, construction companies, and all others as signatures to this letter.
3. To view and add your signature to the letter please click here.

The deadline for affixing your signature to this letter is Thursday, January 19, 2017.

Thanks for your help. If you have any questions please feel free to reach out to Justin Underwood at justin@munibondsforamerica.org.

For more information on the MBFA please visit www.munibondsforamerica.org

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Help GFOA Preserve Muni Bond Tax Exemption.

On Wednesday, December 14th and Thursday December 15th select members of Ways and Means will convene to discuss the Blueprint for Tax Reform, a legislative proposal for comprehensive tax reform that will be introduced in the 115th Congress that begins in January.

In order to achieve Chairman Brady's overall objectives to simplify the tax code, all tax exemptions are at risk, with the exception of the mortgage interest deduction and the deduction for charitable donations.

The Federal Liaison Center is still not certain about the specific contents of the Blueprint, but we would like to be sure that the tax exemption on municipal bond interest is not at risk.

Now is the time for GFOA members to engage your member of Congress to explain how the municipal bond underpins our infrastructure and drives our local economies. Reach out today and tell them:

- Tax-exempt bonds are the primary financing mechanism for state and local infrastructure projects—they have been used for more than 100 years and provide essential funding for states, counties and localities.
- Three-quarters of all public infrastructure projects in the U.S. are built by states and localities, and tax-exempt bonds are the primary financing tool utilized to satisfy these infrastructure needs.
- If the tax exemption is eliminated or reduced, states and localities will pay more to finance projects, leading to fewer projects and fewer jobs, or project costs will be transferred to local tax and rate payers.
- ***Describe to them specific projects in their districts that municipal bonds have built!***

Reaching out to your members of Congress and describing how the muni bond has been used to provide essential infrastructure in your jurisdiction is now more important than ever. Please feel free to access materials and to stay in touch during this hectic and exciting time via the FLC's [Federal Tax Exemption on Municipal Bond Interest Resource Center].

[Local Governments Suffer Tax Blow at California Supreme Court.]

In a loss for local governments, the California Supreme Court decided Monday that online travel companies such as Expedia Inc. are exempt from paying hotel occupancy taxes.

The ruling came in one of several lawsuits filed by California cities and counties against the online firms, including Hotwire Inc. and Priceline.com.

The local governments have been attempting to get the firms to pay hundreds of millions of dollars in back taxes.

Lawyers for the government argued the tax should be based on the total amount the companies collect from consumers, not the lower dollar figure the hotels receive. Cities and counties wanted the online sites to pay the difference.

The state high court agreed the tax should be based on the higher amount but said the online companies were not obligated to pay it.

"It changes the rules in California," said Kent L. Richland, who represented the city of San Diego in the case decided Monday. "It is going to affect all these cases because they are going to have to be decided under new rules."

Several cities and counties still have cases pending, including a lawsuit by Los Angeles.

So far, the online travel firms have won most of the disputes, which have been litigated across the country.

California's top court, examining a San Diego transient occupancy ordinance, said it applied only to hotel operators, not the online businesses.

Online travel companies "are not operators," the court said in a unanimous decision written by Justice Kathryn Mickle Werdegar.

San Diego sued the companies in an attempt to recover about $21 million in back taxes.

Hotels contract with online sites to provide rooms at discounted rates. The sites charge a higher rate and require consumers to pay a charge for taxes and fees.

Hotels have been paying occupancy taxes based on the amounts they received for their rooms, not the higher price paid by consumers to the travel firms

Industry officials say online travel companies typically mark up the wholesale price by 8% to as high as 22%, but there is no standard for this.

Local governments may still be able to recover the additional tax revenue by suing hotels, which were not a party in Monday's case.

If hotels are sued, the Internet firms could end up footing the bill anyway, Richland said.

Most hotels have contracts that obligate online travel companies to compensate them for any taxes eventually owed, Richland said.

San Diego has not yet decided what to do to next, he said.

A spokesman for the California Hotel and Lodging Assn., a trade group for the state's hotels and inns, said the good news is that the ruling calls on online travel companies to pay taxes based on the rate they charge guests, not on the wholesale price charged to them by the hotels.

But it also means that hotel owners will be responsible for finding out from the online travel companies how much they marked up the rooms and collect tax on that higher rate. "It means more work on the part of the hotels," said Lynn Mohrfeld, president and chief executive for the trade group.

In order to change city laws to make online travel companies pay taxes on the total charged to guests, Mohrfeld said an ordinance must be placed before voters and approved by a two-thirds majority.

"Getting a two-thirds majority is an awfully tall order," he said.

The Travel Technology Assn, the trade group that represents online travel companies such as Expedia and Orbitz, declined to comment on the court ruling.

BY TRIBUNE NEWS SERVICE | DECEMBER 13, 2016

By Maura Dolan

IRS Releases Final Issue Price Regulations with Significant Changes: Andrews Kurth

On December 9, 2016, the Internal Revenue Service (the "IRS") released final regulations regarding issue price for tax-exempt obligations (the "Final Regulations") that will be effective for bonds sold on or after June 7, 2017.

Summary of Current Law

The Existing Regulations define issue price generally as the first price at which ten percent of the bonds of any maturity is sold to the public. The Existing Regulations further provide that the issue price of bonds for which a bona fide public offering is made may be determined as of the sale date based on reasonable expectations regarding the initial public offering price. Most bond counsel now interpret this rule to permit issuers to determine the issue price of any maturity of bonds for which at least 10% was not sold to the public based on a certificate of the underwriters regarding their reasonable expectations on the sale date.

Summary of Final Regulations

The Final Regulations provide three options for determining issue price: the general actual facts rule, a special reasonable expectations rule, and a special rule for competitive sales. Underwriters will be required to provide certain certifications in order to fall under the special reasonable expectations rule and special rule for competitive sales. An issuer may use its discretion to select among the rules and may select a different rule for different maturities of the same issue, but must identify the rules selected in its books and records on or before the issue date of the bonds.

1. General Rule (Actual Facts Test)

A. Public Offerings

The Final Regulations provide that generally the issue price of bonds issued for money is the first price at which a substantial amount (ten percent) of the bonds is sold to the public.

B. Private Placements

For a bond issued for money in a private placement to a single buyer that is not an underwriter or a related party to an underwriter, the issue price of the bond is the price paid by that buyer.

2. Special Reasonable Expectations Rule (Hold-the-Offering Price Rule)
In addition to the general rule, an issuer may treat the initial offering price to the public as the issue price of the bonds if:

A. The underwriters offered the bonds to the public at a specified initial offering price on or before the sale date, and the lead underwriter in the underwriting syndicate or selling group (or, if applicable, the sole underwriter) provides, on or before the issue date, a certification to that effect to the issuer, together with reasonable supporting documentation for that certification, such as a copy of the pricing wire or equivalent communication; and

B. Each underwriter agrees in writing that it will neither offer nor sell the bonds to any person at a price that is higher than the initial offering price to the public during the period starting on the sale date and ending on the earlier of (1) the close of the fifth (5th) business day after the sale date, or (2) the date on which the underwriters have sold at least 10% of the bonds of that maturity to the public at a price that is no higher than the initial offering price to the public of that maturity. Sales of bonds to anyone at a price that is lower (rather than higher) than the initial offering price to the public during the holding period are allowed.

We expect the certifications required in (B) will be included in bond purchase agreements and any agreements among underwriters for bonds sold after the Final Regulations take effect on June 7, 2017.

3. Special Rule for Competitive Sales

For bonds issued for money pursuant to an eligible competitive sale, an issuer may treat the reasonably expected initial offering price to the public as of the sale date as the issue price of the bonds if the issuer obtains a certification from the winning bidder regarding the reasonably expected initial offering price to the public of the bonds upon which the price in the winning bid is based.

For purposes of this special rule, the Final Regulations define “competitive sale” to mean a sale of bonds by an issuer to an underwriter that is the winning bidder in a bidding process in which the issuer offers the bonds for sale to underwriters at specified written terms and that meets the following requirements:

A. The issuer disseminates the notice of sale to potential underwriters in a manner reasonably designed to reach potential underwriters;

B. All bidders have an equal opportunity to bid;

C. The issuer receives bids from at least three underwriters of municipal bonds who have established industry reputations for underwriting new issuances of municipal bonds; and

D. The issuer awards the sale to the bidder who offers the highest price (or lowest interest cost).

4. Definitions

"Public" is defined for purposes of determining the issue price of tax-exempt bonds to mean any person other than an underwriter or a related party to an underwriter.

"Underwriter" is defined to mean:

A. Any person that agrees to participate in the initial sale of the bonds to the public by entering into a contract with the issuer or with a lead underwriter to form an underwriting syndicate; and

B. Any person that, on or before the sale date, directly or indirectly enters into a contract with any of the foregoing to sell the bonds.

5. Standard for Reliance on Certifications and Consequences of Violations

The Existing Regulations treat an issuer's expectations or actions as reasonable only if a prudent person in the same circumstances as the issuer would have those same expectations or take those same actions, based on all the objective facts and circumstances. The Preamble to the Final Regulations states that the existing due diligence standard under the Existing Regulations will apply to any certificate under the Final Regulations and that a certificate from the underwriter of the first price at which 10% of a maturity of bonds were sold to the public is an example of reasonable supporting documentation for establishing the issue price of the bonds of any maturity under the general rule in the Final Regulations.

If the issuer selects a rule for determining issue price but a specific eligibility requirement of that rule is not met, issue price may not be determined under that rule and a redetermination of issue price under a different rule will occur. An example of failing to meet a specific eligibility requirement is an underwriter's breach of its hold-the-offering-price agreement under the special reasonable expectations rule.

A false statement by an underwriter in a certification or in the agreement among underwriters under one of these special rules may result in a penalty against the underwriter under section 6700, depending on the facts and circumstances.

Effective Date

These regulations are effective for bonds sold on or after June 7, 2017.

History of Issue Price Regulations

On June 18, 1993, the Department of the Treasury (Treasury Department) and the IRS published comprehensive final regulations in the Federal Register (TD 8476, 58 FR 33510) on the arbitrage investment restrictions and related provisions for tax-exempt bonds under sections 103, 148, 149, and 150. Since that time, those final regulations have been amended in various limited respects, including most recently in final regulations published in the Federal Register (TD 9777, 81 FR 46582) on July 18, 2016 (the regulations issued in 1993 and the various amendments thereto are collectively referred to as the Existing Regulations).

A notice of proposed rulemaking was published in the Federal Register (78 FR 56842; REG-14865--07) on September 16, 2013 (the 2013 Proposed Regulations), which, among other things, proposed to amend the definition of "issue price."

Subsequently, the Treasury Department and the IRS withdrew §1.148-1(f) of the 2013 Proposed Regulations regarding the definition of issue price and published another notice of proposed rulemaking in the Federal Register (80 FR 36301; REG-138526-14) on June 24, 2015, which re-proposed a definition of issue price (the 2015 Proposed Regulations).

National Law Review

by Cathleen Chang, Robert M. Collie, Jr., Gregg Jones, Barbara Jane League

Andrews Kurth Kenyon Law Firm

Tuesday, December 13, 2016

Final Issue Price Regulations Issued: Squire Patton Boggs

The Treasury Department issued final "issue price" regulations on December 9, 2016 (T.D. 9801) (the "Issue Price Regulations"). Below is a summary of the general and special rules for determining issue price under the Issue Price Regulations:

- General Rule. The general rule, retained from the existing regulations, provides that issue price is determined by actual sales to the public of 10% of those bonds having the same credit and payment terms (generally, each maturity of an issue).
- "Hold the Price" Bonds. For bonds offered to the public, issue price may instead be determined based on a certification from the underwriter, accompanied by supporting documentation such as a copy of the pricing wire, that states the price at which the bonds were initially offered to the public. However, the underwriter or underwriters must each agree not to sell the bonds at a higher price until the earlier of more than five business days after the sale date or 10% of the bonds have been sold to the public.
- Competitive Sales. For bonds that have been sold in a competitive bidding process meeting specified requirements, including that at least three bids are received, the issuer may rely upon the reasonably expected initial offering price that is certified by the winning bidder.
- Private Placements. For private placements to a single buyer, the issue price is the actual price paid by the buyer.

If more than one issue price rule could apply, the issuer may select which rule to apply but must do so on or before the issue date. Read below for additional information regarding the Issue Price Regulation.

The Issue Price Regulation also adds and modifies definitions:

- "Public" now means any person other than an underwriter or a related person. Under the existing regulations, the term public did not include "bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters or wholesalers."

- "Underwriter" means (1) any person who participates in the initial sale of bonds to the public pursuant to a written contract with the issuer (or with a lead underwriter) and (2) any person that participates in the initial sale to the public pursuant to a written agreement with a person described in the former clause (for instance, pursuant to a retail distribution agreement).

As discussed on this blog (here, and more light-heartedly, here), the Treasury has previously issued proposed regulations that were not well received. The preamble to the Issue Price Regulation notes that "overwhelmingly negative comments" were received regarding parts of the proposed regulations. In response to comments, various changes were made by Treasury (for example, the private placement rule was added, and an issuer may select which rule to apply.)

The Issue Price Regulations apply to bonds sold to the public on or after June 7, 2017, provided of course that Congress does not take action under the Congressional Review Act or otherwise.

The Public Finance Tax Blog

By Alexios Hadji on December 16, 2016

Squire Patton Boggs

Final Issue Price Regulations Significantly Change Current Rules.

On Dec. 9, the IRS released final Treasury Regulations (the "Final Regulations") relating to the "issue price" of tax-exempt bonds for purposes of arbitrage investment restrictions. Although on balance an improvement to the proposed Treasury Regulations released in 2015, the Final Regulations represent a departure from the current Treasury Regulations (the "Current Regulations") and will affect long-held practices regarding the documentation of issue price. As such, issuers, underwriters, financial advisors and others involved in the municipal bond market will need to determine how they will comply with the Final Regulations, which are effective for bonds sold on or after June 7, 2017.

Set forth below is a general summary of pertinent provisions of the Final Regulations.

Actual Sales Test Adopted for Publicly Offered Bonds
Unless the issuer elects to use one of the two "special rules" for determining issue price, the issue price of bonds that are publicly offered is the first price at which a substantial amount (i.e.,10%) of the bonds is sold to the public. However, unlike the Current Regulations, which allow the issue price to be determined as of the sale date based on reasonable expectations regarding the initial public offering price, the Final Regulations provide that the "issue price of bonds issued for money is the first price at which a substantial amount [defined as 10%] of the bonds is sold to the public." Thus, the Final Regulations adopt an actual sales test to determine issue price for publicly offered bonds, a significant change from the Current Regulations.

Special Rule for Use of Initial Offering Price to the Public
As an alternative to the "actual sales" test, the Final Regulations include a "special rule" for determining the issue price of publicly offered bonds, pursuant to which an issuer may treat the initial offering price to the public as of the sale date as the issue price of the bonds if the following

requirements are met:

- The underwriters offered the bonds to the public for purchase at a specified initial offering price on or before the sale date, and the lead underwriter in the underwriting syndicate or selling group (of, if applicable, the sole underwriter) provides, on or before the issue date, a certificate to that effect to the issuer, together with reasonable supporting documentation for that certification, such as a copy of the pricing wire or equivalent communication; and
- Each member of the underwriting syndicate agrees in writing that it will neither offer nor sell the bonds to any person at a price that is higher than the initial offering price to the public during the period starting on the sale date and ending on the earlier of (i) the close of the 5th business day after the sale date or (ii) the date on which the underwriters have sold a substantial amount (i.e., 10%) of the bonds to the public at a price that is no higher than the initial offering price to the public.

Special Rule for Competitive Sales
Recognizing that competitive sales inherently "favor competition and price transparency that may result in better pricing for issuers," the Final Regulations include a special rule for competitive sales. Specifically, the Final Regulations provide that, for bonds issued in an eligible competitive sale, the issue price is the price produced based on the winning bid and requires the winning bidder to provide an appropriate certification regarding the reasonably expected initial offering prices of the bonds.

An eligible "competitive sale" is a sale of bonds by an issuer to an underwriter that is the winning bidder in a bidding process in which the issuer offers the bonds for sale to the underwriters pursuant to specified written terms and that meets the following requirements:

- The issuer disseminates the notice of sale to potential underwriters in a manner reasonably designed to reach potential underwriters;
- All bidders have an equal opportunity to bid;
- The issuer receives bids from at least three underwriters of municipal bonds who have established industry reputations for underwriting new issuances of municipal bonds; and
- The issuer awards the sale to the bidder who offers the highest price (or lowest interest cost).

Issue Price in Private Placements
The Final Regulations expressly provide that, for a bond issued for money in a private placement to a single buyer that is not an underwriter or a related party to an underwriter, the issue price of the bond is the price paid by the buyer.

Determining Issue Price when More than One Rule is Available
The Final Regulations include more than one way to determine issue price (i.e., the general rule, the special rule, and the competitive bid rule). Accordingly, the Final Regulations provide that for bonds for which more than one rule for determining issue price is available, an issuer may select the rule it will use to determine the issue price at any time on or before the issue date of the bonds by identifying the selected rule in the books and records maintained for the bonds.

Definition of Underwriter
The Final Regulations define "underwriter" to mean (i) any person that agrees pursuant to a written contract with the issuer (or with the lead underwriter to form an underwriting syndicate) to participate in the initial sale of the bonds to the public and (ii) any person that agrees pursuant to a written contract directly or indirectly with a person described in (i) to participate in the initial sale of the bonds to the public (for example, a retail distribution agreement between a national lead underwriter and a regional firm under which the regional firm participates in the initial sale of the

bonds to the public).

Conclusion
Although it is too soon to tell exactly how the Final Regulations will affect the way in which issuers, underwriters, financial advisors and others approach issuances of tax-exempt bonds, the Final Regulations will affect the way that issue price is established and documented and may have other ancillary effects on the municipal bond market. Market participants should review the Final Regulations carefully and consult their advisors, as appropriate.

The Bond Buyer

By Victoria Ozimek and Brian Teaff

December 14, 2016

Victoria Ozimek is a member of Bracewell LLP's Public Finance practice in Austin, and Brian Teaf is a member of its Public Finance practice in Houston.

Charles L. Almond, Stephen H. Gerdes and Todd Greenwalt, members of Bracewell Public Finance practice in Houston, contributed to this article.

Mayors Startled When Trump Promises to Keep Tax-Exempt Bonds.

Tax exemptions on municipal bonds are hardly the sexiest political issue surrounding Donald Trump's transition. But a group of mayors, meeting with the president-elect at Trump Tower on Thursday, were surprised with welcome news when they pressed Trump to keep the exemptions.

"He's the president-elect, and he said he would keep it," said Tom Cochran, the CEO and executive director of the U.S. Conference of Mayors. "My lobbyist has been up on the Hill, and they said to us everything is on the table. We didn't know what would happen."

He added: "As soon as the sun comes up, I will be contacting the authorities in Speaker Ryan's office and others on the Democratic side that we were encouraged by the president-elect."

A spokesman for Trump, who convened the mayors in Trump Tower for about 30 minutes, didn't respond to a request for comment. Trump has vowed to overhaul the country's tax code when taking office, and mayors have feared the exemption could be in jeopardy. It has been targeted by some Republicans as too pricey, particularly when the bonds are used to build sports arenas and stadiums.

In a 2009 report, the Congressional Budget Office called the tax-exempt bonds a "costly mechanism." A 2015 report from the Joint Committee on Taxation said the tax-exempt bonds will cost the government more than $180 billion between that year and 2019.

The exemptions are vitally important to mayors, they say, because they enable cities and counties to build roads, schools and other projects without paying the burden of taxes on the borrowing. Between 2003 and 2012, states and local governments financed $3.2 trillion in projects, according to the National Association of Counties. Trump seemed to understand that and emphasized how committed he was to spending money on infrastructure, the mayors said.

Two other mayors in the room said they were also surprised with Trump's declaration. "I didn't necessarily think we'd hear an opinion back," said Mick Cornett, the Republican mayor of Oklahoma City. "I was very encouraged."

"He definitely said he would keep the exemptions," said Steve Benjamin, the Democratic mayor of Columbia, S.C. A spokesman for New Orleans Mayor Mitch Landrieu, a Democrat also present at the meeting, said he wasn't available for comment.

The U.S. Conference of Mayors, had struggled to secure Trump's attention during the presidential race. And a number of liberal mayors have vowed to oppose many of Trump's proposals, like on immigration.

On Thursday the mayors present said he seemed interested in attending their next meeting and sending members of his Cabinet.

The mayors said they discussed a number of other municipal issues, like community block grants for cities. Trump seemed interested in how cities received money, the mayors said, and how they spent it.

Benjamin said that while he vociferously opposed Trump's candidacy, he was trying to be "optimistic" after the meeting. Cornett said "because Trump has lived in cities, I think he has a good understanding."

"You didn't know what to expect going in," Cochran, the CEO and executive director said. "We're in uncharted waters with this president-elect. We felt like that he was listening to us. We're trying to get to know him. He's the president. We got to get to know him."

POLITICO

By JOSH DAWSEY

12/15/16 07:21 PM EST

TAX - NEW HAMPSHIRE

Bishop of Protestant Episcopal Diocese in New Hampshire v. Town of Durham

Supreme Court of New Hampshire - December 9, 2016 - A.3d - 2016 WL 7177763

Church appealed town's assessment of property tax on 24 spaces in church parking lot that church leased to state university students.

The Superior Court entered summary judgment for town, and church appealed.

The Supreme Court of New Hampshire held that spaces in church's parking lot leased to state university students were not exempt from property tax.

Spaces in church's parking lot leased to state university students were not "used and occupied directly for religious purposes," within meaning of statutory exemption from property tax for "houses of public worship, buildings, and the lands appertaining to them owned, used and occupied directly for religious training or for other religious purposes by any regularly recognized and constituted denomination." University students were using parking spaces for their own private and secular purposes, i.e., parking for about six hours each week, plus special event days and during snow plowing and repair operations, and church did not argue that leasing spaces to university students was reasonably necessary to carry out its mission.

TAX - LOUISIANA

[Arrow Aviation Company, LLC v. St. Martin Parish School Board Tax Sales Dept.]

Supreme Court of Louisiana - December 6, 2016 - So.3d ----2016 WL 7118912 - 2016-1132 (La. 12/6/16)

Taxpayer petitioned to recover amount of sales and use tax paid under protest, claiming collector failed to apply a legislative tax exclusion.

The 16th Judicial District Court, St. Martin Parish, ruled in favor of the collector, finding the exclusion to be unconstitutional. Taxpayer appealed

The Supreme Court of Louisiana held that:

- A legislative tax exclusion must treat all local governmental subdivisions, school boards, and other political subdivisions the same, otherwise it is prohibited by the constitution's uniformity provision, abrogating *Anthony Crane Rental, L.P. v. Fruge*, 833 So.2d 1070;
- State constitution's uniformity provision did not act to compel statewide local tax authorities to apply a permissive tax exclusion adopted by a different local tax authority;
- Statutory exclusion from state and local sales tax, of charges for repairs to tangible personal property that was delivered to customers out of state, was constitutional as applied to taxpayer for audit periods during which the exclusion could be applied by tax authorities in all parishes in the same form, manner, or degree; but
- The exclusion was unconstitutional as applied for audit periods during which the exclusion was mandatory for tax authorities in one particular parish, but optional for tax authorities in all other parishes; and
- Unconstitutional portion of the statute would be severed and removed.

State constitution's uniformity provision placed a limitation on the legislature, rather than on local tax authorities, and therefore, did not act to compel statewide local tax authorities to apply a permissive tax exclusion from sales and use taxes adopted by a different local tax authority, as permitting one local tax authority to direct the actions of another would undermine each authority's power to tax.

Statutory exclusion from state and local sales tax, of charges for repairs to tangible personal property that was delivered to customers out of state, was constitutional as applied to taxpayer for audit periods during which the exclusion could be applied by tax authorities in all parishes in the same form, manner, or degree.

Statutory exclusion from state and local sales tax, of charges for repairs to tangible personal property that was delivered to customers out of state, was unconstitutional as applied for audit periods during which the exclusion was mandatory for tax authorities in one particular parish, but optional for tax authorities in all other parishes, as an example of non-uniformity prohibited by the constitution.

Unconstitutional portion of statute mandating tax authorities in one parish apply tax exclusion from state and local sales tax, of charges for repairs to tangible personal property that was delivered to customers out of state, would be severed and removed. Because earlier versions of the exclusion did not mandate that only one parish apply the exclusion, the purpose of the statute was not dependent on the unconstitutional portion.

With Trump's Support, Muni Exemption Advocates Take Battle to Congress.

WASHINGTON – U.S. mayors and other municipal market participants are stepping up pressure on Congress to maintain the tax exemption on municipal bonds, after President-elect Donald Trump said he supports the tax break that they say is crucial for funding infrastructure projects.

Mike Belarmino, associate legislative director and associate general counsel for the National Association of Counties, said although the group is “highly encouraged” by Trump’s statement, it will now focus its efforts on making sure lawmakers also recognize the importance of the muni exemption.

“We will remain vigilant and stay focused on protecting the tax exemption as a top priority for counties, because it will take a combined effort of the administration and the U.S. Congress to achieve any comprehensive tax reform,” Belarmino said.

Jessica Giroux, general counsel and managing director of federal regulatory policy for Bond Dealers of America, called Trump’s support of the muni exemption an “encouraging development” that she said comes as a result of the lobbying and education BDA and other organizations have been engaged in on the Hill. However, she added that Trump’s statements do not mean the groups’ work is done.

“We have a complicated road ahead with regard to tax reform,” Giroux said.

“Still, this is a very important public step with what the president-elect has said,” she added. “It’s extremely encouraging and we’re happy the meeting went as well as it did.”

Trump told the U.S. Conference of Mayors (USCM) during a 15-t0-20 minute conversation on his infrastructure plan on Thursday that he plans to maintain the tax-exempt standing of municipal bonds. The Republican president-elect’s 10-year infrastructure plan utilizes $137 billion of tax credits that he says will leverage $1 trillion of private investments.

Speaking to reporters at Trump Tower in New York City on Thursday, Columbia, S.C., mayor and USCM second vice president Stephen Benjamin said that Trump “was clear that his support of the tax exemption was there and that was wonderful news.” “Protecting the tax exemption on municipal bonds … is sacrosanct to us delivering on infrastructure.

“[Trump] listened to our issues and concerns and our desire to see a significant investment in infrastructure and the protection of the tax exemption of municipal bonds as a key part of that plan,” he added.

Because Trump’s tax plan still lacks details and doesn’t mention munis directly, state and local groups had expressed concern that the muni exemption could be in jeopardy.

Earlier this year, House Republicans proposed a blueprint for tax reform, which doesn’t mention munis directly, but does suggest limiting or repealing unnamed special-interest provisions.

Because roughly 75% of U.S. infrastructure has been financed using munis, Benjamin said the exemption was an "important piece" of the discussion with Trump.

"A focus on infrastructure goes hand-in-hand with a commitment to preserving the exemption on municipal bond interest," said Emily Brock, director of the Government Finance Officers Association's federal liaison center. "But our work isn't done. We will continue to work with our champions in the House and the Senate to ensure the exemption stays intact during the 115th congress, especially as discussions on tax reform proceed."

USCM has stressed the low-cost borrowing the muni exemption provides issuers as well as the $1.65 trillion in debt issued for infrastructure by state and local governments from 2003 through 2012. Opponents, meanwhile, have argued that the exemption is an inefficient method for financing infrastructure and costs the federal government in the long run.

In addition to infrastructure investment, USCM representatives discussed public safety, unfunded federal mandates and immigration priorities with Trump, according to the group.

At its bipartisan meeting earlier this fall, the mayoral organization stressed that the next president must maintain the tax exemption for municipal bonds or risk costing cities up to $500 billion in spending.

USCM is scheduled to hold its winter meeting in Washington next month, where nearly 300 mayors are expected to meet with representatives from the Trump administration.

The Bond Buyer

By Evan Fallor

December 16, 2016

Bond Market's Silver Lining Playbook: Slicing Next Year's Taxes

- Record stock market meets worst muni returns since 2013
- 'Tremendous volume' of tax-loss swaps, Breckinridge CIO says

Investors see a silver lining in the municipal-bond market rout: Tax-loss swaps.

Thanks to the technique, bondholders are selling securities that have tumbled in value and reinvesting the cash in similar, higher-yielding bonds. The losses that locks in are offsetting gains from a record-setting stock prices, cutting next year's tax bills.

"There is a tremendous volume of this going on," said David Madigan, who oversees $25 billion of municipal bonds as chief investment officer at Breckinridge Capital Advisors in Boston. "We are aggressively pursuing what we can get done."

The rush stems from a financial-market schism that's widened since Donald Trump's presidential victory last month, with his pledge to cut income taxes and boost spending on infrastructure stoking speculation that that the Federal Reserve will need to increase interest rates more rapidly.

The Dow Jones Industrial Average of stocks has risen 14 percent this year and is closing in on 20,000. Meanwhile, the prospect of higher rates caused municipal bonds to tumble in November, putting the securities on pace for the first loss since 2013. Investors who bought state and local government debt this summer — when prices reached a record high — have seen the value tumble by as much as 6.3 percent, according to Bank of America Merrill Lynch indexes.

The ability to use such losses to reduce coming tax bills are a rarity for municipal-debt investors. Before 2013, when the Federal Reserve's decision to wind down its bond-buying spree caused investors to pull out their money, the municipal market hadn't dropped since the 2008 financial crisis. The last money-losing year before that was 1999, another record-setting time for stocks.

This year, tax-loss swaps are giving investors a money-saving opportunity to adjust their portfolios before Trump takes office, said Kathleen McNamara, a municipal strategist at UBS Wealth Management in New York. The Republican's election has changed market expectations about inflation, tax policy and the trajectory of federal spending.

"There are so many factors that changed people's view on how they should be positioned," said McNamara.

To comply with Internal Revenue Service rules, investors executing tax-loss swaps need to avoid a wash sale, when securities are sold for the purpose of establishing a tax loss but the same or a "substantially identical" security is purchased 30 days before or after the sale.

Complying with the rule is easier in the municipal market, where there are more than 50,000 issuers and more than 1 million outstanding bonds.

Tax-loss swaps make the most sense for investors who bought bonds between May and August, otherwise transaction costs minimize the benefit, Breckinridge's Madigan said. He said his firm has executed $60 million tax-loss swap block trades in the last three weeks.

"It's a rare instance," Madigan said. "We had a big market rally and then in November we had a big market sell-off, so we actually have losses now that it makes sense to try to capture."

Bloomberg

by Martin Z Braun

December 16, 2016, 2:00 AM PST

The Looming Threat to Tax-Free Munis.

Donald Trump and House Republicans have proposed lower rates on taxable investment interest; such moves would lessen the advantages of munis

Thousands of municipal-bond investors have benefited from tax advantages for much of the past three decades. Pretty soon, those advantages could shrink dramatically.

That is because both President-elect Donald Trump and Republicans in the House of Representatives have proposed lower rates on taxable investment interest. Such moves would lessen the advantages of tax-free munis in ways that range from relatively minor to severely disruptive.

The most radical proposal, advanced by House Republicans led by Paul Ryan (R., Wis.) and Ways and Means Committee Chairman Kevin Brady (R., Texas), would lower the top rate on interest on taxable bonds, such as Treasurys and corporate debt, to 16.5% from 43.4%, a 62% drop.

Here is how the math works: Say an investment in a taxable bond pays annual interest of 5%. Of that interest, the government currently collects as much as 43.4 cents on every dollar. If the tax rate drops, the investor keeps more of the payout on the bond.

By comparison, tax-free municipal bonds are just that, tax-free, meaning that they don't benefit from a tax-rate cut, while taxable bonds do. This means tax-free bonds would be less desirable to investors, potentially denting prices, while demand would rise for taxable bonds.

"The math on munis is changing, and structurally the tax exemption will be less valuable—we just don't know to what degree," says Robert Gordon, who heads Twenty-First Securities, a tax-strategy firm in New York.

The smallest change, and the one with the broadest support, is repeal of a 3.8% surtax on net investment income such as interest, dividends and capital gains. This levy takes effect at a threshold of $250,000 of income for married couples and $200,000 for singles, and both Mr. Trump and many in Congress have called for its elimination.

Without this surtax, the top rate on interest from munis' taxable competition would be 39.6% rather than the current 43.4%. Other things being equal, the recent benchmark yield of 2.37% on a 10-year muni would need to rise to about 2.55% for top-bracket investors in order to provide an equivalent return, says Richard Ciccarone, a muni specialist who heads Merritt Research Services in Chicago. Bond yields rise as prices fall.

In another proposal, Mr. Trump has called for lowering the top rate on "ordinary" income such as wages and interest to 33% from 39.6%. If this is enacted along with the surtax repeal, then the recent benchmark yield would need to rise to about 2.80%, says Mr. Ciccarone. Absent other market changes, the value of a $10,000 investment would shrink to $9,627, according to Mr. Gordon.

The third and most disruptive proposal is in the House GOP tax reform blueprint. It would give investment interest the same tax-favored treatment that long-term capital gains and certain dividends now receive, ending the decadeslong practice of taxing interest at ordinary-income rates.

The blueprint's proposed top rate on taxable interest is 16.5%. In that case, the yield would need to rise nearly 50%, from 2.37% to 3.50%, according to Mr. Ciccarone, in order to provide an equivalent return for top-bracket investors.

Not since the 1986 tax reform lowered the top rate on taxable interest from 50% to 28% have munis faced such a big shift. During that period, the yield on a common muni index rose from 6.54% to a high of 9.17% as Treasury yields also rose, says Mr. Ciccarone.

How likely is a 16.5% top tax rate on interest for individuals? It's a serious proposal, say tax policy specialists, but it's part of a package that also denies net interest deductions to businesses. This denial "will face opposition from leveraged businesses that don't want to lose deductions," says Alan Cole, an economist with the Tax Foundation in Washington.

Ahead of possible tax shifts, Natalie Cohen, who heads municipal-bond research at Wells Fargo Securities, counsels caution both in buying and selling. Other factors besides tax rates affect munis, she says, such as the perception that they are a safe investment.

Muni-fund investors raced out of the sector immediately after the election, sending yields higher, but prices have rebounded a bit lately. Meanwhile, holders of individual bonds can collect their coupons regardless of what happens in the market.

“Tax reform is still full of unknowns,” says Ms. Cohen.

THE WALL STREET JROUNAL

By LAURA SAUNDERS

Dec. 16, 2016 11:02 a.m. ET

Write to Laura Saunders at laura.saunders@wsj.com

Final Issue Price Rules Make Allowances for Competitive Sales.

WASHINGTON – The Treasury Department and Internal Revenue Service have finalized issue price rules that contain special allowances for competitive sales.

Under the rules, which are to be published in the Federal Register on Dec. 9 and would take effect 180 days later, the issue price for competitive sales will be the reasonably expected initial offering price if several certain conditions are met, including that the issuer receives bids for the bonds from three underwriters.

The rules also clarify that, for bonds issued for money in a private placement to a single buyer that is not an underwriter or related party, the issue price is the price paid by that buyer.

In addition, the rules contain a simplified “hold-the-offering-price” anti-abuse rule, place less emphasis on certifications, and narrow the definition of an underwriter.

“We tried to respond to the comments and make the final rules more flexible and more workable,” said John Cross, Treasury’s associate tax legislative counsel.

On competitive sales, Cross said, “As a policymaker, we think that competitive sales promote competition and price transparency and we wanted to provide a workable rule to accommodate this important market sector.”

Market participants praised some aspects of the new rules, but said they have questions about and want to review other provisions more closely.

Emily Brock, director of the Government Finance Officers Association’s federal liaison center, said, “We are pleased to see the Treasury and IRS addressed our concerns with regard to competitive pricing.” She said the GFOA’s debt committee plans to discuss the three-bid requirement for competitive sales and the five-day “hold-the-offering-price” requirement with Cross at its meeting here tomorrow.

Cliff Gerber, president of the National Bond Lawyers Association, also is pleased to see the special rule for competitive sales. “And they’ve now created a modified hold-the-offering-price rule, which I think is good,” he said. But he worried that bad underwriter behavior could hurt issuers’ bonds under the final rules.

Michael Decker, managing director and co-head of municipal securities for the Securities Industry and Financial Markets Association, said, “We are pleased that the issue price rule is now final. While we are still reviewing the release, several provisions of the final rule represent welcome changes. In particular, we support the provision specifying that the general rule will apply at any time the 10-percent sales threshold is met as well as the clarification that underwriters can sell bonds at prices below the initial offering price without breaking the rule. We are also pleased about the provision for special treatment for competitive offerings."

John Vahey, Bond Dealers of America's director of federal policy, said, "BDA appreciates the efforts of the IRS and Treasury to adopt improvements to the issue price rule. However, we have concerns with how the final rule's requirement to hold the initial offering price for five days will alter the market and, also, how the three-bid requirement for competitive deals has the potential to negatively impact the competitive offerings of smaller issuers."

Issue price is important because it is used to help determine the yield on bonds and whether an issuer is complying with arbitrage rebate or yield restriction requirements. It is also used to determine whether federal subsidy payments to issuers for direct-pay bonds such as Build America Bonds are appropriate.

Under existing rules that have been in place for years, the issue price of each maturity of bonds that is publicly offered is generally the first price at which a substantial amount, defined as 10%, is reasonably expected to be sold to the public.

But tax regulators became concerned several years ago that some dealers were "flipping" bonds — selling them to another dealer or institutional investor who then sold them again almost simultaneously — with the prices continually rising before the bonds were eventually sold to retail investors. The regulators worried that the "reasonably expected" issue prices for bonds were not representative of the prices at which the bonds were actually sold.

To address their concerns, the Treasury and IRS proposed issue price rules in 2013, eliminating the reasonable expectations standard and basing the determination of issue price on actual sales. They also proposed raising the "substantial amount" of bonds standard to 25% from 10%.

The rules were strongly criticized as unworkable by issuers and underwriters. They complained about the 25% standard and said they often don't sell 10% or 25% of every maturity right away.

The tax regulators scrapped those rules and re-proposed them in June 2015. Under the re-proposed rules, the issue price for each maturity of bonds generally would be the price at which the first 10% of the bonds are actually sold to the public.

Issuers could use an "alternative method" of determining issue price when 10% of a maturity was not sold by the sale date. The issue price would be the initial offering price of the bonds sold to the public as of the sale date, as long as the lead or sole underwriter certified to the issuer that no underwriter filled an order from the public after the sale date and before the issue date at a higher price, unless market changes justified the higher price. The lead underwriter would then have to document any market changes that justified a higher price.

Dealers complained about the lead underwriter having to provide certifications about the actions of other underwriters.

The final rules contain a general rule under which the issue price is the price at which the first 10% of a maturity of bonds is actually sold to the public.

The rules include a special rule, under which the issue price is the initial offering price as long as the underwriter sticks with the IOP for bond sales during the five business days after the sale date (or a shorter period if 10% of a maturity of bonds is sold to the public at a price that does not exceed the IOP).

The five-day “hold-the-offering-price” provision is an anti-flipping or an anti-abuse provision. The lead underwriter must certify the IOP to the issuer, as well as provide documentation, such as the pricing wire. Each underwriter in a syndicate must agree in writing that it will not offer or sell the bonds at a price higher than the IOP for five business days after the sale date.

Under a special rule for competitive sales, an issuer may treat the reasonably expected IOP of the bonds to be sold to the public as the issue price if the issuer obtains a certification from the winning underwriter bidder as to the reasonably expected IOP upon which it based its bid.

To achieve a competitive sale: the issuer must disseminate the notice of sale in a manner reasonably designed to reach potential underwriters; all bidders must have an equal opportunity to bid; the issuer must receive bids from at least three underwriters “who have established industry reputations for underwriting new issuances of municipal bonds;” and the issuer must award the bonds to the bidder who offers the highest price or lower interest cost.

Issuers have the option of using any of these rules up until the closing (issue) date for their bond transactions.

The IRS also modified the definition of “underwriter” in response to concerns that it was vague and unworkable.

The definition still says “an underwriter is any person that contractually agrees to participate in the initial sale of the bonds to the public by entering into a contract with the issuer or into a contract with a lead underwriter to form an underwriting syndicate.”

But the final rules remove the phrase “or other arrangement” from provisions that say an underwriter “includes any person that, on or before the sale date, directly or indirectly enters into a contract or other arrangement with any of the foregoing to sell the bonds.”

The tax regulators certified that the final rules “will not have a significant economic impact on a substantial number of small entities.

The Bond Buyer

By Lynn Hume

December 8, 2016

TAX - PENNSYLVANIA

City of Philadelphia v. Lerner

Supreme Court of Pennsylvania - November 22, 2016 - A.3d - 2016 WL 6873039

City brought collection action against taxpayer. Following a bench trial, the Court of Common Pleas found taxpayer waived his right to challenge net profits tax and/or business income and receipts tax assessments, and awarded city $280,772.67, which included principal liability of $74,907, $85,828.05 in interest, and $120,037.62 in penalties.

Taxpayer appealed. The Commonwealth Court affirmed. Taxpayer appealed.

The Supreme Court of Pennsylvania held that taxpayer waived for purposes of appeal his argument that his failure to exhaust administrative remedies within the Department of Revenue did not prevent him from challenging city's assessments, where taxpayer failed to raise the issue in the trial court.

COUNTIES - ILLINOIS

Blanchard v. Berrios

Supreme Court of Illinois - December 1, 2016 - N.E.3d - 2016 IL 120315 - 2016 WL 7007820

County inspector general brought action against county assessor for declaratory judgment that it was obligated to comply with inspector's investigation into circumstances surrounding grant of exemptions from property tax and to comply with subpoena.

The Circuit Court entered order requiring assessor to produce subpoenaed documents. Assessor appealed. The Appellate Court affirmed. Assessor's leave to appeal was granted.

The Supreme Court of Illinois held that:

- County ordinances creating office of inspector general and imposing duty on elected county officials to cooperate with investigation by inspector general were proper exercise of county board of commissioners' constitutional authority to exercise those duties, powers and functions provided by law and those provided by county ordinance";
- Ordinances were proper exercise of board' statutory authority to "alter any other duties, powers or functions or impose additional duties, powers and functions upon county officers";
- Assessor did not have authority to oversee or supervise its office free from oversight or investigation by inspector general;
- Ordinances did not impermissibly conflict with county assessor's home rule authority to assess property taxes and grant exemptions from same;
- Board had home rule authority to enact ordinances creating office of inspector general and imposing duty on elected county officials to cooperate with investigation by inspector general; and
- County assessor, as elected official, was not separate from county, as local unit of government recognized under Illinois Constitution, and thus, was subject to ordinances enacted by board.

What Happens When the IRS and Issuer Agree to Disagree?

My last blog post was about how, as a result of a change in the Internal Revenue Code (the "Code"), the IRS will be altering the manner in which it audits many partnerships (and limited liability companies that are taxed as partnerships under the Code). In a nutshell, for tax years beginning on or after January 1, 2018, the IRS may assess a tax deficiency against certain partnerships rather than flowing the taxable income adjustment at the partnership level through to the individual partners and then collecting the additional tax from each individual partner. This change in the Code was deemed to be a revenue raiser due to the increased efficiency in assessing the tax against the partnership rather than the individual partners. This streamlined partnership audit process is similar to the IRS being permitted to settle an IRS audit involving tax-exempt bonds with the issuer or conduit borrower rather than having to assess a tax deficiency against the various bondholders and collecting the tax from each individual bondholder. This got me thinking . . . what happens if the issuer or conduit borrower and IRS cannot agree to a resolution when the IRS believes the tax-exempt bonds are taxable?

As you know, the IRS treats the issuer as the “taxpayer” when it begins an audit of tax-exempt bonds even though the bondholders will ultimately be the “taxpayers” if the tax-exempt bonds become taxable. For example, under IRS guidelines, the IRS sends the information document requests (“IDRs”) to the issuer of the tax-exempt bonds and is authorized to reach a settlement with the issuer. In addition, it is the issuer of the tax-exempt bonds that has the ability to either (a) request a technical advice memorandum (“TAM”) from the IRS national office with respect to one or more issues relating to the tax-exempt bonds, or (b) after receiving a proposed adverse determination from the IRS agent, request that the matter be referred to the IRS’ Office of Appeals (“Appeals”). Although the goal of Appeals is to settle cases with the Appeals’ officer acting as an independent reviewer, sometimes the parties cannot agree. If settlement attempts at Appeals between the IRS agent and issuer are unsuccessful, the IRS will issue a final adverse determination that the tax-exempt bonds are now taxable. If the IRS has not already done so, around the same time that the IRS issues the final adverse determination, the IRS will contact the trustee for the subject bonds and request the names and address of all bondholders thereof.

Once the final adverse determination is made that the tax-exempt bonds are taxable, the issuer no longer has any rights in the audit process. Rather, the IRS will begin treating the bondholders as the “taxpayer” from that point until final resolution of the tax controversy. In general, the IRS has three years from the date that a bondholder filed his or her income tax return reporting tax-exempt interest to assess a tax on the now allegedly taxable interest. The IRS will assess this tax by sending each bondholder a statutory notice of deficiency that is oftentimes referred to as a “90 Day Letter.” The 90 Day Letter sent to each bondholder will set forth the basis for the tax deficiency and will also set forth the amount of tax, interest and penalties owed by such bondholder. The bondholder will have 90 days to respond by filing a petition challenging the assessment in the U.S. Tax Court. In the alternative, the bondholder could pay the assessed tax, interest and penalties due, but then file a claim for refund. At this point, the bondholder could attempt to reach a settlement with the IRS, although there is no formal procedure in place to do so. The incentive for both the bondholder and IRS to settle, however, would be to avoid the costly litigation process discussed below.

After the bondholder’s refund is denied by the IRS (which it presumably would be), the bondholder could then file a claim for refund in the U.S. district court with jurisdiction over his or her tax residence or in the U.S. Court of Federal Claims located in Washington D.C. If the bondholder was to lose at the district court or Tax Court, the bondholder could appeal to the appropriate U.S. Court of Appeals. Similarly, if the bondholder was to lose at the U.S. Court of Federal Claims, he or she could appeal to the U.S. Court of Appeals for the Federal Circuit, which is also located in Washington D.C. If the bondholder then loses at the appellate level, the bondholder could appeal to the U.S. Supreme Court. However, as you know, the U.S. Supreme Court could decide not to hear the case (i.e., by denying the taxpayer’s writ of certiorari), thus affirming the appellate court’s decision.

Assuming that the bondholder hires legal counsel to help navigate the above-described litigation, the process could become very costly for the bondholder even if he or she ultimately wins the case. This bondholder-by-bondholder litigation process would also be very expensive for the IRS. Accordingly, it is a good thing that the vast majority of tax controversies involving tax-exempt bonds are settled by the issuer and IRS before a final adverse determination is issued by the IRS. This is because the issuer has a very strong incentive to settle with the IRS so that the marketplace does not react negatively the next time the issuer wants to issue tax exempt bonds. In addition, from the IRS’ standpoint, it is far more efficient to settle with the issuer than to pursue each bondholder. Therefore, thankfully, it is very rare for the IRS and issuer to agree to disagree.

Squire Patton Boggs

The Public Finance Tax Blog

By Cynthia Mog on December 7, 2016

IRS Publishes Issue Price Definition for Tax-Exempt Bonds.

Final issue price regulations in Treasury Decision 9801 were publicly filed with the Federal Register on December 8 and have been published as of December 9. The effective date will be 180 days after publication of the final regulations.

The final regulations include a special rule for competitive sales.

Federal Register Final Regulations

How Big-Box Retailers Weaponize Old Stores.

Merchants such as Walmart are using a novel legal tactic to sharply lower their property taxes.

Tucked away on the northern edge of Michigan's rugged Upper Peninsula, Sault Ste. Marie is bracing for the battle of its life. The tourist town is heading to court in early 2017 to fight Walmart Stores, which seeks to cut $286,000 off its annual property tax bill on a local store. Using what critics call the "dark store loophole," Walmart is following in the footsteps of big-box merchants including Lowe's and Target by arguing that its bustling store should be assigned about the same value for tax purposes as one that's been vacant for years, hundreds of miles away.

The financially strapped town of 14,000 faces legal bills of about $100,000 to take on the retailing giant. The cost of the battle that started in 2014 already has forced local authorities to slash budgets for everything from senior meals and the local animal shelter to police and fire pensions. Now its leaders have decided they've been pushed around long enough. "It is like David and Goliath," says Jim German, the county administrator in Chippewa County, which includes Sault Ste. Marie. "We are going to give it our best shot, because it isn't fair."

The city has tried for years to keep the dispute out of court to avoid the legal fees, agreeing with Walmart in 2014 and 2015 to lower the store's local taxes by a total of $103,000. This year, Walmart has gone too far, German says. It wants its store, currently assessed at $63 a square foot, to be valued at $16 a square foot based on sales of similar-size vacant properties across the state—less than what some local small businesses pay. Chippewa County is hedging its bets in case of a loss, freezing salaries for all nonunion employees.

Walmart, which annually pays $3.3 billion in property taxes, state income taxes, and franchise taxes plus $15 billion in state and local sales taxes, says it pays its "fair share" of property tax in Michigan based on standard appraisal methodology. "When we can't reach an agreement, we seek clarification through the legal process for a fair market value of our property," says Walmart spokesman Lorenzo Lopez.

The dark store tax argument has been gaining use since a Michigan court accepted it in 2010. In that case, the judge agreed that a Target store in a depressed Detroit suburb was worth about half the city's valuation. From that one ruling, which turns on its head the traditional way municipalities value businesses based on the cost of acquiring the land and building the structure, big-box retailers including Lowe's, Best Buy, and Menards have spread out across the country, taking to court more than 100 townships, cities, and counties in at least a dozen states over the past four years. In most cases the stores have prevailed, saving millions of dollars in property taxes, according to the National Association of Counties. Two-thirds of Michigan's counties have lost more than $75 million in property taxes since 2012 as a result of the ruling. Indiana estimates it could lose $120 million in tax revenue annually if the strategy takes hold.

That's left many municipalities scrambling to cope with lost revenue. Library hours have been curtailed, roads have gone unpaved, and police and fire departments have made do with aging equipment. County officials in Alabama and Texas, where Lowe's only recently began filing dark store suits, say they fear a similar fate.

"If the big-box folks do this, then you'll have it spill down to the banks, the fast-food places, the drugstores," says Don Armstrong, property tax commissioner for Shelby County, Ala., where Lowe's is pursuing a challenge. "It would just multiply and have a domino effect."

Target, noting that it wants to ensure its properties are assessed at fair market value, said in a statement that it "remains committed to supporting the communities in which we do business, and this includes paying a fair share of property taxes."

Michael Shapiro, a Detroit real estate tax attorney who pioneered the dark store argument, says he's not insensitive to the financial needs of communities, but "whether it is unfair or not doesn't have anything to do with me. I'm just looking at what the law is." For more than 40 years, Shapiro has made a career out of helping businesses challenge property tax bills. A lawyer with the Detroit firm Honigman Miller Schwartz and Cohn, he made a name for himself representing car companies, successfully arguing their plants' taxes should be based on the values of closed factories. Years later, he saw a similar opportunity in big-box stores. He made his first such successful case in 2010.

Typically, local property tax assessors set values of such stores based on the purchase price of the land plus the cost of construction, less depreciation. Shapiro believed a more accurate way to measure the value was to use comparable sales of similar properties, the way a house is valued for tax purposes.

He began amassing comparable sales data to make a case that the value of a big-box store on the market was far lower than what tax assessors had determined because they were built to suit the needs of a specific owner—the way "a suit would lose its value once it was tailored to a specific person," says Shapiro.

There's now a thriving cottage industry of lawyers, tax representatives, and appraisers helping retailers initiate dark store challenges. Larry Clark, director for strategic initiatives at the International Association of Assessing Officers in Kansas City, Mo., says lawyers and tax representatives typically target smaller towns that are less able to mount a vigorous defense. "They pick the low-hanging fruit," he says. "It probably costs $50,000 or more to litigate one big-box chain," says Jack Van Coevering, who's represented small towns in Michigan that have faced big-box valuation challenges. "If you are a township with a whole bunch of these properties, imagine that."

Towns can find it hard to attract companies to fill vacant buildings that bring down valuations. Often a closed store has deed restrictions that prevent another big-box retailer from moving in, sometimes for years, significantly limiting the pool of potential buyers. Buildings can sit vacant for years and deteriorate or end up repurposed for low-revenue uses such as roller-skating rinks or flea markets.

Probably no community has suffered more from Shapiro's brainchild than Marquette, a three-hour drive west of Sault Ste. Marie. In 2012, Lowe's argued that its two-year-old store there, which cost about $10 million to build, was worth just $3.5 million based on the resale value of shuttered big-box stores in other parts of the state. A judge with the Michigan Tax Tribunal agreed, and Lowe's tax bill was slashed by two-thirds, forcing Marquette to pay the company nearly $450,000 in back taxes and lowering its tax bill by more than $150,000 a year going forward.

"Lowe's pays property tax, income tax, sales and use tax, and, just like homeowners, we want to be taxed on the fair value of our buildings and land," the retailer said in a statement. "It's Lowe's intention to always pay our fair share of taxes."

The home center chain's suit opened the floodgates for Marquette's other retail chains. Even car dealerships made the same case. In the almost five years since, the timber and mining community on the edge of Lake Superior has lost more than $2 million in property tax revenue from retailers including Target, Best Buy, and Kohl's.

Shortly after the ruling, a county-funded group home for troubled teens was forced to close, and the local library has slashed its hours. Ron DeMarse, the township's fire chief, worries his 23-year-old fire truck and battered two-way radios won't weather another winter. That would be a disaster, since he has no money left to replace them. DeMarse says the $56,000 he's lost in this year's budget from Lowe's tax challenge would have been enough to cover annual payments on a new engine to replace his aging one—the only truck the department has with a pump and ladder large enough to put out a fire at a building the size of Lowe's. Now his only option is a ballot initiative that would raise the needed money from the township's residents. "Maybe we just won't replace it," he says, and Lowe's might be forced to pay higher insurance premiums. "Maybe that would be fair."

Sentiments are equally raw in Sault Ste. Marie, where civic leaders are gearing up to keep its tax dollars in town rather than hand them back to Walmart. "It is an attack on all the services we provide: the sheriff's department, the health department, the schools, everyone is going to suffer here," Chippewa County Commissioner Jim Martin told residents at a recent county meeting. "That money will leave our community and go to their corporate offices."

The bottom line: *Big-box retailers are often thriving businesses. Now some are petitioning to pay the same property tax as shuttered stores.*

Bloomberg

by Shannon Pettypiece

December 8, 2016 — 5:01 AM EST December 8, 2016 — 9:47 AM EST

New Information Document Request (IDR) – What's the Point?

On November 21, as most of us were preparing for a relaxing Thanksgiving holiday, the IRS publicly released two internal guidance memoranda (both available at TEGE-04-116-0028) addressed to "All

TE/GE Examiners," the first of which describes new procedures for the preparation and issuance of IDRs in connection with tax-favored bond audits and procedures for the enforcement of responses to those IDRs, and the second sets forth IDR "Best Practices." The announcement of the new procedures on the IRS website describes their purposes:

"The updated process will:

- Provide for open and meaningful communication between the IRS and taxpayers.
- Reduce taxpayer burden and provide consistent treatment of taxpayers.
- Allow the IRS to secure more complete and timely responses to IDRs.
- Provide consistent timelines for IRS agents to review IDR responses.
- Promote timely issue resolution."

A review of the new procedures, however, gives the clear impression that they are primarily designed to provide IRS agents increased leverage to force issuers and their counsel to respond more quickly to the often lengthy and burdensome IDRs that the IRS has been lately issuing, while imposing no pressure on the IRS to resolve audits more quickly.

The following are some key excerpts from the new IDR procedures, with a little commentary of my own.

Continue reading.

Squire Patton Boggs

The Public Finance Tax Blog

By Bob Eidnier on December 1, 2016

TAX - TEXAS

City of Austin v. Travis Central Appraisal District

Court of Appeals of Texas, Austin - November 10, 2016 - S.W.3d - 2016 WL 6677937

City brought action seeking judicial review of appraisal review board's order, which denied city's challenge to level of appraisal for vacant land and commercial real property for 2015 tax year, and challenging constitutionality of provisions of Tax Code concerning unequal appraisal protests by property owners.

The District Court granted a plea to the jurisdiction filed by a group of commercial property owners and a motion for summary judgment filed by a separate commercial property owner. City appealed.

The Court of Appeals held that:

- City failed to plead injury sufficient to confer standing to challenge constitutionality of Tax Code provisions, and
- City failed to exhaust its administrative remedies in connection with its challenge to appraisal levels.

City failed to establish injury sufficient to confer standing to challenge constitutionality of provisions of Tax Code allowing appraisal district to defeat property owner's unequal appraisal protest by demonstrating that median appraised value of reasonable number of comparable properties exceeded appraised value of owner's property. City was not charged with giving effect to provisions or ensuring their fulfillment, as provisions did not describe or concern any mechanism by which tax units to were to access, impose or, collect ad valorem taxes, and fact that city would eventually calculate and impose ad valorem taxes based on property values determined by appraisal district failed to demonstrate an injury that was concrete and particularized to city, as opposed to its property owners.

City failed to exhaust its administrative remedies in connection with its challenge to level of appraisals for vacant land and commercial property for 2015 tax year, and district court thus lacked subject-matter jurisdiction to consider city's petition for judicial review of appraisal review board's order denying city's challenge petition. Although city's attorneys and representatives attended hearing on its challenge petition, it did not present a case on the merits of its challenge, but rather presented a joint motion requesting that the review board enter an order denying its challenge petition, thus depriving the review board of any opportunity to decide the merits of the petition.

TAX - SOUTH CAROLINA

Olds v. City of Goose Creek

Court of Appeals of South Carolina - November 16, 2016 - S.E.2d - 2016 WL 6776295

Taxpayer appealed decision of city council regarding computation of gross income under business license tax ordinance, and further asserted claims against city for violation of equal protection, violation of procedural due process, abuse of process, violations of state and federal constitutions, and violation of the South Carolina Freedom of Information Act, against city administrator and city finance director for conspiracy, and against city's department of public works for breach of contract.

The Circuit Court affirmed the city council's decision regarding the meaning of gross income under city ordinance, and granted city summary judgment on taxpayer's other claims. Taxpayer appealed.

The Court of Appeals held that:

- City's power to levy a business license tax under statute governing the powers conferred upon municipalities was not limited by the meaning of the term "gross income," as used in the remainder of the statute;
- Taxpayer's gross income for business license tax purposes constituted the total revenue of his business, before deducting expenditures for any purpose;
- On appeal to the Circuit Court from decision of city council regarding computation of gross income under business license tax ordinance, any evidence of animus that existed between taxpayer and city employees was irrelevant in determining the meaning of gross income under the ordinance;
- Affidavit of law professor offered by taxpayer on appeal to the Circuit Court was inadmissible because it constituted nothing more than a legal argument;
- City council's refusal to allow taxpayer to participate in appellate hearing with regard to appeal from business license tax assessment, and city's decision to withhold water service until taxpayer paid past due business license tax, did not prejudice defendant, as required to support due process claim; and
- No evidence existed to demonstrate that city singled out taxpayer for disparate and arbitrary tax treatment, and shut off the water supply to his properties in an attempt to force him to capitulate to city's position in a business license tax dispute.

City's power to levy a business license tax under statute governing the powers conferred upon municipalities was not limited by the meaning of the term "gross income," as used in the remainder of the statute. The only limitation on the broad grant of power was that the ordinance could not be inconsistent with the constitution or general laws of the state, and taxpayer challenging city's interpretation of "gross income" made no argument explaining how the ordinance was inconsistent with the constitution or general laws.

Notwithstanding city ordinance's later explanation that gross income for business license tax purposes shall conform to the gross income reported to the State Tax Commission and that gross income may be verified by the inspection of state and federal tax returns, taxpayer's gross income for business license tax purposes constituted the total revenue of his business, before deducting expenditures for any purpose, and thus, the term "gross income" applied to the total sale price of any real property, rather than merely to the business's gain.

On appeal to the Circuit Court from decision of city council regarding computation of gross income under business license tax ordinance, any evidence of animus that existed between taxpayer and city employees was irrelevant in determining the meaning of gross income under the ordinance.

On appeal to the Circuit Court from decision of city council regarding computation of gross income under business license tax ordinance, affidavit of law professor offered by taxpayer was inadmissible because it constituted nothing more than a legal argument.

City council's refusal to allow taxpayer to participate in appellate hearing with regard to appeal from business license tax assessment, and city's decision to withhold water service until taxpayer paid past due business license tax, did not prejudice defendant, as required to support due process claim. Because the issue regarding the interpretation of the ordinance was one of statutory construction, and taxpayer was able to raise the issue of water service again in the circuit court, the circuit court, in its appellate capacity, was able to review the issues without deference to the city council's decision.

Counties Urge Preservation of Tax-Exempt Municipal Bonds.

For over 100 years, municipal bonds have served as a key tool for county and state governments to finance roads, bridges, schools and other facilities while saving taxpayers money.

At a Capitol Hill briefing today, National Association of Counties Executive Director Matthew Chase urged Congress to preserve the tax exemption of municipal bond interest in any potential rewrite of the federal tax code. Removing the interest deduction would increase state and local borrowing costs by over $500 billion, costs that would be ultimately shifted to local taxpayers and potentially result in decreased infrastructure investment.

"Much of the complex infrastructure counties, states and cities deliver can only be delivered through municipal bond financing," said Chase.

Through municipal bonds, state and local governments have invested more than $3 trillion in infrastructure between 2003 and 2012.

For America's counties, it's a substantial portfolio of responsibility, as counties:

- own and maintain 46 percent of the nation's public roads

- own nearly 40 percent of all public bridges
- are involved with nearly a third of the country's transit systems and airports
- operate 91 percent of all local jails, and
- operate 976 hospitals and over 1,500 local health departments.

Additionally, taxing municipal bond interest would violate the principle of sovereign tax immunity — states cannot tax the powers, the operations or the property of the United States, nor how the United States executes its powers, nor can the United States tax either the instrumentalities or the property of the states.

"Municipal bonds are not only a fundamental building block of the federalism system, but they also help to build America's infrastructure," said Chase.

For more information, visit http://www.naco.org/advocacy/action-centers/municipal-bonds

National Association of Counties

Nov. 29, 2016

TAX - WEST VIRGINIA

Matkovich v. CSX Transportation, Inc.

Supreme Court of Appeals of West Virginia - November 16, 2016 - S.E.2d - 2016 WL 6833988

Tax Commissioner appealed decision of the Office of Tax Appeals (OTA) which determined that taxpayer that paid motor fuel use tax was entitled to sales tax credit for the sales taxes it paid on motor fuel purchased from the cities, counties, and other municipalities of other states.

The Circuit Court affirmed. Tax Commissioner appealed.

The Supreme Court of Appeals held that dormant Commerce Clause required that taxpayer, which paid motor fuel use tax, receive sales tax credit for the sales taxes it paid on the motor fuel both to other states and to the subdivisions of other states.

Both the motor fuel use tax imposed on taxpayer and the corresponding sales tax credit allowed for sales taxes that taxpayer paid on motor fuel purchased from other states had substantial nexus with the State, as required for use tax and sales tax credit to comply with the dormant Commerce Clause. Taxpayer operated interstate rail transportation service in the State and purchased fuel outside the State which it used in its operations in the State.

Motor fuel use tax imposed on taxpayer that purchased motor fuel from other states which it used in its interstate rail transportation operations in the State was fairly apportioned, as required for use tax to comply with the dormant Commerce Clause. Use tax was calculated with specific reference to the amount of motor fuel that taxpayer used in the State, and use tax charged to taxpayer directly correlated to the fuel that it used for the miles it traveled within the State.

Dormant Commerce clause required that taxpayer, which paid motor fuel use tax, receive sales tax credit for the sales taxes it paid on the motor fuel both to other states and to the subdivisions of other states. Disallowance of sales tax credit for sales taxes imposed by subdivisions of other states would produce total tax burden on interstate commerce that was higher than purely intrastate transaction, and allowing sales tax credit only for sales taxes paid to other states would unfairly discriminate against interstate commerce.

TAX - ILLINOIS

Village of Arlington Heights v. Pappas

Appellate Court of Illinois, First District, Sixth Division - November 10, 2016 - N.E.3d - 2016 IL App (1st) 151802 - 2016 WL 6651591

Village appealed order of Circuit Court granting summary judgment in favor of the county treasurer on the village's declaratory judgment action and finding that the treasurer had the authority to seek repayment from the village for refunds the treasurer made to taxpayers of certain incremental tax payments received by the village during the lifetime of two tax increment financing (TIF) districts.

The Appellate Court held that legislature authorized treasurer to be reimbursed by village for her post-TIF refunds of protested property taxes.

Legislature authorized county treasurer, in Property Tax Code, to be reimbursed by village for her post-tax increment financing (TIF) refunds of protested property taxes. Although legislature never set forth a reimbursement mechanism specifically for post-TIF refunds, it did set forth a general mechanism for the refunding and reimbursement of overpaid taxes in the Code, and thus, policy adopted by treasurer, in making the post-TIF refunds out of Class A fund and then seeking reimbursement from next property taxes collected by village, was consistent with the Code.

TAX - CALIFORNIA

City of San Jose v. Sharma

Court of Appeal, Third District, California - November 3, 2016 - Cal.Rptr.3d - 2016 WL 6520123

City petitioned for writ of mandate to compel county to give city tax increment revenue from county's ad valorem tax on real property. County cross-petitioned for writ of mandate.

The Superior Court ruled that city was entitled to the tax increment portion of the tax proceeds to put toward the winding down of city's former redevelopment agency, but that tax increment revenue not needed to pay bond debt of the former redevelopment agency was subject to a passthrough agreement requiring the revenue to be passed through to the county. City and county appealed.

The Court of Appeal held that:

- Tax increment revenue from county's ad valorem tax on real property had to be used to pay obligations of city's former redevelopment agency, and
- The amount necessary to service former redevelopment agency's bond debt could be deducted from the amount that passed through to the county.

Under the constitutional provision stating that tax increment "shall be allocated to and when collected shall be paid into a special fund of the redevelopment agency," tax increment revenue from a county's ad valorem tax on real property had to be used to pay the obligations of a city's former redevelopment agency, even though the tax was a special tax to finance county's participation in the

Public Employees Retirement System (PERS), where the tax increment portion of the special tax had been, for 60 years, a tax on real property within the former redevelopment agency's project area to finance redevelopment in that area.

The constitutional provision stating that tax increment "shall be allocated to and when collected shall be paid into a special fund of the redevelopment agency" prevails over the statute providing that "revenues from any special tax shall be used only for the purpose or service for which it was imposed," since the constitutional provision applies to all ad valorem taxes on real property, without regard to whether the tax is a general or special tax.

City's use of tax increment revenue associated with county's ad valorem tax on real property to pay the obligations of city's former redevelopment agency did not constitute an unconstitutional gift of public funds, since the tax increment revenue never belonged to the county, and since redevelopment in the city was a public purpose of general interest to the county, where the tax increment portion of the retirement levy was collected within the city's former redevelopment agency's project area, by law, for the purpose of paying the obligations of the redevelopment agency.

City's use of tax increment revenue associated with county's ad valorem tax on real property to pay the obligations of city's former redevelopment agency did not violate county employees' vested contractual rights to continuation of retirement benefits or of the funding for such benefits, even though the tax was a special tax to finance county's participation in the Public Employees Retirement System (PERS), since distribution of the tax increment portion of the retirement levy did not prevent the county from paying the required amount to PERS for the county employees' benefits.

Under the statute authorizing deduction of a trust fund deficiency from payment of passthrough funds in the "waterfall" payment schedule for the benefit of the holders of former redevelopment agency enforceable obligations, the amount necessary to service a former redevelopment agency's bond debt could be deducted from the amount that passed through to the county under a contractual passthrough agreement between the county and the former redevelopment agency, and thus tax increment revenue that would have passed through to a county could be used to pay the former redevelopment agency's enforceable obligations listed in the Recognized Obligation Payment Schedule (ROPS), where the passthrough agreement made payment of passthrough funds to the county subordinate to the former redevelopment agency's "debt service payments."

Under the statute authorizing deduction of "funds for servicing bond debt" from payment of passthrough funds in the "waterfall" payment schedule for the benefit of the holders of former redevelopment agency enforceable obligations, the amount that could be deducted from the ad valorem tax revenue proceeds that passed to a county under a passthrough agreement was limited to the amount necessary to service a former redevelopment agency's bond debt.

TAX - SOUTH CAROLINA

Olds v. City of Goose Creek

Court of Appeals of South Carolina - November 16, 2016 - S.E.2d - 2016 WL 6776295

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TE/GE Announces New Information Document Request Management Process.

The Tax Exempt and Government Entities Division of the Internal Revenue Service has issued new internal guidance for its agents on issuing information document requests (IDRs). The IRS issues IDRs to gather information during an examination. The new process will go into effect on April 1, 2017. Prior to its implementation, TE/GE will provide training to its agents on the new process.

Under the new process:

1. Taxpayers will be involved in the IDR process.
2. Examiners will discuss the issue being examined and the information needed with the taxpayer

prior to issuing an IDR.
3. Examiners will ensure that the IDR clearly states the issue and the relevant information they are requesting.
4. If the taxpayer does not timely provide the information requested in the IDR by the agreed upon date, including extensions, the examiner will issue a delinquency notice.
5. If the taxpayer fails to respond to the delinquency notice or provides an incomplete response, the examiner will issue a pre-summons notice to advise the taxpayer that the IRS will issue a summons unless the missing items are fully provided.
6. A summons will be issued if the taxpayer fails to provide a complete response to the pre-summons letter by its response due date.

The new process requires the examiners' managers to be actively involved early in the process and ensures that IRS Counsel is prepared to enforce IDRs through the issuance of a summons when necessary. Throughout this process, the IRS will respect taxpayer rights and the changes will reflect the agency's commitment to the Taxpayer Bill of Rights.

The updated process will:

- Provide for open and meaningful communication between the IRS and taxpayers.
- Reduce taxpayer burden and provide consistent treatment of taxpayers.
- Allow the IRS to secure more complete and timely responses to IDRs.
- Provide consistent timelines for IRS agents to review IDR responses.
- Promote timely issue resolution.

How Did Arbitrage "Rebate" Get its Name?: Squire Patton Boggs

Rick Weber of Norton Rose Fulbright is the Editor-in-Chief of The Bond Lawyer, NABL's quarterly journal. He writes a wonderful column on language that introduces each issue, and in the Summer 2016 issue, he posed the following question: When issuers are required to pay arbitrage profits earned on investments of tax-exempt bond proceeds to the federal government, why is it called "rebate," when the arbitrage profits were not the federal government's money in the first place? "In order to have a "return" or "refund" or "pay-back" of funds to the US government," Weber notes, "the funds must start there." We venture an explanation below.

Continue reading.

Squire Patton Boggs

By Johnny Hutchinson on November 21, 2016

TAX - CALIFORNIA

City of San Jose v. Sharma

Court of Appeal, Third District, California - November 3, 2016 - Cal.Rptr.3d - 2016 WL 6520123

City petitioned for writ of mandate to compel county to give city tax increment revenue from county's ad valorem tax on real property. County cross-petitioned for writ of mandate.

The Superior Court ruled that city was entitled to the tax increment portion of the tax proceeds to put toward the winding down of city's former redevelopment agency, but that tax increment revenue not needed to pay bond debt of the former redevelopment agency was subject to a passthrough agreement requiring the revenue to be passed through to the county. City and county appealed.

The Court of Appeal held that:

- Tax increment revenue from county's ad valorem tax on real property had to be used to pay obligations of city's former redevelopment agency, and
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Under the constitutional provision stating that tax increment "shall be allocated to and when collected shall be paid into a special fund of the redevelopment agency," tax increment revenue from a county's ad valorem tax on real property had to be used to pay the obligations of a city's former redevelopment agency, even though the tax was a special tax to finance county's participation in the Public Employees Retirement System (PERS), where the tax increment portion of the special tax had been, for 60 years, a tax on real property within the former redevelopment agency's project area to finance redevelopment in that area.

The constitutional provision stating that tax increment "shall be allocated to and when collected shall be paid into a special fund of the redevelopment agency" prevails over the statute providing that "revenues from any special tax shall be used only for the purpose or service for which it was imposed," since the constitutional provision applies to all ad valorem taxes on real property, without regard to whether the tax is a general or special tax.

City's use of tax increment revenue associated with county's ad valorem tax on real property to pay the obligations of city's former redevelopment agency did not constitute an unconstitutional gift of public funds, since the tax increment revenue never belonged to the county, and since redevelopment in the city was a public purpose of general interest to the county, where the tax increment portion of the retirement levy was collected within the city's former redevelopment agency's project area, by law, for the purpose of paying the obligations of the redevelopment agency.

City's use of tax increment revenue associated with county's ad valorem tax on real property to pay the obligations of city's former redevelopment agency did not violate county employees' vested contractual rights to continuation of retirement benefits or of the funding for such benefits, even though the tax was a special tax to finance county's participation in the Public Employees Retirement System (PERS), since distribution of the tax increment portion of the retirement levy did not prevent the county from paying the required amount to PERS for the county employees' benefits.

[IRS Publishes Arbitrage Guidance for Tax-Exempt Bonds.]

[Read the IRS Guidance.]

[The Tax Man Demands a Rain Check - Er . . . Stormwater Fee.]

An EPA mandate to reduce runoff is inspiring a new levy on precipitation in my Virginia town.

When it rains, it pours—and where I live, stormy weather will soon be subject to a new tax. Such is life in a deep-blue Washington suburb that's trying to comply with a mandate from the Environmental Protection Agency.

Six years ago, the EPA issued a regulation forcing D.C. and the states in the Chesapeake Bay watershed to control the quality of their rainfall runoff. Alexandria's solution is to implement a new "stormwater management fee" to fund green pet projects like rooftop gardens on municipal buildings and permeable pavement in parks.

Maryland tried a similar approach under Gov. Martin O'Malley, a Democrat, in 2012. The state law required nine counties and Baltimore to levy a fee on every property owner in their jurisdiction. But the "rain tax," as it came to be known, was a point of public anger—and mockery. Republican gubernatorial candidate Larry Hogan made its repeal central to his 2014 campaign, and he fulfilled his promise by devolving the mandate down to local jurisdictions.

Virginia's system is roughly the same. It allows counties and independent cities like Alexandria to decide for themselves how to best comply by minimizing or treating runoff. But higher taxes seem to be what politicians are most eager to entertain.

That's certainly the case in Alexandria. Last month residents received an email inviting them to a public meeting with the city's Environmental Policy Commission, which would detail its proposal to meet the runoff mandate. My interest was piqued by a line suggesting that the city had decided not to "raise taxes or cut spending" but would instead pursue a "fee" on residents.

On the night of the meeting, several people—a mix of citizens, environmental activists and state and federal bureaucrats—crowded into the small conference room to watch a slideshow and ask questions. From the start, the committee described the new levy as a matter of fairness, that great progressive principle.

Currently, 70% of the money that the city is spending to comply with the mandate comes from the general fund, with the rest coming from property taxes. According to the city's math, this means residential properties—including homeowners like me—pay about 58% of the total cost, although we contribute only 37% of the rainfall runoff.

The committee's solution is a fee based on the percentage of a property's land that is covered with non-permeable surfaces—meaning it contributes to runoff. That way all parties would pay "their fair share." Commercial properties that contribute 63% of the runoff would pay 63% of the new fee. Homeowners would pay about $145 a year for a typical single-family dwelling, according to the city. That might seem low, but local taxes and fees add up quickly.

There are also a number of fictions hiding under the surface. Most glaring is the claim that the fee isn't a tax. This is a distinction without a difference—especially since the fee will be assessed annually with property taxes.

Nor does the facade of "fairness" hold up. Alexandrians might assume that the new fee will replace the existing taxes they pay toward complying with the mandate. It won't. When pressed by several attendees, city officials conceded that the fee will exist on top of the old revenue stream. The committee tried to deflect criticism by saying that the city council could decide to return that money to taxpayers later.

This elicited a few disbelieving laughs. The man seated next to me asked a pointed question: Had Alexandria ever passed a tax cut or refund in conjunction with a new fee? The city official couldn't think of an example—hardly a shock in a town as blue as mine.

Naturally, the rain tax will increase over time. One slide, which the committee sped by, indicated that the fee is expected to rise by 32% in its first four years. When one attendee pointed this out, another ruefully shook her head and mumbled, "That's how it always goes." After four years the city provides no projections, but the fee will probably keep on rising.

One official expressed hope that the rate would level off after a few years, but he also said the city's environmental projects will only require more capital over time. Although the updates to the city's infrastructure are supposed to be completed in 10 years, the fee will doubtless outlast it.

Judging by the meeting, it's unlikely that my fellow Alexandrians will respond the way voters did in Maryland. The general mood was one of approval, even excitement. One aging hippie could hardly contain his glee; another resident thought the tax didn't go far enough. By my count, only three people, including me, seemed opposed.

Before we broke for the evening, the Environmental Policy Committee reminded us that the rain-tax proposal was still subject to change. Lowering or eliminating the storm-water fee for churches, which will average $2,000 in the first year, was mentioned. But the City Council—composed entirely of Democrats—is all but guaranteed to include some version in its 2018 budget. Here's hoping it rains the day they vote.

THE WALL STREET JOURNAL

By STEPHEN FORD

Nov. 25, 2016 5:07 p.m. ET

Mr. Ford is a writer in Virginia.

As Soda Taxes Gain Wider Acceptance, Your Bottle May Be Next.

For more than a decade, Coca-Cola, Pepsi and other beverage companies have fought mightily against efforts to tax sugary sodas, defeating more than three dozen such proposals around the country.

But this month, voters in San Francisco, Oakland and Albany, Calif., as well as Boulder, Colo., stunned the industry by approving ballot measures in favor of soda taxes. Cook County, Ill., followed a few days later, bringing a soft-drink tax to Chicago and surrounding areas. They are joining Berkeley, Calif., which passed a tax two years ago, and Philadelphia, which passed one in June, bringing to seven the number of American communities with soda taxes.

With that public momentum, a soda tax may be coming to a city near you.

Advocates say the recent sweep represents a watershed moment in the fight for soft-drink taxes. Once viewed as measures likely to find support only in largely health-conscious cities like Berkeley and Boulder, soda taxes have emerged as a bountiful revenue source for cash-strapped local governments to fund early childhood education, public safety and deficit reduction. Soda tax advocates say they believe more cities will now consider their own taxes on sweetened beverages to combat obesity and to finance local programs.

“There’s a momentum with these taxes that will be hard for the industry to stop,” said Kelly Brownell, dean of the Sanford School of Public Policy at Duke University, who met with some ridicule when he first proposed a “sin tax” on junk food in 1994. “I expect a year or two from now that the taxes will be widespread.”

All of the new measures so far impose a tax of at least a penny per ounce of sugary drinks, including sodas, sweetened iced teas and some fruit drinks. Soda tax supporters say they are taking inspiration from the fight against tobacco, which included successful efforts to impose hefty taxes on cigarettes as a way to curb consumption. They have even taken to calling the industry “Big Soda,” a not-so-veiled reference to Big Tobacco.

The tax measures came as soft-drink sales were already slumping — more and more consumers have switched to bottled water and other drinks they consider healthier options than carbonated soft drinks. Viewing taxes as another threat to its core products, the beverage industry has fought vigorously, organizing local business coalitions, lobbying politicians, and spending millions of dollars on advertising and direct mail. The American Beverage Association, an industry trade group, spent $38 million opposing the fall ballot proposals, though it lost every one.

Even so, beverage makers say they are not convinced that soda taxes will be widely adopted. With the help of the beverage association, they have effectively painted the taxes as unfair nanny-state measures that are bad for business and impose a disproportionate burden on the poor.

“I’m originally from Iowa, born and bred, and I just don’t see this discriminatory, regressive tax being embraced by Iowans or Midwesterners or Southerners and others in a large swath of the country,” said Susan Neely, the president of the American Beverage Association. “I just do not believe that this is going to be a tax sweep throughout America.”

But public opinion on soda has turned more negative in recent years, with a growing share of Americans believing that sugary drinks contribute to obesity, Type 2 diabetes and other maladies. And the industry now faces a more sophisticated and well-financed opposition. Soda taxes, once a fanciful cause of amateur health crusaders and academics like Dr. Brownell, have drawn the support of politically active billionaires. Michael R. Bloomberg, the former New York City mayor, poured nearly $20 million into the Bay Area soda tax campaigns, hiring political consultants and media experts with extensive experience lobbying city councils and shifting public opinion.

In 2012, when the mayor proposed a limit of 16 fluid ounces on sugary drinks sold in New York, he was pilloried by opponents and ridiculed by late-night comedians as a fun-hating scold. The measure was rejected in court. Four years later, Mr. Bloomberg said, he is still met at speaking engagements with Big Gulp cups, a gibe at his failed soda regulation effort.

But now he sees soft-drink regulation gaining mainstream acceptance.

“While we may have lost that battle in the courts, you can make the very good case that we won the war,” Mr. Bloomberg said.

The industry remains adamant that it will continue fighting soda taxes. The beverage association argues that sugary drink consumption has not increased obesity, and that soda taxes will not reduce it. But the trade group also claims it is doing its part to reduce obesity by encouraging consumers to drink its diet and low-calorie options instead of full-calorie sodas. Ms. Neely, the beverage association president, has been trumpeting industry efforts to market lower-calorie choices as proof of a commitment to public health.

“One thing we’ll continue to do with full gusto is try to reduce calories and sugar in the American diet,” Ms. Neely said. “We don’t want to fight with public health. We agree that more needs to be done, and we’re trying to do it in a very serious and systematic way. We believe we have a responsibility to help address the obesity problem, and we’re doing it in a way that we think is powerful and will yield lasting results.”

Research from Mexico, which approved national taxes on sugary drinks and junk food in 2013, has found that taxes did drive down soft-drink sales, particularly among low-income populations that tend to drink the most of those. Research on Berkeley’s soda tax found a similar trend. But it is too soon to know whether those drops in sales will lead to lower rates of obesity or diabetes.

Still, not every politician has needed a public health argument to embrace a soda tax. Jim Kenney, the mayor of Philadelphia, sold a tax there to City Council members by linking it to a popular initiative to expand prekindergarten. Cook County officials described the tax revenue as crucial to closing budget shortfalls so they could save public safety jobs. And Santa Fe, N.M., the latest city to propose a soda tax, presented it as a way to raise much-needed money for early childhood education.

John Arnold, a hedge fund billionaire who invested heavily in the Philadelphia and California campaigns, said he became interested in soda taxes for public health reasons, but also believes soda taxes have advantages over other ways to raise municipal money. “Do you do it by increasing sales taxes or increasing income taxes, or can you find ways, like through soda taxes, where you get an added benefit of improving the health at the local level in addition to raising money?” he asked.

Both Mr. Arnold and Mr. Bloomberg said they hoped the recent election successes would make soda taxes a more popular idea, able to attract political support and a wider array of financial supporters. Mr. Bloomberg said he was committed to funding well-organized efforts as they continue to emerge.

“We certainly aren’t going to walk away from this,” he said.

THE NEW YORK TIMES

By ANAHAD O’CONNOR and MARGOT SANGER-KATZ

NOV. 26, 2016

TAX - MINNESOTA

Minnesota Energy Resources Corp. v. Commissioner of Revenue

Supreme Court of Minnesota - November 9, 2016 - N.W.2d - 2016 WL 6635550

Taxpayer, a natural gas utility, sought judicial review of determination by Commissioner of Revenue valuing its natural-gas pipeline distribution system for purposes of taxing personal property.

The Tax Court reduced valuation and ordered recalculation of tax liability. Taxpayer and Commissioner appealed.

The Supreme Court of Minnesota held that:

- Evidence supported Tax Court's exclusion of company-specific risk factor in calculating taxpayer's cost of equity;
- Tax Court failed to adequately explain its determination of beta factors used in calculating taxpayer's cost of equity, thus requiring remand for further explanation;
- Evidence supported Tax Court's rejection of build-up method of calculating taxpayer's cost of equity;
- General evidentiary principles, rather than heightened standard, applied to determination of whether taxpayer demonstrated external obsolescence, abrogating *Guardian Energy, LLC v. Cty. of Waseca*, 2014 WL 7476215, *Am. Crystal Sugar Co. v. Cty. of Polk*, 2009 WL 2431376;
- Taxpayer's intangible assets and working capital were exempt from taxation;
- Taxpayer acted within its discretion in deviating from formula for making specific deductions under regulation;
- Evidence supported Tax Court's use of 5% deductions for working capital and intangible assets; and
- Tax Court did not clearly err in declining to consider prior sale when estimating market value of system.

Tax Court's decision to exclude company-specific risk factor from its calculation of cost of equity for taxpayer, a natural-gas utility, as a component used to calculate value of pipeline distribution system under income approach to valuation of system for purposes of taxing personal property, was factual determination subject to clear error standard of review, not legal issue subject to de novo standard of review. Tax Court excluded company-specific risk factor from taxpayer's cost of equity based on lack of evidentiary support in record for proposition that taxpayer's business was riskier than the market, not because it determined, as a matter of law, that a regulated entity's cost of equity could never be augmented to account for additional risk.

Evidence supported Tax Court's exclusion of company-specific risk factors from calculation of cost of equity for taxpayer, a natural-gas utility, as component used to calculate value of pipeline distribution system under income approach for purposes of taxing personal property, though taxpayer's expert appraiser opined that addition of risk factor to cost of equity for small, undiversified firms was appropriate based on business valuation publication. Independent appraiser testified that there was no conclusive empirical evidence supporting risk premium, and Department of Revenue's employee largely agreed with independent appraiser, stating that he had not seen support for application of additional risk factor other than one relied on by taxpayer's expert.

Tax Court, in calculating taxpayer's cost of equity, as component used to calculate value of taxpayer's natural gas pipeline distribution system under income approach for purposes of taxing personal property, failed to adequately explain adoption of beta factor of less than one to account for relative volatility of specific investment compared to volatility of market as whole, and thus remand was warranted for further explanation. Other than stating that beta factor was less than one for each tax year in question, Tax Court did not specify value of beta factors it used for each year, much less explain how or why it selected them.

Evidence supported Tax Court's decision to reject build-up method of calculating cost of equity for taxpayer, a natural-gas utility, as component used to calculate value of pipeline distribution system under income approach to valuation for purposes of taxing personal property, though taxpayer's expert incorporated build-up method into his calculation. Independent appraiser identified problems with use of build-up method by taxpayer's appraiser, and nothing relied on by taxpayer contradicted independent appraiser's testimony regarding appropriate use of build-up method.

General evidentiary principles, rather than heightened standard requiring taxpayer claiming external obsolescence for natural gas pipeline distribution system to offer probative evidence of cause of claimed obsolescence, quantity of obsolescence, and that asserted cause of obsolescence actual affected subject property, applied to determination of whether system suffered from external obsolescence, so as to support downward adjustment to estimated value of system under cost approach to valuation for purposes of taxing personal property. Fact that taxpayer could not identify specific causes of external obsolescence and precisely calculate contribution of each to decreased revenues or profit margins did not mean that property did not suffer from external obsolescence, and external obsolescence could exist and be difficult to quantify, resulting in variation amongst experts in their estimation of impact of external factors on fair market value of certain properties; abrogating *Guardian Energy, LLC v. Cty. of Waseca*, 2014 WL 7476215; *Am. Crystal Sugar Co. v. Cty. of Polk*, 2009 WL 2431376.

Intangible property, including intangible assets and working capital, of taxpayer, a natural-gas utility, was not subject to tax as personal property under statute and relevant regulations granting Commissioner authority to tax pipeline systems' mains, pipes, and equipment attached thereto, and thus was required to be deducted from valuation of taxpayer's pipeline distribution system under income approach for valuation of property, though Commissioner of Revenue asserted intangible assets and working capital were taxable as reflecting going-concern value of property. Statute and relevant regulations allowed Commissioner to tax only tangible property, and deduction for intangible assets did not reduce taxpayer's going-concern value.

Tax Court, in determining valuation of taxpayer's natural gas pipeline distribution system under income approach for purposes of taxing personal property, acted within its discretion in making specific deductions for value of taxpayer's nonoperating and tax-exempt property, namely deductions of 5% for working capital and 5% for intangible assets, from income indicators of value, rather than following process set forth in regulations and making deductions after each indicators of value had been considered and weighed in calculating property's unit value, since regulations allowed for exercise of discretion when deviating from formula would lead to more accurate valuation.

Tax Court did not clearly err when it declined to consider prior sale of natural gas pipeline distribution system to taxpayer in calculating estimated value of system under market approach for valuing pipeline for purposes of taxing personal property. Taxpayer's purchase did not just include system, purchase price captured overall value of entire enterprise, including intangible assets, goodwill, investments, and working capital, some of which was nontaxable, as well as appliance-repair business that was completely separate from system, trial court was authorized to reject market approach after determining it was unreliable and unhelpful, and experts did not rely on market approach or sale in their valuation analyses.

NABL: Tax Reform On Its Way.

The election of Donald Trump and the Republicans holding their majorities in the House of Representatives and the Senate means that there will be an effort, probably a successful one, to enact tax reform. The exemption of interest on state and local obligations is at serious risk of being curtailed or even eliminated.

The Trump campaign put out its tax reform proposals that largely mirrored the tax reform plans put out by the House Republican leadership earlier in the year. Neither mentions municipal bonds, but the House proposal does include a provision that says that interest would have a 50 percent exclusion. It is unclear whether this refers just to currently taxable interest or to all interest, including interest on state and local obligations. It is also possible that some version of the proposals by the Obama administration to cap the value of the tax exemption at the 28 percent bracket could be proposed.

NABL members should contact their members of Congress, and urge their issuers clients to do so also, and make sure they understand the importance of municipal bonds. NABL has a tax reform resource page with information and sample letters.

Read more here.

TAX - WEST VIRGINIA

University Park at Evansdale, LLC v. Musick

Supreme Court of Appeals of West Virginia - October 26, 2016 - S.E.2d - 2016 WL 6407491

Taxpayer appealed decision of county commission, sitting as board of equalization and review (BER), which determined that taxpayer's protest to county assessor's assessment of its leasehold interest in property located on campus of State University was issue of taxability, rather than valuation, reviewable only by Tax Commissioner.

The Circuit Court denied petition for appeal. Taxpayer appealed.

The Supreme Court of Appeals held that taxpayer's challenge to assessment of its leasehold interest on the basis that leasehold purportedly did not have separate, independent value from freehold estate presented issue of valuation, rather than taxability, and thus was reviewable by BER, rather than by Tax Commissioner.

Although taxpayer alleged that leasehold's value was $0 resulting in lack of taxability, value of leasehold was threshold issue distinct from taxability, and taxpayer did not contend that its property was exempt from taxation.

An Open Letter to the IRS on Revenue Procedure 2016-44: Squire Patton Boggs

Dear Internal Revenue Service:

At the Bond Attorneys' Workshop this past October, certain of your officials indicated that you will be considering the issuance of clarifications and amendments of Revenue Procedure 2016-44 to address concerns that have been raised about particular provisions of this Revenue Procedure (which, by and large, is an excellent piece of guidance regarding which management contracts will not result in private business use of facilities financed by tax-exempt bonds). These officials indicated that there was no intent to change any law under the safe harbors from private business use for management contracts and that continuity was intended between Revenue Procedure 2016-44 and the safe harbors set forth in Revenue Procedure 97-13 (which is superseded by Rev. Proc. 2016-44).

When you issue these clarifications and amendments of Rev. Proc. 2016-44, please don't forget to address the concern raised by The Public Finance Tax Blog on September 27, 2016.

As detailed in that post, a manager is treated under Rev. Proc. 2016-44 as receiving compensation from the qualified user of the managed facility if the qualified user reimburses the actual and direct expenses (and related administrative overhead expenses) paid by the manager. Revenue Procedure 2016-44 further provides that the reimbursement of actual and direct expenses paid by the manager to unrelated parties is disregarded as compensation for purposes of determining whether the management contract attempts an impermissible sharing of net profits of the bond-financed facility through the payment of compensation that takes into account both the revenues and expenses of the managed facility. However, in direct contrast to Rev. Proc. 97-13, as interpreted by Private Letter Rulings 200222006 and 201145005, Rev. Proc. 2016-44 expressly provides that an employee of the manager is not an unrelated party to the manager. A literal interpretation of Rev. Proc. 2016-44 could therefore result in the conclusion that a manager of a tax-exempt bond-financed facility shares in the net profits of that facility in the not-uncommon arrangement where the manager is reimbursed for its employee expenses and also receives a percentage of the managed facility's gross revenues.

Subsequent to the post on The Public Finance Tax Blog, you issued Private Letter Ruling 201641002 on October 7, 2016, which continues the trend established by Private Letter Rulings 200222006 and 201145005 that the reimbursement of a manager's direct and actual employee expenses is disregarded as compensation to the manager under Rev. Proc. 97-13. Given your statements at the Bond Attorneys' Workshop that Rev. Proc. 2016-44 was not intended to effect a change in law and that continuity between Rev. Proc. 2016-44 and Rev. Proc. 97-13 was instead intended, please include in your amendments of Rev. Proc. 2016-44 an amendment to treat a manager's employees as unrelated to the manager so that the reimbursement of the manager's direct and actual employee expenses does not result in the conclusion that the manager shares in the net profits of the managed facility if the manager is reimbursed for such expenses and also receives a percentage of the facility's gross revenues.

Sincerely,

Everyone Who Cares About Good Administrative Guidance

Squire Patton Boggs

The Public Finance Tax Blog

By Michael Cullers on November 16, 2016

Arizona Court Of Appeals Permits Utility To Seek Preemption Of State Property Taxes On Power Plant Located On Tribal Land.

On November 3, 2016, the Arizona Court of Appeals allowed South Point Energy Center, LLC ("South Point") to pursue challenges to the assessment of property taxes for tax years 2010 and 2011 and for 2012 and 2013 on its power plant on the Fort Mojave Indian Reservation. The appeals court reversed the decision of the Arizona Tax Court that granted summary judgment to the Arizona Department of Revenue and Mohave County. The Tax Court held that a prior unsuccessful challenge to property tax assessments levied against the plant for 2003 and 2004 barred South Point from pursuing the current challenges. The opinion, *South Point Energy Center, LLC v. ADOR/Mohave County*, Case Nos. 1 CA-TX 15-0005, 1 CA-TX 15-0006 (Consolidated), can be accessed on the Arizona Court of Appeals at the website here.

South Point filed its actions arguing that federal law preempted the assessments, making the assessments at issue erroneously assessed taxes (A.R.S. § 42-16524(G)), and that, under A.R.S. § 42-11005, it could lawfully seek to recover illegally collected taxes. The defendants argued that, because the plant's prior owner, Calpine, had unsuccessfully challenged assessments against the plant, South Point was precluded from seeking relief for the later tax years. Calpine had argued that, for Arizona property tax purposes, the plant should have been deemed to be owned by the Tribe and, therefore, not subject to Arizona property taxation. The tax court denied Calpine's challenge, ruling that, because Calpine owned the improvements on the land, the improvements were subject to taxation. *Calpine Constr. Fin. Co. v. Ariz. Dep't of Revenue*, 221 Ariz. 244, 246, 248-49, ¶¶ 1, 17-22 (App. 2009). The Arizona Supreme Court denied Calpine's petition for review.

In view of this history of challenges to property tax assessments against the plant, the Defendants argued that, because Calpine could have raised the preemption argument in the prior proceedings, South Point was collaterally estopped from raising the preemption and illegal tax arguments for later tax years. The Tax Court accepted this argument and entered summary judgment for the defendants. On appeal, South Point argued that collateral estoppel did not bar its pursuit of legal theories neither raised nor adjudicated in the prior litigation. The Court of Appeals accepted South Point's arguments. It held that, because Calpine did not litigate the question of preemption, "the fact that it could have been litigated is of no consequence here." South Point at ¶11 (emphasis in original). The Court further held that South Point could challenge whether the assessment was erroneous under the "error" correction statute, reasoning that, "[i]f the correct property tax rate is zero because of preemption, the imposition of any other tax rate is necessarily an illegal tax rate, and constitutes 'error' under the statute." South Point at ¶14. The court remanded the proceedings to Tax Court to resolve the preemption issues.

In sustaining South Point's appeal, the Court of Appeals did not resolve South Point's preemption argument. The court stated that "[w]e offer no opinion as to the merits of South Point's preemption theory. But because the issue was not previously litigated, issue preclusion cannot bar it." Id. at ¶11.

On remand, South Point will have the ability to litigate the preemption question. The owners of power plants – and their successors in interest – will be well-served to be precise in the issues raised before the tax court and thus certain that Arizona law permits plant owners to bring later challenges on new legal theories that were both not raised and not resolved on the merits in earlier proceedings.

Last Updated: November 10 2016

Article by Gregory Y. Harris

Lewis Roca Rothgerber Christie LLP

TAX - WISCONSIN

Medical College of Wisconsin Affiliate Hospitals, Inc. v. United States

United States District Court, E.D. Wisconsin - September 14, 2016 - Slip Copy - 2016 WL 4916811 - 118 A.F.T.R.2d 2016-5798 - 2016-2 USTC P 50, 409

The Medical College of Wisconsin Affiliated Hospitals, Inc. overpaid its Federal Insurance Contributions Act (FICA) tax and received a tax refund with interest calculated at the rate for corporations. It filed this lawsuit to recover additional interest at the higher, noncorporate rate. IRC § 6621(a)(1)

"Under § 6621(a)(1) noncorporate taxpayers receive interest on tax refunds at a higher rate than corporate taxpayers receive. Hence, the question here is whether for purposes of IRC § 6621(a)(1) a § 501(c)(3) nonprofit is considered to be a corporation. When the pending summary judgment motions were briefed initially, the identical legal issue had been decided in the government's favor by district courts in New York and Michigan and presented on appeal to the Second and Sixth Circuits. Both circuit courts have since issued their decisions affirming the judgments in the government's favor."

"This court has fully considered the parties' arguments here, the statutory and regulatory language cited, the opinions of the two district courts, the Second Circuit's Maimonides Medical Center v. United States, 809 F.3d 85 (2d Cir. 2015), the Sixth Circuit's United States v. Detroit Medical Center, No. 15-1279, ––– F.3d ––––, 2016 WL 4376431 (6th Cir. Aug. 17, 2016), the Court of Federal Claims' Eaglehawk Carbon, Inc. v. United States, 122 Fed. Cl. 209 (2015), and the Tax Court's Garwood Irrigation Co. v. Commissioner of Internal Revenue, 126 T.C. 233 (2006). Because this court's determination is in accord with the decisions of the Second and Sixth Circuit, there is no need to add a lengthy opinion to the mix. In short, this court rejects the Hospital's argument that the parenthetical in the "flush language" of § 66211 incorporates the "C corporation" limitation of (c)(3)(A), notwithstanding that the flush language cites only "(c)(3)." The flush-language parenthetical more naturally refers only to the definition of "taxable period" in (c)(3)(B), especially as the flush language does not use the defined term "large corporate underpayment" (or, as possibly adjusted, "large corporate overpayment"). And this court is unpersuaded that perfect symmetry between the overpayment and underpayment provisions was intended by Congress. Instead, it appears that where Congress intended to use "C corporation" in § 6621 it did so and where it used only "corporation" it included all corporations—C, S, and § 501(c)(3) together. Although the Hospital's policy arguments for a higher interest rate for refunds to nonprofits have merit, those arguments are better aimed at Congress. Here the text of the statute expresses Congress's intent. For these reasons and the reasons discussed by the Second Circuit and Sixth Circuit in Maimonides and Detroit Medical College."

Trends And Tips – Tax Equity For Mid-Market Energy Projects: Mintz, Levin

Last week's "Financing Renewable Energy" tax credit conference, by Novogradac and Company, affirmed some market trends that we have seen in recent project finance deals. Perhaps most striking was the slow expansion of small and mid-market tax equity investors, compared to their counterparts upmarket. The result is that developers of projects and project portfolios under $50 million may need to look harder to find the right partner to monetize their tax credits.

Looking back even a couple of years, we saw a tax equity market that was dominated by a small handful of large players, most of whom were focused on big investments investing large amounts of capital into utility-scale projects. Today, the number of investors has increased (JPMorgan Chase reports at least 20 wind investors and 28 solar investors in 2015), as has the amount of tax equity investment (up 14% between 2014 and 2015, according to JPMorgan Chase). Our anecdotal experience, affirmed by investors and developers we have spoken with, is that the bulk of that expansion has been among large banks, insurers and Fortune 500-sized corporate investors, which have grown increasingly comfortable with the risk profile of renewable energy projects and the diligence required to evaluate a prospective investment.

A similar trend has been lagging among smaller investors. Smaller tax equity investments are not necessarily simpler to diligence, negotiate or document than large deals, and renewable energy continues to be seen as a "new" industry to many banks, insurance companies and other potential investors. Despite this friction slowing the entry of new investors into the marketplace, there are some encouraging signs. First, we see evidence of increasing cross-over from investors in other tax credit-driven spaces (new market, low income housing, etc.). Second, when they do enter the market, smaller investors are often more nimble at the investment-stage and can be better at building ongoing relationships that can ease future investor interactions (e.g., when seeking consent to refinance project debt).

These trends suggest some actionable advice for mid-market project sponsors:

1. Don't be afraid to look outside the usual pool of energy tax credit investors. Cross-over investors have existing experience with some of the same structures used in Section 45 and Section 48 investments, but there is an educational process to help them become comfortable with the diligence process and risk profile for energy projects. A willingness to work through that learning curve may open the door to new investor relationships.
2. Look for opportunities to build long-term relationship that can support multiple deals. It is an unfortunate reality that doing an $8 million tax equity deal is not one tenth as complicated and costly as doing an $80 million deal. Working with an investor that can be a longer-term partner creates potential economies of scale as the parties replicate and recycle investment terms, documents and diligence standards across multiple deals.
3. Consider who will be a strong partner after closing. A typical tax equity investor will have consent rights over material events in a project's life, such as a debt refinancing. Demands for hefty consent fees, lengthy diligence reviews and other requirements can strain the relationship between a project sponsor and the tax equity investor. If the parties have a relationship that extends beyond the immediate project (see #2 above), then motivations will be better aligned at these important milestones.

Last Updated: November 9 2016

Article by Eric Macaux

Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C.

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.

[Management Contracts For Projects Financed With Tax-Exempt Bonds: Faegre]

Government and nonprofit borrowers recently received some favorable new rules from the IRS regarding management contracts for projects financed with tax-exempt bonds. Rev. Proc. 2016-44 provides flexible guidance to determine when management contracts and similar service agreements involve problematic private use. It establishes a new safe harbor for identifying whether such contracts exceed the private business use limitation applicable to governmental bonds and tax-exempt bonds issued on behalf of 501(c)(3) organizations.

The new safe harbor is effective for agreements entered into on or after August 22, but issuers can apply it to any management contract entered into before that date.

Rev. Proc. 2016-44 replaces Rev. Proc. 97-13 which established separate safe harbors for management contracts based on the term of the contract. For longer-term contracts it required that a minimum percentage of the manager's compensation be based on a fixed fee depending on the length of the contract. These formulaic tests are replaced with a flexible safe harbor for contracts up to 30 years based on such things as control, risk of loss, economic levies of managed projects and consistency of tax positions taken by the service provider. The general principle that compensation may not be based on a share of the net profits from the managed property is retained.

The other features of a safe-harbor management contract are as follows:

- Compensation may be fixed or variable, but must be reasonable compensation for the service provided. Incentive compensation based on the service provider's performance in meeting one or more standards that measure quality of services, performance or productivity is expressly permitted.
- The contract must not require the service provider to share the burden of net losses from operation of the managed property.
- The term of the contract, including renewal options, may not exceed the lesser of 30 years or 80% of the weighted average reasonably expected economic life of the managed property.
- The service recipient must exercise significant control over the use of the managed property.
- The service recipient must bear the risk of loss upon damage or destruction of the managed property.
- The service provider must not take a tax position inconsistent with being a service provider, such as taking depreciation, investment tax credits or rent deductions.
- The service provider must not have a role or relationship with the service recipient that limits the service recipient's ability to exercise its rights under the contract. A safe harbor is provided if (a) no more than 20% of the voting power of the governing body of the service recipient is vested in the directors, officers, shareholders, partners, members and employees of the service provider; (b) the governing body of the service recipient does not include the chief executive officer of the service provider or the chair of the service provider's governing body; and (c) the chief executive officer of the service provider is not the chief executive officer of the service recipient or any of its related parties.

The economic life restriction in the new safe harbor applies to the "managed property" under both long-term and short-term contracts, while the economic life restriction in Rev. Proc. 97-13 applied to "financed property" under only long-term contracts. Managed property is defined as the portion of a project (as defined in the regulations) with respect to which the services are provided. These wording changes may have unexpected substantive consequences, including possibly requiring issuers to determine the scope of the project being financed and the useful life of property other than financed property and regardless of the term of the contract.

While the new safe harbor can be applied to existing contracts, the safe harbors of Rev. Proc. 97-13 may be applied to a contract entered into before August 18, 2017, and that is not materially modified or extended on or after August 18, 2017, other than pursuant to a renewal option.

Last Updated: November 8 2016

Article by Stephen C. Rosholt and Stefanie N. Galey

Faegre Baker Daniels LLP

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.

An Inconvenience of Qualified Equity: Squire Patton Boggs

Like me, at some point in your childhood, you were probably told not to "look the gift horse in the mouth." After reading this blog post, the same could be said to me. We have written in great detail (see here, here, and here) about the increased flexibility afforded issuers by the recently promulgated Final Treasury Regulations governing, among other things, allocating proceeds of tax-exempt bonds and other sources to projects that involve both qualified and private uses (the "Allocation and Accounting Regulations"). The Allocation and Accounting Regulations permit "qualified equity" to be allocated first to private business use and then to governmental use. As discussed in the prior posts, "qualified equity" is essentially defined as amounts other than tax-exempt proceeds. However, there are timing and other restrictions on what is eligible to be considered "qualified equity."[1] These restrictions have led to an inconvenience that is the topic of this blog.

The reimbursement window is larger than the qualified equity window

Qualified equity includes amounts other than proceeds of tax-exempt bonds that are spent on the same eligible mixed-use project as the proceeds of the applicable bonds. To be spent on the same eligible mixed-use project, the qualified equity must be spent pursuant to the "same plan of financing."

The preamble to the Allocation and Accounting Regulations says that qualified equity is spent under the same plan of financing if

> "the qualified equity is spent on capital expenditures of the project no earlier than the earliest date on which the expenditure would be eligible for reimbursement were the bonds from which the proceeds are derived issued as reimbursement bonds . . . ."

The rule, as enunciated in the preamble, makes perfect sense. However, the actual language of the rule in the Allocation and the Accounting Regulations says that qualified equity is spent under the same "same plan of financing" if

> "the qualified equity pays for capital expenditures of the project on a date that is no earlier than a date on which such expenditures would be eligible for reimbursement by proceeds of the applicable bonds under [Regulations] 1.150-2(d)(2) . . . ."

Regulations 1.150-2(d)(2) says that a reimbursement allocation must be made not later than 18 months after the later of (a) the date of the original expenditure or (b) the date the project is placed in service or abandoned, but in no event more than 3 years after the original expenditure is paid (collectively, the "Reimbursement Period").

If you are reading this blog, you may know that there are certain expenditures that are eligible to be reimbursed even though they were paid before the Reimbursement Period began. Specifically, a de minimis amount of pre-Reimbursement Period expenditures may be reimbursed as well as a certain amount of preliminary expenditures. Therefore, the window of time during which qualified equity can be used to finance a project begins after the period of time that expenditures would be eligible to be reimbursed under the reimbursement rules!

In reality, this discrepancy is less significant than it may initially seem. As discussed in the previous paragraph, the pre-Reimbursement Period expenditures are eligible for reimbursement even though the amounts paid to finance such expenditures are not eligible to be qualified equity. Therefore, a reimbursement allocation could be made on or after the issue date and the issuer could be reimbursed for the amount of equity that it used to finance the pre-Reimbursement Period expenditures. The issuer could then contribute the equity made available by the reimbursement allocation to finance a portion of the mixed-use project. Because the equity contribution occurs within the Reimbursement Period (assuming the mixed-use project has not yet been placed in service), it is contributed pursuant to the same plan of financing.

[1] As a technical matter, the restrictions do not preclude amounts other than tax-exempt bond proceeds from being qualified equity; rather, the restrictions prohibit the qualified equity from financing a project under the same plan of financing.

By Joel Swearingen on November 11, 2016

Squire Patton Boggs

TAX - OHIO

New York Frozen Foods, Inc. v. Bedford Hts. Income Tax Bd. of Rev.

Supreme Court of Ohio - November 3, 2016 - N.E.3d - 2016 WL 6519128 - 2016 -Ohio- 7582

Municipal income taxpayer sought judicial review of decision of the Board of Tax Appeals (BTA) affirming decisions of the Regional Income Tax Agency (RITA) and municipal income tax board of review denying taxpayer's refund claim.

The Supreme Court of Ohio held that:

- Change from filing separate return to filing consolidated return was prohibited change in method of accounting, and
- State statute did not preempt city ordinance placing limitation on refund claims.

Municipal income taxpayer's change from filing a separate return to filing a consolidated return was a change in method of accounting prohibited by city ordinance in pursuing a refund claim. Amended return took broadly different approach to basic computation of taxable income, and term "method of accounting" was not limited to only cash versus accrual accounting under federal law.

State statute governing municipal income taxes did not preempt municipal ordinance placing limitation on refund claims to prohibit amendment of returns to change method of accounting. Plain language of the state law did not expressly override city's power to bar a change of accounting or apportionment method when filing an amended return, and preemption of local tax law could not be accomplished impliedly.

Trump's Tax, Infrastructure Plans Jeopardize Exemption for Munis.

WASHINGTON — Donald Trump's presidency and the Republican-controlled Congress set the stage for historic tax reform and increased spending on infrastructure next year, which has the potential to jeopardize the tax exemption for municipal bonds, according to market participants.

Both Trump and House Republicans are pushing for tax reform plans that would lower individual and corporate tax rates and broaden the tax base, repealing or restricting tax deductions and exemptions.

"The win, because it means that the GOP will control the executive office and both houses of Congress, almost surely means the next Congress will act on major tax legislation focused on cutting rates," said Frank Shafroth, director of the Center for State and Local Government Leadership at George Mason University. "I would guess it will be the most significant, early bill signed into law by the new president."

"They're going to strike while the iron is hot," agreed Chuck Samuels, a partner at Mintz Levin.

They could propose tax reform legislation that would be the most significant since the 1986 Tax Reform Act, which contained major restrictions for municipal bonds, said Shafroth.

The Trump and House Republican plans do not contain many details and do not specify what deductions might be repealed. Market participants worry that the exclusion on interest for tax-exempt bonds could be capped or eliminated to raise revenue for other tax reforms or increased infrastructure spending.

"In the last 24 hours, tax exemption under possible tax reform in 2017 or 2018 has gone from a concern/priority to 'hair on fire,'" said John Vahey, managing director of federal policy for Bond Dealers of America.

Charlie Henck, a partner with Ballard Spahr here, said it's a given that the tax exemption for municipal bonds will be on the table during the tax reform debate. "In the years I've been watching Congress and all of the new administrations, you can take it as a given that the economic folks at the Treasury Department and the Joint Committee on Taxation will put the tax exemption for munis on their hit list," Henck said. "It's generally thought by those folks to be an inefficient incentive."

Henck said he expects state and local groups to rally together to maintain the tax-exemption for muni bond interest, which is currently excluded from taxes.

Infrastructure

Trump's victory speech placed heavy emphasis on his plans to shore up the nation's infrastructure. "We are going to fix our inner cities and rebuild our highways, bridges, tunnels, airports, schools, hospitals," he said. "We're going to rebuild our infrastructure, which will become, by the way, second to none. And we will put millions of our people to work as we rebuild it."

Trump has proposed a $1 trillion, 10-year infrastructure plan. While that would normally be strongly supported by state and local governments and bankers, there is some uncertainty about the plan's reliance on $137 billion of tax credits that Trump would ask Congress to authorize.

"The little we know about Trump's plan is that it focuses on tax credits," said Jessica Giroux, BDA's general counsel. “Our concern is that it says nothing about munis. But with lowering individual rates under tax reform we wonder if munis are going to be as attractive anymore.”

Trump’s lack of detail in how he would raise revenue for his proposed infrastructure spending as well as other unspecified changes to deductions is concerning, said Vahey.

“This is going to be a very big item for the muni market in the coming years,” he added. “With a unified executive branch and legislative branch, it’s a whole new ballgame.”

Trump advisors Wilbur Ross, a billionaire private-equity investor, and Peter Navarro, a professor at the University of California at Irvine, said the infrastructure plan’s tax credits could be used by investors to leverage $167 billion in private funds.

Companies taking advantage of the tax credits would be able to borrow money on the private market at low interest rates to finance $1 trillion of projects without the need for any new taxes, they said.

“Trump’s plan will harness market forces to help raise construction funds by incentivizing private sector investors through tax credits, thereby revolutionizing American infrastructure finance,” Navarro said.

Companies would be able to bring overseas earnings back to the U.S. at Trump’s proposed reduced tax rate of 10% rather than the current 35%. With the credits, companies could avoid any tax liability by investing $122 million of the repatriated profits in infrastructure projects, Ross and Navarro said.

Repatriation would take away a significant amount of tax revenue available for tax reform, thereby increasing the pressure on Congress to look even harder at cutting tax deductions and exemptions.

The Joint Committee on Taxation has estimated that American companies hold a total of $2.6 trillion of foreign income in overseas banks.

Transportation groups also have some concerns about Trump’s infrastructure plan. Bud Wright, executive director of the American Association of State Highway and Transportation Officials, said tax credits are not a long-term solution.

“We’re sort of agnostic about the tax credits,” Wright said. “We’re not opposed to the idea, but it is not the long-term funding solution that we need to repair the deficit in the Highway Trust Fund.”

Federal tax credits are not transportation user fees, he said.

“A one-off, short-term type of program like that would be useful but it does not do anything for the long-term sustainability of federal transportation funding,” Wright said. “Corporate tax reform is not really a transportation issue either, but in some circles it has been linked to infrastructure funding as well. Again, it’s not something we oppose but it is not a solution.”

However, Wright concedes that Increases in the federal gasoline tax are not likely. “The fuel tax is the best understood and most administratively effective revenue source there is but it is about as politically volatile as any issue I’ve seen in Washington,” he said. “That goes for Democrats as well as Republicans. There’s just a knee-jerk reaction to oppose it.”

Jim Tymon, chief operating officer and director of policy at AASHTO, said, “I think we’ll see an infrastructure package coming out of Congress, probably not quickly but certainly within the first year.”

As always, the sticking point will be how to pay for increased infrastructure spending, he said. "We'll have to see what sort of pay-fors and offsets are available and acceptable," Tymon said.

Regulatory Moratorium

Trump has also proposed a moratorium on new regulations, which could thwart the Municipal Securities Rulemaking Board initiatives on markup disclosure, pre-trade price transparency, and syndicate practices. He has also joined Republicans in calling for a rollback of some existing laws and rules, such as the Dodd-Frank Act, which provided more funding for the MSRB from the enforcement of muni rule violations and subjected muni advisors to federal oversight and regulation.

The moratorium and rollback raise questions about whether the Securities and Exchange Commission and MSRB will continue to move forward with muni market initiatives, said Vahey.

"As of right now, if you look at the types of things that have been impacting the muni market, especially on the retail and regulatory side, they're all born out of the 2012 [Report on the Municipal Market]," he said. The report came out of the SEC with bipartisan support, but the expected changeover in the administration raises questions about whether such support will continue.

Vahey said that from BDA's perspective, the biggest issue with regulation specifically in the muni market has been its scope, pace, and the amount of change that has come in the last five years.

"Could dealers use a breather from reg compliance changes and time to adapt to a new environment? Yes," Vahey said. "Is there at the same time some potential negatives out there to a regulatory moratorium across the entire economy? Potentially, yeah."

Matt Fabian, a partner with Municipal Market Analytics, said that it is easier to imagine Trump would appoint industry-friendly individuals to fill the chair and vacant commissioner slots at the SEC. Mary Jo White is expected to step down as chairwoman.

Uncertainty

But one of the biggest concerns about Trump, reflected in the plummeting financial markets Tuesday night and Wednesday, is the uncertainty surrounding him.

Fitch Ratings said Trump's policies would be "negative for U.S. public finances" because of uncertainties about the detail of his proposals, the degree to which he'll promote them, and his ability to implement them. Senate Democrats will still be able to filibuster Republican legislation they don't like, the rating agency pointed out.

Samuels stressed that Trump is a "great unknown" for the municipal market because of his campaign's overall lack of detail regarding economic advisors and plans. "We really don't understand who will be running economic and tax policy," he said. "The situation is very unclear."

Vahey said, "He's not an in-the-box Republican, adding, "He doesn't have a voting record and is very light on details."

The Bond Buyer

By Evan Fallor, Jack Casey, Jim Watts, and Lynn Hume

November 9, 2016

TAX - NEW YORK

T-Mobile Northeast, LLC v. DeBellis

Supreme Court, Appellate Division, Second Department, New York - October 26, 2016 - N.Y.S.3d - 2016 WL 6270168 - 2016 N.Y. Slip Op. 07031

Cellular telephone service provider brought hybrid article 78 proceeding and declaratory judgment action against city and school district, seeking to compel city to determine and approve provider's petitions for property tax refunds for tax paid related to its equipment and antennas housed on rooftops of office buildings within its service area.

The Supreme Court, Westchester County, denied the petition and dismissed the proceeding. Provider appealed.

The Supreme Court, Appellate Division, held that:

- Fiber optic and coaxial cables constituted taxable real property;
- Base transceiver station cabinets constituted taxable real property;
- Rooftop antennas were fixtures that were taxable as real property.

Fiber optic and coaxial cables, as well as connections between cellular telephone services provider's equipment housed on rooftops of buildings in its service area and that of local exchanger carrier, were "lines" or "wires" under tax statute permitting taxation of real property, and thus constituted taxable real property.

Cellular telephone service provider's base transceiver station cabinets housed on rooftops of buildings in its service area constituted "inclosures for electrical conductors" within meaning of statute permitting taxation of such inclosures as real property, and thus constituted taxable real property.

Cellular telephone provider's rooftop antennas, which were flat and four to five feet in both length and width, could properly be characterized as "inclosures for electrical conductors" within meaning of tax statute permitting taxation of real property, inasmuch as they were a part of base transceiver station cabinet, and thus constituted taxable real property.

Cellular telephone provider's rooftop antennas constituted fixtures within meaning of tax statute permitting taxation of real property, and thus constituted taxable real property. Equipment was fastened to host buildings by bolts, frames, pipes, and brackets, and was weighted down with I-beams and cinder blocks, and provider demonstrated its intent to make equipment permanent for term of the leasehold.

IRS Releases Three-Part Video Series on Conduit Issuers.

Conduit Issuers for Tax-exempt Financings – Overview

Conduit Issuer Responsibilities

Conduit Issuer Policy and Procedural Considerations

Bond Attorneys' Workshop Round-up: Squire Patton Boggs

The National Association of Bond Lawyers recently held its 41st Annual Bond Attorneys' Workshop in Chicago. Below are some odds and ends from the conference.

1. I think I've finally nailed the punctuation on "Bond Attorneys' Workshop," a grammatical conundrum as bedeviling as the proper punctuation of the phrase "physicians/physician's/physicians' group contract" from the world of private business use.
2. From the IRS Tax-Exempt Bond Office (TEB), we learned that TEB (and the IRS as a whole) is implementing a program called the "IRS Future State Initiative," which is billed as addressing a need "to take advantage of the latest technology to enhance the entire taxpayer experience . . . in a way that meets the needs of taxpayers and the tax community in an efficient and effective manner." The website includes several "vignettes" that tell us the story of how fictional taxpayers would fare under the new program when the IRS fully implements it, including the tale of "Sheila," a state government employee in charge of making her state's employment tax payments. Although her story doesn't deal with tax-exempt bonds, you can read it and see by analogy how it might affect state and local governmental issuers.
3. "Future State" will manifest itself in several ways, including increased use of the website, increased use of what is called "prefiling education," and increased use of "interactive" forms. The IRS already uses an interactive Form 8038-CP (that's the one you've been using, right?), which is the form that issuers should use to request direct payments for tax-exempt bonds, which we've written about before. The Form is "interactive" in the sense that it will tell you if there are internal inconsistencies (for example, an interest payment date that is three years prior to the issuance date). It was noted at the conference that error rates have gone down significantly on Form 8038-CP since the IRS started using it. Expanding the interactive forms to the other 8038s would be a welcome development.
4. On the IRS's Voluntary Closing Agreement Program, it was noted that the IRS has received fewer requests by a significant margin, even though the IRS says that it has increased its efficiency in processing the requests and decreased the time it takes to process them. (One wonders whether the two points are related, that is, whether the drive for "consistency," which will necessarily lead to payment and bond redemption amounts that aren't tailored to each issuer's particular facts, has contributed to decreased interest in the program.)
5. You may have seen in The Bond Buyer that the IRS released "interim guidance" to examining agents that advises when agents may close an exam during an audit when the issuer redeems all of the bonds with funds other than an issue of tax-exempt bonds. (Theoretically, the IRS could assess income tax on interest on the bonds for years that would still be open under the bondholders' statute of limitations, if it were able to successfully assert that interest on the bonds is taxable.)
6. Where in the past there have been significant guidance projects that have been released soon before the conference, this year, there were no new major proposals, nor were there any new developments on the two major currently brewing proposals, which are the proposed (or now re-proposed) issue price regulations and the proposed regulations defining a "political subdivision" that can issue bonds on its own behalf. We were told by Treasury officials that the issue price regulations will be finalized by the end of the year, and that the political subdivision regulations will probably be re-proposed.
7. On Rev. Proc. 2016-44, the new private business use safe harbor, which has now been out for two months, Treasury officials confirmed that many of the concepts that are now explicitly stated in Rev. Proc. 2016-44 come from private letter rulings (or ruling guidelines) and concepts that already lurked in the background of Rev. Proc. 97-13 (as modified by Notice 2014-67). The new revenue procedure also contains provisions that are designed to ensure that the contract in

question is not, in substance, a lease to a private person.

8. What remains unclear is the extent to which Rev. Proc. 97-13 has any continuing vitality once Rev. Proc. 2016-44 finally replaces it, for contracts entered into or materially modified after August 18, 2017. Rev. Proc. 2016-44 clearly states that it "supersedes" Rev. Proc. 97-13, so Rev. Proc. 97-13 will not provide an actual legal safe harbor from private business use beyond that date. Rev. Proc. 2016-44 has been described as "expanding" or "liberalizing" Rev. Proc. 2016-44, and it certainly does that by eliminating the pigeon-holes of compensation and their corresponding permitted contract lengths.
9. But there are aspects of Rev. Proc. 2016-44 that look like they may be more restrictive, too. For example, Rev. Proc. 97-13 did not require service providers to affirmatively agree in the management contract to not take a tax position that would be inconsistent with their status as a service provider. It is likely that service providers would "agree" (in terms of logic) that they should not take a position contrary to their tax status as service providers, but under Rev. Proc. 97-13 they didn't have to say so in the contract.
10. At the conference, Treasury and IRS officials noted that the intent of Rev. Proc. 2016-44 was not to revoke prior rules, and that the intent was to provide continuity to Rev. Proc. 97-13. One option might have been to add the new, expanded safe harbor, with its arguable additional restrictions as the price of admission for the expanded safe harbor, as a "new" safe harbor grafted on to Rev. Proc. 97-13 (in which case it could have been said that Rev. Proc. 2016-44 "amplified" Rev. Proc. 97-13, rather than superseding it). An even better approach would be to amend Rev. Proc. 2016-44 to simply state that any contract that met or meets a Rev. Proc. 97-13 safe harbor will continue to be within a safe harbor from private business use.
11. Finally Treasury and IRS officials again told us that we may finally see the long-awaited final TEFRA regulations, which among other things would allow for TEFRA notices to be published on governmental websites (as well as disseminated through something called a "radio broadcast"), another setback for the much beleaguered print media. If other recent events in Chicago foretell the future, maybe yet another long-awaited event will come to pass.

By Johnny Hutchinson on November 3, 2016

The Public Finance Tax Blog

Squire Patton Boggs

Why New York City Gave Up $3 Billion in 2016.

New York City is the first major government this year to release what it gives up in economic development-related tax incentives to corporations, following new financial reporting requirements. In its annual financial report, the city disclosed that it waived more than $3 billion in potential tax revenue in 2016 alone, mostly in uncollected property taxes.

The tax abatements represent a little under 4 percent of the city's nearly $80 billion in general fund revenue in fiscal 2016, which ended on March 31.

The most expensive abatement was for the commercial conversion program, which cost nearly $1.3 billion in forgone revenue last year. The program encourages new housing in the city by offering a property tax discount on new construction or on commercial space that was converted into residential housing. Developments have to meet certain requirements, like reserving one-fifth of the units for affordable housing.

The Takeaway: New York has an earlier fiscal year than most of the country, so it's not a surprise that it's the first out with its tax incentives data. Still, it's commendable that the city's assessment of its tax abatement program also includes 2015's data, which was [not required] by the new accounting rules. It allows for observers to start tracking trends sooner than previously thought.

The other notable detail from the annual financial report is that of the 11 city programs listed offering abatements, only two of them had any provisions for recapturing the abated taxes. The two programs, which both encourage commercial development, accounted for about $130 million in forgone revenue in 2016. That means that, for the remainder of the $3 billion in abatements, the government has no established means of ensuring the deal continues to be worth the cost. This is likely just the tip of the iceberg of tax giveaways in this country that have few strings attached.

GOVERNING.COM

BY LIZ FARMER | NOVEMBER 4, 2016

Cato: Bonds Are Taxes.

On Nov. 8, voters where I live in Fairfax, Va., will be asked to approve general obligation bonds to finance subway maintenance, park renovations, and other run-of-the-mill local spending. There will be hundreds of similar questions on ballots across the country to issue billions of dollars in new debt.

Voters typically approve state and local bonds by large margins. Bond Buyer data show that bond approval rates in presidential election years have been more than 80 percent. Apparently, voters think that there are prudent and practical reasons for governments to issue general obligation bonds. But there usually aren't.

Using debt allows politicians to claim credit for spending while evading responsibility for the resulting higher taxes, which hit citizens down the road. By putting bonds on the ballot, politicians are really asking voters to hike taxes, to enrich finance industry middlemen, and to make government budgets more complex and opaque.

State and local governments issue bonds to finance infrastructure, such as schools. The interest and principal on bonds is paid back over time from taxes. The states have been issuing debt for infrastructure since at least 1818, when New York floated bonds to finance the Erie Canal.

However, debt is not the only way to pay for investments. Indeed, much of state and local infrastructure is financed on a pay-as-you-go basis. Under that approach, governments construct needed facilities in sequence over time with a portion of annual revenues.

Pay-as-you-go financing is more transparent and less risky than debt financing. The Erie Canal was a success, but it spurred many other states to borrow heavily and spend lavishly on their own, more dubious, canal schemes. Politicians at the time overestimated the demand for canals and underestimated the costs. As a result, most state-sponsored canals turned out to be money-losing failures that damaged state finances.

Those debt-financed failures led to sweeping budget reforms. Nineteen states imposed constitutional limits on government debt issuance between 1840 and 1855, and other states followed in later years. Reformers recognized that political incentives to spend combined with easy access to money is a combustible combination. In recent years, we've seen places such as Greece, Puerto Rico, and

Detroit burn their fiscal houses down from their debt-fueled spending.

Today, all state governments operate within statutory and/or state constitutional limits on debt. But voters should be asking their governments why they need to borrow at all. Why can't they plan ahead for the schools and parks that are needed, and allocate a portion of ongoing tax revenues for construction and renovation?

Debt financing costs more than pay-as-you-go financing because of the interest payments, but also because governments pay fees to the municipal bond industry. Thousands of high-paid underwriters, traders, advisors, bond insurers, and other finance experts are the overhead costs of bond financing. That means billions of dollars a year of taxpayer money going to Wall Street, not to schools and parks.

A further cost of state and local debt is corruption. The municipal bond industry has been plagued by scandals related to political influence. If you Google "muni bonds" and "pay-to-play," you find story after story about finance firms using campaign contributions and other payments to win bond business from government officials.

Debt financing also makes budgeting less transparent to citizens, especially given the complex ways that governments borrow these days. Also, citizens have less appreciation for the costs of government projects if they do not feel the bite of current taxes to pay for them.

Total state and local government debt now totals more than $3 trillion. While some states such as New York are heavily indebted, other states such as Idaho issue very little debt and finance their capital expenditures primarily on a pay-as-you-go basis.

It is true that for particularly large capital projects, general obligation debt may be appropriate in some cases. But if you have bonds on the Nov. 8 ballot where you live, they are probably for routine spending that should be funded by ongoing tax revenues. Next door to Fairfax is Arlington, Va. It has bonds on the ballot next week to fund street paving, park maintenance, playground improvements, school renovations, and similar sorts of projects.

Bonds don't magically make these spending projects free. Instead, the projects will end up costing taxpayers more than they should have because of the debt servicing costs.

I benefit from local parks and schools, but I always vote "no" on bond questions.

The Cato Institute

By Chris Edwards

This article appeared on The Hill (Online) on November 2, 2016.

Chris Edwards is editor of DownsizingGovernment.org at the Cato Institute.

What a Shift In Power in the Senate Could Mean for Munis.

WASHINGTON – A Democratic takeover of the Senate, as has been predicted by some polls, could mean good news for tax reform as well as maintaining the tax exemption of municipal bonds, according to several muni market participants.

Micah Green, a partner with Steptoe and Johnson in Washington, said that the formula to accomplish tax reform after at least six years of debate would be perfect under three very possible conditions.

“If the Senate turns Democrat, the House stays Republican, and Secretary [Hillary] Clinton wins the presidency, what was the makeup of the House and Senate when The Tax Reform Act of 1986 passed?,” he asked, adding, “A Republican president, Republican House and Democratic Senate.”

In addition, Sen. Chuck Schumer, D-N.Y., who is in line to become Senate Majority Leader if the Democrats win the Senate, has made tax reform a top priority, as has House Speaker Paul Ryan, R-Wis., who spearheaded the GOP blueprint for tax reform released this year, he said. This bipartisan agreement is necessary for comprehensive tax reform, Green noted.

“The lesson from ’86 is, if the White House is committed to some form of tax reform discussion, then I think Chuck Schumer and Paul Ryan would try and get it done,” he said. “The pure policy idea of having a serious discussion or action on tax reform is very much in the wheelhouse of both Schumer and Ryan.”

As of Wednesday, Democrats had a 59% chance of taking back the Senate in next week’s election, according to the New York Times, which bases its data on state and national polls. The House of Representatives is widely expected to remain Republican.

Republicans currently hold 54 Senate seats, while Democrats hold 44 and independents hold two. Of the 34 seats up for election next week, 24 are Republican-held. For Democrats to re-take the Senate, they must win 15 seats. To maintain control, Republicans would need to win 21 seats.

Several muni participants have taken note and have begun to analyze how a shift in the balance of power in Congress could shape their goals for the next administration.

John Godfrey, the senior government relations director for the American Public Power Association, said APPA has been in talks with Republicans regarding their blueprint for tax reform released in June, which proposes repealing unnamed special-interest provisions, leading some muni participants to believe the tax-exempt standing of munis could be in jeopardy.

Godfrey said whichever party controls Congress, their message should be consistent: maintain the muni exemption to keep borrowing costs low for issuers.

“Some Democrats believe munis are inefficient and want to increase inefficiency by changing them,” Godfrey said. “We think they’re wrong.”

“Some Republicans think munis over-encourage spending,” he added. “We also think they’re wrong.”

Still, Godfrey said there are plenty of members from both parties of Congress who understand the importance of municipal bonds as an efficient financing tool and that he is “heartened” by the Democratic platform, which supports the exclusion of interest for tax-exempt munis.

“I think that was significant,” Godfrey said. “One of the problems has been that for a long time there’s been an assumption that the tax exemption of munis was a given and there was not a whole lot of advocacy in support. Suddenly that’s not a given.”

Godfrey cited several proposals to tax or place a surtax on munis that have surfaced in recent years, including those in President Obama’s budget requests that would cap the value of the muni exemption at 28%.

Clinton has proposed a 28% limit on the tax benefit from specified deductions and exclusions, but has not said if that will include the muni tax exemption.

Proponents like Godfrey stress the low costs the muni exemption provides for issuers in financing infrastructure costs, while opponents contend it is an inefficient method of borrowing that leads to federal revenue losses.

Emily Brock, director of the Government Finance Officers Association's federal liaison center, said she could not comment on what a party change would mean for munis.

"There are many legislators from both sides of the aisle who have offered unwavering support of the muni and recognize its importance as the primary financing tools across the U.S. to satisfy infrastructure needs," she said.

Sen. Orrin Hatch, R-Utah, is the current chairman of the Senate Finance Committee. He would likely be replaced by Sen. Ron Wyden, D-Ore., the ranking minority member, if Democrats seize control of the Senate,

Wyden, who has previously expressed support for municipal bonds, would be welcomed as the finance committee head, said Justin Underwood, federal policy advisor for Bond Dealers of America.

Underwood said that although Wyden does not have an extensive legislative record on munis, Oregon's has had $26 billion of infrastructure construction and improvements financed through munis over the past decade.

"We know that he is following the issue very closely, both in terms of how the pieces of the puzzle fit in tax reform discussions and, possibly, into negotiations on an infrastructure plan," Underwood said. "We hope that Sen. Wyden will continue to place the benefits of municipal bonds and preserving their full tax-exempt status at the top of his priority list."

BDA will be tracking any legislation effecting municipal finance and attempts to limit the tax exemption of munis, including bills in both the House and Senate that would treat certain munis as high quality liquid assets under bank rules and raise the limit for bank-qualified bonds. Pending before the Senate Finance Committee is The Municipal Bond Market Support Act of 2016 (S. 3257), which would raise the annual issuer limit for issuers of bank-qualified bonds to $30 million from $10 million and index it for inflation.

The bill was introduced in July by Sen. Bob Menendez, D-N.J., as an identical companion bill to The Municipal Bond Market Support Act of 2015 (H.R. 2229) introduced in the House in May of last year by Rep. Tom Reed, R-N.Y.

Brock said that when Congress' temporary increase to a $30 million issuer limit in 2009 and 2010 provided state and local governments with significant benefits. GFOA is now asking Congress to permanently increase the limit.

"We remain hopeful that this issue will be addressed this year and remain committed to work with Senators Menendez and Cardin to make this happen," Brock said. "If it isn't completed this year, it will remain a priority for GFOA in 2017."

The House passed a bill (H. R. 2209), and a similar one is pending in the Senate (H.R. 3404), that would require federal banking agencies to treat as high quality liquid assets (Level 2A) any muni obligations that are liquid, readily marketable and investment grade as of a certain date.

Another bill pending before the Senate Finance Committee is The Green Bank Act of 2016 (S. 3382), which was introduced by Connecticut Democrats Sens. Chris Murphy and Richard Blumenthal as well as Sen. Sheldon Whitehouse, D-R.I., in September.

The bill would create a federal green bank to attract larger private investments in clean energy and energy efficient projects. An identical companion bill was also introduced in the House.

The Bond Buyer

By Evan Fallor

November 4, 2016

TAX - MISSISSIPPI
[Pascagoula-Gautier School District v. Board of Supervisors of Jackson County]
Supreme Court of Mississippi - October 20, 2016 - So.3d - 2016 WL 6125423

School district and city brought action against county board of supervisors, challenging board's approval of tax assessor's methodology in assessing taxes on lessee of county property located in school district but not within city boundaries.

The Circuit Court granted board's demand for jury trial, denied plaintiffs' motion to join lessee as party, and ultimately granted board's motion to dismiss for lack of standing. Plaintiffs appealed.

The Supreme Court of Mississippi held that:

- Plaintiffs experienced adverse effect different than that of general public due to tax assessment of leased property and, thus, plaintiffs had standing to bring action against board, and
- Trial court abused its discretion by refusing to order joinder of lessee of county property.

City and school district in which leased county property was located, as taxing authorities and direct recipients of revenue from taxes collected on property, experienced adverse effect different than that of general public due to approval by county board of supervisors of tax assessor's methodology in assessing taxes on such property and, thus, school district and city had standing to bring action against board challenging tax assessment, despite lack of statutory authority to sue. City and school district funding was reduced by any allegedly improperly low tax assessment, city was required to set higher millage rate for rest of taxpayers in order to meet budget, and school district had to incur costs encountered in raising millage rates.

Trial court abused its discretion by refusing to order joinder of lessee of county property, in action by city and school district challenging approval by county board of supervisors of tax assessor's methodology in assessing taxes on leased property, which was located in school district. Lessee was subject to joinder either as party that needed to be joined for just adjudication, or had waived right to object to being joined due to unfettered participation in the case.

IRS PLR: Intergovernmental Organization Qualified as Wholly Owned

Instrumentality of Member Cities.

Intergovernmental organization requested a letter ruling that donations to the organization are tax deductible under § 170 because the organization, as a consolidated department of all incorporated cities in the State, is a wholly owned instrumentality of political subdivisions of the State.

The IRS ruled that the organization qualified as a wholly owned instrumentality of its member cities of the State within the meaning of Rev. Rul. 57-128.

Read the Private Letter Ruling.

What's in your Partnership Agreement? Why Non-Taxpaying Entities Should Care About Allocations of Taxable Income.

Even before the advent of P3s (public-private-partnerships), it was not uncommon for a governmental entity or a 501(c)(3) to enter into a joint venture with a for-profit, taxpaying entity. Sometimes these joint ventures take the form of either a state law partnership or a state law limited liability company ("LLC"). Most LLCs are taxed as partnerships for federal income tax purposes, which generally means that they are pass-through entities. In other words, the partnership itself does not pay tax on its taxable income (like a corporation would). Rather the taxable income flows through to the partners who are required to pick up their respective distributive shares of the partnership's items of income and loss on their own separate federal income tax returns.

Why would a non-taxpaying entity care about allocations of taxable income? Because the manner in which "taxable income" is determined, and its allocation among the various partners in the partnership could impact the amount of cash flow available to be distributed to the partners in the partnership. Even non-taxpaying entities should care about their cash flow from partnerships and/or LLCs. This is especially important in light of new legislation that changes the manner in which partnership audits by the IRS are resolved.

Over the past several decades, most partnership audits were conducted by the IRS under the rules set forth in the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA" yes, that TEFRA, the same act that gave us the notice, hearing, and approval requirements for qualified private activity bonds). Under the audit rules set forth in TEFRA, the IRS would determine what adjustments needed to be made at the partnership level. The IRS would then recalculate each partner's tax liability after flowing the adjustments through the partnership to the separate partners, and collect any additional tax owed from the individual partners rather than the partnership. Especially for large partnerships, this has been a cumbersome process for the IRS. It would be similar to the IRS trying to collect from the bondholders rather than the issuer the additional tax owed on bonds that were issued as tax-exempt bonds but that were ultimately determined to be taxable.

For tax years beginning on or after January 1, 2018, the manner in which a lot of partnership audits are conducted by the IRS will change. Most significantly, for many partnerships, any additional taxes owed to the IRS will be assessed against the partnership rather than the individual partners. This change can have inequitable results under certain circumstances. For example, assume that the IRS finalizes an audit of a partnership's 2018 tax year in 2020. Any additional taxes resulting from partnership adjustments made to the 2018 taxable year will normally be paid by the partnership in 2020. Thus, a partner that joined the partnership in 2019 will, as a result of the partnership's reduced cash flow (used to pay the 2018 tax liability), own a less valuable partnership interest in

2020, and have a decreased chance of receiving distributions from the partnership beginning in 2020.

The new IRS audit rules do allow partnerships to adopt certain procedures intended to alleviate the unfairness outlined above. First, the partnership agreement can require that each person who was a partner from the adjustment year (2018 in the above example) file an amended tax return picking up its distributive share of the audit adjustment. This would benefit tax-exempt partners, because only the taxable partners would be required to file an amended income tax return to report the distributive share of taxable income that arises from the audit adjustment. Second, the partnership can make an election to transfer its obligation to pay the additional tax to the partners that were partners in the audit year who would then pay the tax in the year the audit was finalized (2020 in the above example). This election would shift the economic burden of the additional tax liability from the partnership (and, thus, all of its current partners, including tax-exempt partners) to the taxable persons who were partners in the partnership for the year under audit.

Although the new IRS audit rules for partnerships do not apply until January 1, 2018, partnerships can elect into them now, and once they are effective, certain partnerships may elect out of them. Accordingly, it is important that all partners, including non-taxpaying partners, understand the economic ramifications of these rules and know what the partnership agreement says about them. In other words, each partner should be able to answer the question: What’s in your partnership agreement?

Squire Patton Boggs

The Public Finance Tax Blog

By Cynthia Mog

October 26, 2016

Tax on a Haircut? Missouri Voters Weigh Sales Tax Limits.

JEFFERSON CITY, Mo. — Missouri voters will be the first in the nation to decide whether to amend their state constitution to prohibit sales taxes from being expanded to services such as auto repairs, haircuts, legal work and financial accounting.

The proposal on the Nov. 8 ballot is a backlash against efforts in numerous cash-hungry states that have considered extending sales taxes beyond goods to keep pace with the service-based economy.

Concerned that states could try to tax services related to home sales, national and local organizations representing real estate agents have poured about $7 million into a campaign to pass the amendment, with hopes of a trend-setting victory.

“If we can do this here, it would be a model for the rest of the country,” Missouri Realtors CEO John Sebree said.

Opponents have not reported raising any money to fight the measure. But the Missouri Municipal League warns there could be “dire consequences” for police, fire and road departments if governments are constitutionally barred from enlarging their sales tax base.

“It’s a short-sighted attempt to solve a problem that doesn’t exist,” said the league’s deputy director, Richard Sheets.

Sales taxes have long provided an important financial foundation for governments. They are levied by 45 states and more than 10,000 local jurisdictions. But only a few states currently charge sales taxes on a wide array of services.

State revenue from general sales and gross receipts taxes has rebounded more slowly than individual income taxes following the recession that ended in 2009, according to U.S. Census Bureau figures.

Some states have sought to compensate for sluggish sales tax growth with proposals to apply the tax more widely. The rise of Republican-led statehouses since 2010 has also spawned proposals to cut income taxes and offset the cuts with higher sales taxes on a greater number of goods and services.

In March, North Carolina began charging sales tax on labor for a number of services, including vehicle maintenance, flooring and cabinet installation and jewelry repairs. The expansion was part of a new law that also will cut individual income tax rates starting in 2017.

Many customers initially questioned the new sales taxes and some decided to delay repairs, said Dean Bailey, owner of King’s Auto Service in Raleigh, North Carolina.

But, he added, “It’s a thing that now we’ve sort of grown accustomed to.”

Over the past five years, about half the states have considered some sort of proposal to expand sales taxes to services, according to bill tracking by the National Conference of State Legislatures, the American Institute of Certified Public Accountants, the National Association of Realtors and research by The Associated Press. Many of those proposals have failed.

Missouri is the first state where voters will consider a constitutional amendment putting a halt to sales tax expansions, according to the NCSL. Amendment 4 would bar state and local sales taxes from being applied to any transaction or service not already taxed as of Jan. 1, 2015.

The campaign has drawn support from a broad coalition, including associations for accountants, attorneys, banks, funeral homes, newspapers and broadcast media.

Mark Ewers, who runs a home siding and window business in Jefferson City, was among several dozen people who recently attended a free lunch hosted by the committee backing the initiative. He said he already pays sales tax on materials, but calculating a tax for his installation work would be a paperwork headache.

“I can’t imagine having to tax for all of the services that I provide,” he said.

How voters will react remains unclear. There is scant public polling on the ballot proposal, although focus groups have shown some voter confusion over the wording of the measure.

A similar idea was proposed in Florida after legislators in 1987 expanded the sales tax to dozens of services that included construction and advertising. But the petition drive for that ballot measure subsided after lawmakers repealed the services sales tax just six months after it began.

During the past decade, Maryland, Massachusetts and Michigan also have quickly repealed expanded sales taxes on services in the face of public disapproval.

Missouri lawmakers for several years have considered expanding the sales tax base in exchange for phasing out the state income tax, but those bills gained little traction this year.

Republican lawmakers contend recent decisions by courts and the state Department of Revenue have nonetheless gradually expanded the sales tax base. For example, the revenue agency sent a letter to businesses in July notifying them that delivery services are subject to taxes if included with certain retail sales.

By THE ASSOCIATED PRESS

OCT. 28, 2016, 11:01 A.M. E.D.T.

TAX - MAINE

Angell Family 2012 Prouts Neck Trust v. Town of Scarborough

Supreme Judicial Court of Maine - October 13, 2016 - A.3d - 2016 WL 5940101 - 2016 ME 152

Taxpayers challenged increased property tax assessment levied by town.

The Business and Consumer Court found that taxpayers lacked standing, and taxpayers appealed.

The Supreme Judicial Court of Maine held that:

- Taxpayers had standing to challenge town’s excess land program;
- Town’s abutting property program violated state constitution;
- Town’s board of assessment review was compelled to conclude that abutting property program resulted in an unequal apportionment of tax burden;
- Town’s large lot program was not discriminatory;
- Town had legitimate basis for its increased assessments; and
- Town assessor’s decision to increase assessments did not constitute unjust discrimination.

Taxpayers had standing to challenge town’s excess land assessment programs which provided a method for valuing single residential lots larger than one acre, and permitted owners of multiple contiguous lots to combine those lots for assessment purposes, even though taxpayers did not qualify for the programs, where taxpayers did not benefit from the favorable tax treatment that town gave to owners of qualifying lots.

Town’s abutting property program, which permitted owners of multiple contiguous lots to combine those lots for assessment purposes, violated state constitutional requirement that an individual parcel of real estate be assessed separately according to just value.

Town’s abutting property program, permitting a taxpayer who owns multiple abutting lots to elect to have the separate lots assessed as a single unit, resulted in an unequal apportionment of the tax burden in violation of the state constitutional requirement that an individual parcel of real estate be assessed separately according to just value, since some taxpayers received a major benefit as a result of the program, and those who did not own abutting lots were subjected to taxes not imposed on owners of lots that happen to be abutting.

Town’s large lot program, which applied to the valuation of a single parcel larger than one acre, was not discriminatory against taxpayers who did not qualify for program, where the program resulted in an assessment reflecting the just value of taxpayers' waterfront property.

Town had legitimate basis for its increased assessments of waterfront property owned by taxpayers, where town assessor's reevaluation of properties was grounded in an ongoing analysis of sales data, and although some of the sales used in the analysis were private sales, there was no evidence that those sales were not arm's length transactions.

Town assessor's decision to increase assessments on waterfront properties in area of property owned by taxpayers, but not to raise assessments of comparable properties in another area, did not constitute unjust discrimination against taxpayers, where the waterfront properties in the comparable area were not similarly situated to those in taxpayer's area, the other properties were generally larger, and were located a significant distance from the taxpayer's area's amenities.

State Tax Commissions: 2000-2016

Abstract

Tax policy is one of the most challenging and controversial components of state governance. Determining how and from whom to collect revenue involves questions of equity, fairness, efficiency, and simplicity. As a result, states often create special tax commissions before attempting major tax reform. This brief discusses who establishes commissions, who serves on commissions, who advises commissions, what commissions recommend, and if and when their reports lead to changes in state tax policy.

Download the brief.

The Urban Institute

by Richard C. Auxier

October 16, 2016

How State Tax Commissions Approach Economic Development.

Abstract

Nearly all state tax commissions—independent groups that study and make recommendations for improving a state's tax system—are tasked with improving economic development within the state. Their report introductions include phrases such as "growth-friendly," "unleash innovation," and "optimum competitor." And many commissions cite economic development to justify their concluding recommendations. But most reports ultimately contain little exploration or explanation on how taxes and economic development are (or are not) linked. This is a missed opportunity because most commissions thoroughly investigate their state's tax structure, often with the assistance of respected tax and budget experts.

Download the brief.

The Urban Institute

by Richard C. Auxier

October 16, 2016

Former TEB Head Says IRS Ignoring Violations.

WASHINGTON – The former head of the Internal Revenue Service's tax-exempt bond office is accusing the office of ignoring alleged tax law violations in a $228 million tax-exempt financing for a Syracuse mall that benefited from tax breaks sought by Hillary Clinton when she was a Senate candidate.

The bonds were issued in February 2007 by the Syracuse Industrial Development Agency (SIDA), which loaned the proceeds to Destiny USA Holdings LLC to finance an expansion of the Carousel Center shopping complex in Syracuse. They were supposed to be "qualified green building and sustainable design project" bonds issued under tax law provisions pushed for by Clinton and Sen. Chuck Schumer, DN.Y.

The IRS began auditing the bonds in March 2011 after SIDA and Destiny told the IRS in a letter that, because of a legal dispute and the recession, it had failed to meet the green bond requirements. The IRS later closed the audit with no change to the tax-exempt status of the bonds because SIDA had reasonably expected the requirements would be met.

Mark Scott, the former TEB director who spent 18 years at the IRS and represents whistleblowers in a private practice here, thinks the IRS is ignoring alleged tax law problems with the transaction because of politics.

Scott said he alerted IRS officials to roughly $30 million in fees paid to SIDA and Syracuse from bond proceeds as well as issuance costs that violated a 2% limit, both alleged tax law violations. The IRS told him it would not pursue these allegations.

Scott has written a five-page analysis of the transaction on his website detailing the alleged violations and warning that, by ignoring them, TEB is opening the door for other issuers to commit similar violations.

"In a stunning reversal of more than 30 years of existing law and its own Publication 5005, `Your Responsibilities as a Conduit Issuer of Tax Exempt Bonds,' the IRS Office of TaxExempt Bonds … has [decided] to not apply any limits on the amount of fees a government conduit issuer may be paid out of bond proceeds," Scott said in analysis.

IRS Publication 5005 states that while conduit issuers may charge fees payable out of bond proceeds, Section 148 of the Internal Revenue Code generally limits the size of such fees to prevent bonds from becoming taxable arbitrage bonds.

Scott argues that the issuer fees should have been added to the investment yield on the conduit borrower's obligation. Under the tax law, that investment yield should have been limited to one eighth of one percent. Instead, it was much higher, making the bonds arbitrage bonds.

"IRS officials are ignoring upwards of $30 million in issuer fees," Scott said, calling this "the largest violation of this provision I have ever seen."

“Any member of Congress worth his or her mettle would not allow their state or local government agencies to be penalized for behavior that the IRS has openly permitted to a much larger degree for another government agency,” he added.

Scott also said the IRS is ignoring issuance costs that significantly exceed the limit of 2% of bond proceeds for private activity bonds. The issue price of the 2007 bonds was $238.5 million, which should limit issuance costs to $4.8 million. But the underwriters’ discount for the bonds, in and of itself, took up most of the issuance costs, at $4.77 million.

Scott claims the 2% limit was exceeded by $2.6 million, which if included, would have pushed issuance costs over 3% of bond proceeds.

“As with its complete waiver of enforcing the previously described `issuer fee’ limit, the IRS will be hard pressed to walk back this broader [issuance cost limit] waiver policy now that it is publicly known,” Scott said in the analysis.

Scott told The Bond Buyer on Tuesday that his article is meant to prevent the TEB from hiding behind a “wall of secrecy” and to level the playing field for smaller issuers, who he believes would have been targeted for similar, but much smaller violations.

Scott said the decision not to proceed to pursue the alleged tax law violations was not made by one agent, but rather involved at least two IRS senior bond agents, a field manager, multiple senior managers, multiple senior analysts and multiple officials of the Tax Exempt & Government Entities Division, as well as Office of Chief Counsel officials,. As of Tuesday, neither the IRS TE/GE Division nor the Office of Chief Counsel had released formal or informal guidance on the issue. IRS officials did not respond to a request for comment. SIDA representatives also could not be reached for comment.

Scott believes the IRS has backed off this deal because of the appearance of impropriety and the election.

“In my view, there’s an appearance of impropriety because the developer was a Friend of Bill [Clinton] who contributed to the Clinton Foundation and because of Hillary Clinton’s involvement in getting legislation passed for this project,” he said.

In early 2009, Hillary Clinton told The New York Times, “I’ve been a big supporter of Destiny. I worked successfully to get the green bonds bill passed. I think it would be a big shot in the arm. It would be a destination site for the area.”

The mall has been rebranded Destiny USA.

The NYT reported that developer, Robert J. Congel, contributed about $100,000 to the Clinton Foundation at about the time Hillary Clinton helped secure the tax breaks. At that time, Congel told the NYT reporter: “There was no connection with Bill Clinton and the ‘green bonds’ and the contribution – none at all.”

A spokesman for Clinton told the NYT that she supported the expansion of the mall “purely as part of her unwavering commitment to improving upstate New York’s struggling economy and nothing more.”

Scott noted in his analysis that the bonds were “issued to finance a not-so-green shopping mall.”

Scott said he expects SIDA will issue refunding bonds this week to refund the 2007 bonds, adding that the roughly $30 million issuer fee and issuance cost problems will likely be carried forward into the new financing.

Scott said both of the alleged violations will "continue to taint" the tax-exempt status of the interest paid to holders of the 2007 bonds for at least three more years.

The Bond Buyer

By Evan Fallor

October 20, 2016

[TEB Says Muni Audits Can Be Closed After Full Redemption.]

CHICAGO — The Internal Revenue Service's Office of Tax-Exempt Bonds has told its auditors that, if an issuer redeems 100% of the outstanding principal amount of its tax-exempt or tax-credit bonds, the audit can be closed without further TEB action.

But the interim guidance, which was released this week in a memo from Rebecca Harrigal, TEB's director to amend the Internal Revenue Manual (IRM) to include a new resolution method for audits, has drawn criticism from a former TEB director who says it could lead to more tax law violations.

The guidance gives four factors auditors must consider when closing an audit with no further action: the reasons for noncompliance and whether it falls under an anti-abuse rule; whether the underwriter, conduit borrower or other user of proceeds with a financial interest in the transaction were involved in aspects of the deal that led to noncompliance; and whether the issuer or borrower took reasonable steps to ensure the bonds complied with law or attempted to self-correct the problem before the audit.

Speaking at the National Association of Bond Lawyers' Bond Attorneys' Workshop here on Wednesday, Harrigal said that the guidance "generally won't affect bond issues."

"If the guidance is going to resolve a problem you see then it is worth putting effort into the audits," Harrigal said. "Certain times – yes it makes sense to close audits and other times that doesn't make sense and we should continue audits."

"The rules for re-opening a TEB exam are not as clear as I hope they would be," she added. "There are very strict rules of re-opening a case that has already been reviewed."

Should an auditor determine the bonds don't comply with law, it can issue a closing Letter 5859, Full Bond Redemption – Compliance Issue Identified.

The new guidance does not apply if the bonds are redeemed with other tax-advantaged bonds or if they are direct-pay bonds. It also does not apply if the issuer did not make appropriate rebate payments on the bonds or if the issuer asks for a closing agreement. The guidance is applicable for two years.

Mark Scott, the former head of TEB who is now in private practice representing whistleblowers, said that IRS officials are "clearly walking away from doing their job" and are trying to prevent the payment of what is owed. This could lead to bond counsel opinions that do not meet the NABL standard, he warned.

Because IRM provisions are not law and can be changed at will, Scott said the “unthinkable” provision should be revoked.

“This sounds like a pass for a bad bond counsel opinion,” Scott said. “This could lead to significantly aggressive tax opinions given by bond counsel in an industry that is already out of control.”

“If the only penalty that applies is redeeming and refunding bonds, then it is essentially encouraging tax counsel to not comply with tax laws,” he added.

Although redemption of bonds is important, he said, this guidance will lead to inappropriate actions and does not clearly state whether the issuer took reasonable steps if bond counsel gives an incorrect tax opinion.

The interim guidance comes as TEB continues to work with a diminished staff and limited resources. At BAW, Harrigal said that TEB lost eight employees in the past year for various reasons, including transfers and retirements. The office is now down to roughly 65 employees, she said, including 14 tax law specialists.

For this fiscal year, TEB will work on selecting audits with a higher risk of noncompliance, including specific returns as well as classes of returns.

She said the office is using market segments where there is information that there may be a high level of noncompliance for targeted audits, including sports facilities, advance refundings and government facilities with private activity. None of those market segment audits are closed, she said, though some are more than 80% complete, Harrigal said.

“We identify issues and fact patterns we hypothesize have a higher risk of noncompliance,” she said. “What we do with those is create a sample. We will pick out a statistical sample of returns and examine them. Some in there will be perfectly fine.”

In March, TEB released model closing agreements for both the general examination program and the Voluntary Closing Agreement Program (VCAP) to expedite and increase consistency. Harrigal said that VCAP “continues to be a priority and we will devote resources based on that,” but added that the office has gotten significantly fewer VCAPs since then.

TEB also said in its two-page work plan for fiscal 2017, which began this month, that the highest priority would be given to claims and referrals warranting audit resources.

Because of revisions made to the direct-pay bond refund process, TEB said it expects fewer direct-pay referrals in fiscal 2017, but that they will likely to have a higher risk of noncompliance than under the prior process.

Mike Bailey, a partner with Foley & Lardner in Chicago and chair of Wednesday’s panel, noted TEB typically audits bonds five-to-six years after their issuance to give it time to see how the proceeds were spent and other determining factors. He also noted that it marks six years since the issuance peak of direct-pay bonds and Build America Bonds (BABs), and asked Harrigal if a wave of audits can be expected.

Harrigal said it is “happening under the radar,” adding that BABs are included in the market segment audits.

The Bond Buyer

By Evan Fallor

October 20, 2016

[Chicago Schools' Labor Deal Boosted by TIF Infusion.]

CHICAGO – Chicago's tax-increment financing program is in the spotlight after the city said it would release a bigger-than-planned chunk of surplus TIF revenues to help Chicago Public Schools pay for a new teachers' contract.

Mayor Rahm Emanuel unveiled a proposed 2017 budget Tuesday that declares a $175 million TIF surplus.

Based on the distribution formula, the city will receive about $40.5 million while about $88 million will flow to the financially distressed school district.

CPS had only built $32 million of TIF money into its fiscal 2017 budget, expecting the city to declare a more modest $60 million surplus.

The remainder will go to other area taxing bodies. CPS received $103 million in fiscal 2016.

Word began to circulate of the expected action in the early morning hours of Tuesday shortly after CPS and the Chicago Teachers' Union reached a tentative agreement on a new four-year contract that averted a strike set to begin Tuesday.

The city has annually freed up surplus TIF revenue but it has resisted political pressure by limiting the amount with the annual releases varied in size.

The action — promoted and endorsed by some city council members and union officials and initially resisted by Emanuel — has prompted debate over a series of issues.

They include questions over the appropriate use of TIF revenues, which are supposed to be set aside for development purposes, whether even more should be freed, and whether the funds provided too easy a political escape hatch for the district, which was seeking deeper concessions from the Chicago Teachers' Union.

They also have spurred questions over whether or not the revenue represents a non-recurring revenue stream that can't be counted annually to cover an annual operating expense, a position Emanuel seemed to previously back in statements.

That position has now changed.

"I don't see TIF surplus at this stage as a one-time revenue," city budget director Alexandra Holt said when asked about the issue during a meeting with Crain's Chicago Business' editorial board. "I see it as an ongoing revenue."

Much of the surplus funding being freed up comes from frozen, canceled, and expiring TIFs as well as the "declared" amount.

Holt projected that surpluses will be available for well over a decade, and therefore should not be considered a so-called one-shot.

Holt made her case during an interview along with Emanuel and chief financial officer Carole Brown that Crain's posted on Facebook.

The majority of this year's surplus comes from the seven downtown TIF districts that were frozen last year and will be retired when existing projects are paid off.

Those districts will generate about $250 million in surplus revenue over the next five years, according to the city's annual financial analysis.

Market participants, rating agencies, and budget watchdogs warn against relying on non-recurring revenue streams to cover recurring operational expenses as they drive up structural gaps.

The district's heavy use of one-shots, from debt restructurings to a three-year partial pension holiday to cover past deficits, have driven the school district's structural deficit up to $1 billion and helped sink its ratings deep into junk territory.

One of Emanuel' top council allies acknowledged TIF funding is only a temporary salve.

"TIF is a one- or two-year fix," Emanuel's floor leader, Alderman Patrick O'Connor, said on WTTW's Chicago Tonight program. "We've done it this year so we can keep the schools open…but what we need to do is find a permanent solution."

TIF has long been used to support school capital projects — the city committed funds to bond issues in 2007 and 2010 under former Mayor Richard Daley's school modernization program — so it's not improper to now use to help with an operating expense, O'Connor added.

Chicago's 146 TIF districts are expected to generate $475 million next year. The program began in 1984 and Daley used it heavily to spur development resulting in criticism that it provided subsidies for wealthy downtown developers for areas some might not consider "blighted."

Once designated a TIF district, the amount of property taxes that flows to general government coffers is frozen and revenue growth goes to fund qualified work in the district to support development for 23 to 24 years. The city has also issued bonds backed by the revenue.

Emanuel implemented reforms after taking office in 2011 and signed an executive order in 2013 that required the city to declare a surplus from TIF districts annually of at least 25 % of the available cash balance after accounting for current and future projects or commitments.

Emanuel froze the downtown TIFs last year.

Since 2011, a total of $853 million of surplus revenue has been distributed but the amount has varied significantly.

In 2011, a $276 million surplus was distributed to taxing bodies.

That dropped to $97 million in 2012, $43 million in 2013, $65 million in 2014, $84 million in 2015, $113 million in 2016, and now $175 million will be released in 2017.

The use of revenue that can't be relied upon annually, at least at the level being freed up in 2017, heightens worry over the district's prospects because of its precarious liquidity, reliance on credit lines to keep afloat, and the uncertainty over some funding streams in its budget.

The state committed $215 million to help fund teachers pensions' but only if Gov. Bruce Rauner and Democratic lawmakers can bridge their partisan divide that has blocked passage of a state budget and agree on state pension reforms. An additional $130 million of state aid is also uncertain beyond fiscal 2017.

CPS has further fueled concerns by failing to provide a price tag for the new teachers contract.

"For the district, not only does this deal provide teachers with a raise and secure their pensions, it also achieves meaningful savings that helps stabilize our finances," CPS spokeswoman Emily Bitner said in a statement that offered no dollar figures.

The union's House of Delegates will meet next week and decide whether to recommend a rank-an--file vote.

The district's $5.4 billion fiscal 2017 budget was based on figures from a January offer that was rejected by union delegates.

It counted on $30 million in savings this year assuming the district would phase out the $130 million annual expense of covering 7% of teachers' 9% pension contribution.

But the tentative agreement leaves intact that benefit for existing teachers. It phases the cost out for teachers hired after Jan. 1 but gives them a 7% base pay raise.

Cost-of-living raises proposed in January were scaled back and occur in only year three and year four.

Teachers also agreed to healthcare concessions.

An early retirement offer for some teachers adds to the unknown costs of the deal.

The contract would be retroactive to last year, when the previous pact expired.

"Chicago Public Schools are in big financial trouble, they did not budget anything for additional spending," said Laurence Msall, president of the Civic Federation, adding that the budget is "already over reliant on things coming from Springfield that haven't been fully settled."

Emanuel defended the deal and denied that it too generously favored the union.

"Getting the agreement that didn't adversely affect the classroom was the goal," he said, acknowledging that the district had to relent on the pension pickup.

Emanuel argued the present value of the contract is not that far off from the January offer after the raises were scaled back.

But his administration offered no figures to support that assessment.

The Bond Buyer

By Yvette Shields

October 13, 2016

NABL: TEB Adds Exam Resolution Method.

The Internal Revenue Service (IRS) Office of Tax Exempt Bonds (TEB) has announced it will amend Internal Revenue Manual (IRM) 4.81.5 to include an additional resolution method. The additional method is available when, during an exam of a tax-exempt or tax-credit bond issue, an issuer redeems 100 percent of the outstanding principal amount of the bonds. In that case, the examiner and group manager should consider whether to close the exam without further TEB action, although there may be a referral to another IRS business unit. The memorandum communicating the new method sets out factors to be considered in making the determination to close the exam. The new resolution method is available as of October 18, 2016.

The memorandum is available here.

TAX - KENTUCKY

Wilgreens, LLC v. O'Neill

Court of Appeals of Kentucky - September 23, 2016 - S.W.3d - 2016 WL 5319593

Taxpayer appealed determination of the Board of Tax Appeals upholding county property valuation administrator’s property tax assessment on commercial real property, asserting administrator overvalued property under income generation approach by including income generated under commercial lease.

The Circuit Court affirmed. Taxpayer appealed.

The Court of Appeals held that:

- Taxpayer failed to present evidence demonstrating that property tax assessment overvalued property, and
- Property tax assessment under income generation approach, which included rental payments, was reasonable and did not overvalue property.

Taxpayer failed to present evidence demonstrating that property tax assessment by county property valuation administrator overvalued property by using income generation approach for estimating fair cash value, which required consideration of present value of all future benefits, including net rental income generated under triple net lease for retail pharmacy that encumbered property, and thus assessment’s prima facie validity was required to be upheld, though taxpayer asserted income from lease was above-the-market. Taxpayer attempted to show property was overvalued by relying on properties very different from the subject property, as none of the allegedly comparable properties were located on same major throughway or anywhere similar.

Property tax assessment of commercial property by county property valuation administrator under income generation approach for estimating fair cash value, which required consideration of present value of all future benefits, including net rental income generated under triple net lease for retail pharmacy that encumbered property, was reasonable and did not overvalue property, though taxpayer asserted lease was above-the-market; lease was part of property, property was capable of generating kind of income derived under lease with or without retail pharmacy by virtue of its location on major throughway, several properties located in same area, such as national grocery store chain, generated similar benefits for their owners, and fact that property was able to generate such income made it more valuable.

[Muni Pros Bemoan Lack of Detail in Tax Plans for Infrastructure, Muni Exemption.]

WASHINGTON – As the presidential campaigns have become increasingly focused on personality and name calling, municipal finance pros are begging for more defined infrastructure spending plans and clarity on how the muni tax exemption will fare in the event of tax reform.

The Tax Foundation, in what may be its final evaluation] before Election Day, released its latest report, estimating Hillary Clinton's proposed tax plan would increase federal tax revenue by $1.4 trillion over the next decade.

But in the eight-page report, the think tank said that Clinton proposed several tax policies without indicating exactly how they would work, a criticism that has been made of both candidates.

"Because campaigns are not in the business of crafting legislative language, it is often the case that many proposals are too vague to model precisely," the report read. "As a result, it is necessary to make assumptions about how campaign proposals would operate."

In its report released on Oct. 12, the Tax Foundation said Clinton's plan would increase federal tax revenue by $1.4 trillion over the next decade on a static basis and $663 billion after accounting for the smaller economy and narrower tax base it would create.

The report is an update from the group's January analysis of the Clinton plan. The most recent report accounted for new policies the Democratic nominee introduced, which the Tax Foundation said "significantly" impacted its growth and revenue estimates. These included a 28% limit on the tax benefit from specified deductions and exclusions, leaving the muni exemption standing in question.

The Tax Foundation's January analysis assumed the 28% cap would only apply to itemized deductions but that the limitation would be identical to the cap President Obama has proposed in his last several budget requests.

Mike Nicholas, chief executive officer of Bond Dealers of America, stressed the importance of tax-exempts for infrastructure as uncertainty over the muni exemption lingers.

"If a concern of either candidate is in reducing fiscal burdens on localities, while simultaneously rebuilding the nation's infrastructure and putting people back to work, then maintaining the tax exemption should be of paramount importance," Nicholas said. "It is our hope that this tool is not compromised by placing any cap or limit on the value of the tax exemption."

Tax Foundation director of federal projects Kyle Pomerleau, who compiled the report, said most of the revenue gain is due to increased individual income tax revenue that the group projected to create roughly $817 billion over the next decade. Clinton's proposed estate tax changes will raise an additional $310 billion over the next decade, while increased corporate and payroll taxes would account for $300 billion in revenue, the group said.

The $1.4 trillion projection is in line with a Clinton plan estimate released this month by the Tax Policy Center, which also projected an additional $2.7 trillion in raised revenue over years 11-to-20 of implementation.

TPC also estimated that Donald Trump’s plan would increase the federal debt by $7.2 trillion, which the Republican took exception to, calling it a “fraudulent analysis.”

Trump’s revised plan included reduced marginal tax rates and increased standard deduction amounts but lacked many “important details,” TPC said, leaving analysts to make many assumptions.

Late last month, the Tax Foundation released an updated analysis of Trump’s plan – which would reduce the current individual income tax brackets to three from seven with a 33% top rate. The planwould also reduce the corporate rate to 15% from 35%. The Tax Foundation analysis estimated Trump’s plan would reduce federal revenues by $11.98 trillion over the next decade.

Many muni participants have pegged 2017 as the year for long-awaited tax reform legislation, leaving some eager for more detailed proposals as the presidential election nears.

Frank Shafroth, the director of the Center for State and Local Government Leadership at George Mason University, said Monday that estimates can be made with the plans in their current forms, but more detail would be welcome.

“It clearly makes it harder,” Shafroth said. “But you get a general idea. The mainstream organizations that have evaluated Trumps plan have said would it would increase the debt and deficit. There’s some consensus that the Clinton plan would modestly reduce the deficit.”

He called the Trump plan a “double whammy” in its current form due to the fact that it would substantially lower rates and enhancing the benefits from capital gains. This could discourage investment in munis, he said.

The U.S. Conference of Mayors earlier this month called on both candidates to maintain the tax-exempt standing of munis in their tax plans or risk costing cities billions of dollars. Should the incoming president cap the muni exemption at 28%, as President Obama has proposed in his last several budget requests, cities would see roughly $200 billion in additional costs.

Should the exemption be removed entirely, the group said that figure could balloon to $500 billion and prohibit cities from making much-needed investments in infrastructure. Nicholas also stressed the economic effects of any limit or removal.

“We would hope that [Trump] views tax-exempt municipal bonds as a proven, economically efficient solution to the U.S. infrastructure problem,” Nicholas said. “BDA urges both candidates to avoid eliminating or placing an unnecessary limit or cap on the value of the municipal bond interest exemption and we look forward to learning more about their individual tax plans in the coming days leading up to the election.”

Using figures provided by the Tax Foundation and the Tax Policy Center, the Committee for a Responsible Federal Budget (CRFB) estimated that Clinton’s infrastructure spending could cost up to $300 billion, while Trump’s could cost between $500 and $600 billion.

Clinton has proposed allocating $25 billion to direct public investment as well as $25 billion to a new national infrastructure bank that would be leveraged to support additional loans as well as Build America Bonds, which would be renewed and expanded under her plan.

Still, CRFB said that both proposals lack the infrastructure spending details needed to make anything beyond a preliminary cost estimate, especially Trump’s, which it said is “assumed to be insignificant." Trump's estimate was based on statements he made planning to double the cost of Clinton's infrastructure plan.

The Bond Buyer

By Evan Fallor

October 17, 2016

More on Rev. Proc. 2016-44: What Light Is Shed on Net Profits Compensation?

As reported several times in this blog (here, here, and here), Rev. Proc. 2016-44 significantly expands the opportunities for management/service contracts that don't result in private business use. One such post was Joel Swearingen's very thoughtful piece on the future of the facts and circumstances test as applied to these contracts (here). Of course, Rev. Proc. 2016-44 retains the prohibition against any portion of the manager's compensation being based on net profits, as that rule is set forth in the Treasury Regulations (specifically Treas. Reg. 1.141-3(b)(4)(iv)), so the IRS cannot override that rule through a Revenue Procedure. Unfortunately, in restating this prohibition, the IRS has muddied the water as to its boundaries, creating potential need for application of the facts and circumstances test. Please read on for a discussion of the questions that have been created.

Rev. Proc. 97-13 states the net profits prohibition very simply: "The contract must provide for reasonable compensation for services rendered with no compensation based, in whole or in part, on a share of net profits from the operation of the facility." Section 5.02(1). It then states that the compensation arrangements specifically authorized in 97-13 – percentage of gross revenues or expenses, capitation fee and per-unit fee – are not based on net profits.

In contrast, Rev. Proc. 2016-44 expands the discussion of a net profits arrangement, including the following:

> The contract must not provide to the service provider a share of net profits from the operation of the managed property. Compensation to the service provider will not be treated as providing a share of net profits if no element of the compensation takes into account, or is contingent upon, either the managed property's net profits or both the managed property's revenues and expenses for any fiscal period. For this purpose, the elements of the compensation are ***the eligibility for, the amount of, and the timing of the payment of the compensation."***

Section 5.02(2) (emphasis added).

Prior to the issuance of 2016-44, the IRS issued several private letter rulings applying the facts and circumstances test to conclude that the management fee described in the ruling did not violate the net profits prohibition. In one such ruling, the contract permitted the qualified user to defer paying a stated dollar amount of a fixed periodic management fee and the full amount of a productivity reward to the service provider if net cash flow was insufficient, after taking into account a payment to the qualified user, to pay those fees. Ltr. Rul. 200222006 (Feb. 19, 2002). Any deferred compensation was payable when cash flow was sufficient to make the payment or, at the latest, upon expiration or earlier termination of the contract. In ruling that the contract did not create private business use, based on the facts and circumstances test, the IRS reasoned as follows:

> The Owner’s right to defer a stated dollar amount that represents a portion of the management fee and the full amount of the productivity reward (the ‘deferred fees’) under the circumstances presented raises the issue of whether the these fees are based on a share of Hotel net profits. Although the timing of payment of the deferred fees is based on Hotel net profits and, therefore, indicates private business use of the Hotel by Manager, we think that the circumstances support a conclusion otherwise. The full amount of all deferred fees will be payable regardless of the existence and amount of net profits when the Management Contract expires or is terminated. In addition, the deferrable portion of the management fee is a stated dollar amount and is not, itself, a percentage of Hotel net profits. The productivity reward is analogous to the productivity reward approved by Rev. Proc. 97-13, 5.02(3) because it is to be made only once and is based on an increase in gross revenues for a period specified in the Management Contract. Finally, the feasibility study projects that no deferrals will occur. Thus, although the deferred elements of the Manager’s compensation do not satisfy the requirements of Rev. Proc. 97-13, 5.03(1), on balance, these deferred elements do not indicate private business use under 1.141-3(b)(4).”

In a later ruling, the IRS addressed a compensation arrangement that included an incentive fee that was payable only if three tests were met, one of which required that the manager “meet a stated net operating surplus/deficit level for the applicable fiscal year that is established in advance of each fiscal year of the term of the Management Contract in the approved budget for such fiscal year.” Ltr. Rul. 201145005 (Aug. 4, 2011). Only if all three tests were met, the manager was entitled to a set incentive fee; the fee did not vary based on the level of the surplus/deficit. In its analysis, the IRS first stated that the contract did not meet the requirements of 97-13. However, it then applied a facts and circumstances analysis to conclude that the contract did not result in private business use. While its reasoning isn’t entirely clear, the IRS appears to have concluded that the provision described above did not result in compensation based on net profits because the incentive payment did not vary based on the level of surplus or deficit.

While these rulings provide authoritative guidance only to the issuers receiving them, bond counsel regularly study these rulings and interpret the underlying law and regulations with these rulings in mind. As a practical matter, bond counsel have no choice but to place some importance on letter rulings given the dearth of authority in the tax-exempt bond area.

The question that bond counsel now face is whether Rev. Proc. 2016-44 backtracks from these favorable conclusions. As quoted above, 2016-44 states that a compensation arrangement does not violate the net profits prohibition if no “element” of the compensation takes into account, or is contingent upon, the managed property’s net profits. And for this purpose, 2016-44 states that the elements of the compensation are the ***eligibility for*** (arguably violated in Ltr. Rul. 201145005), the amount of, and the ***timing of*** (almost certainly violated in Ltr. Rul. 200222006) the payment of the compensation.

Was it the IRS’s intent in Rev. Proc. 2016-44 to signal a reversal of the above letter rulings? While this would be a plausible conclusion, I do not believe it is warranted. It appears that Treasury was reflecting its knowledge and experience gained in addressing various compensation arrangements in the ruling context, and that it sought in 2016-44 to make clear, if it was not clear already, that provisions of the sort addressed in the above rulings disqualify the contract from the safe harbor. Exclusion from the safe harbor of contracts where eligibility for, or timing of, compensation is contingent upon sufficient net cash flow is consistent with the position of the IRS expressed in these rulings, where the IRS applied a facts and circumstances test. Whether those contracts give rise to private business use depends now, as it did before, on the facts and circumstances test. So, just as the compensation provisions addressed in the above pre-2016-44 rulings, taken in the overall context of the respective contract, did not violate the net profits prohibition under a facts and circumstances analysis, the same conclusion should be reached under the facts and circumstances test of Rev. Proc. 2016-44.

Squire Patton Boggs

by Robert J. Eidnier

USA October 7 2016

TAX - CALIFORNIA

Covarrubias v. Cohen

Court of Appeal, Third District, California - October 7, 2016 - Cal.Rptr.3d - 2016 WL 5864578

City residents petitioned for writ of mandate to compel Director of the Department of Finance, the state Controller, city, and county auditor-controller to continue payments of set-asides from “tax increment” to city’s subsidized housing fund.

The Superior Court denied petition. Residents appealed.

The Court of Appeal held that:

- City’s set-asides for future affordable housing payments were not “deferred” payments that remained enforceable after the dissolution of the redevelopment agency, and
- City’s set-asides for future affordable housing payments were not “obligations imposed by state law” that remained enforceable after the dissolution of the redevelopment agency.

TAX - CALIFORNIA

City of San Diego v. San Diegans for Open Government

Court of Appeal, Fourth District, Division 1, California - September 22, 2016 - Cal.Rptr.3d - 2016 WL 5231822

City filed validation action regarding the city’s plan to levy a special tax. A suspended corporation filed a verified answer. After the corporation was revived, the Superior Court issued a ruling validating the special tax.

Corporation appealed, and the Court of Appeal reversed and remanded with directions to enter judgment in favor of the corporation. The Superior Court denied validation and partially granted corporation’s attorney fee motion. City appealed.

The Court of Appeal held that on issue of first impression, private attorney general fees could not be awarded to a suspended corporation that was not revived before the expiration of the deadline to appear in the validation action.

Private attorney general fees could not be awarded to a corporation that was suspended when it filed an answer in a validation action, where both the corporation and its attorney knew the corporation was suspended, the corporation was not revived before the expiration of the deadline to appear in the validation action, and the corporation did not explain what additional benefit it provided in the matter in light of the fact that another objector had already appeared and was protecting the public interest.

IRS Requests Comments on Tax-Exempt Bond Forms.

The IRS has requested public comment on Forms 8038, 8038-G, and 8038-GC, information returns for tax-exempt bond issues; comments are due by December 12, 2016.

Read the RFC.

IRS PLR: Organization Is Instrumentality of State Political Subdivisons.

The IRS ruled that an organization that is a consolidated department of all incorporated cities in a state is a wholly owned instrumentality of political subdivisions of the state and, thus, contributions to the organization may be deductible under section 170(c)(1).

Read the Private Letter Ruling.

California Cities Seek Record Tax Hikes as Boom Passes By.

California's booming, yet many of its cities aren't feeling it.

From Yreka, near the Oregon border, to El Centro, just north of Mexico, more than 80 local governments are asking voters next month to approve sales-tax increases, the most on record. While some aim to boost spending on roads or other projects, most measures would just provide extra cash. In Ridgecrest, Fairfax, and Fountain Valley, officials say the revenue would eliminate budget deficits or prevent cuts to police and fire departments.

The governments' revenues aren't keeping up with rising expenses, including for employee pensions, despite the thriving technology industry, home-price gains and rapid economic growth in much of the state. That's due in part to the landmark property-tax limits California voters approved almost four decades ago that have prevented municipalities from reaping windfalls as the housing market rebounded from last decade's crash.

"Like a lot of mid-sized communities in California, we are struggling with staffing our essential services," said Brent Weaver, vice mayor of Redding, which is seeking an increase in the sales tax so it can hire more police. "We have been really struggling the last several years trying to grow our economy."

The proposals are timed to coincide with the presidential election, which will increase voter turnout in a state divided between the Democrat-heavy coast and the less-populous Republican interior. On Nov. 8, Californians will decide 427 local measures authorizing taxes and bond issues, almost twice the 240 on ballots four years ago, according to a report by Michael Coleman, the fiscal policy adviser for the League of California Cities.

California's local governments have turned increasingly to sales taxes since the passage of Proposition 13 in 1978 capped how much they can raise from homeowners. At the same time, services — which have helped drive the economy — generally aren't taxed. Another impediment: the state in 2012 dissolved redevelopment agencies that cities had previously used to finance infrastructure projects.

The lingering financial pressure stands in contrast to the overall state, whose government has seen once chronic deficits disappear as the economy revived. California's gross domestic product grew by 4.1 percent in 2015, more than any other state but Oregon, which expanded at the same pace, according to the U.S. Bureau of Economic Analysis.

Welcoming the fiscal turnaround, investors have pushed the yield on California's 10-year bonds to just 0.22 percentage point more than top-rated debt, down from as much as 0.67 percentage point in 2013, according to data compiled by Bloomberg.

Localities "can't fully enjoy the benefits of economic growth because they're limited in one of their major sources of revenue," said Howard Cure, head of municipal research in New York at Evercore Wealth Management, which oversees $6.3 billion of investments. "They're feeling a certain pinch."

Los Angeles County, Orange County, San Francisco and 60 other cities are among the local governments pushing for higher sales taxes, according to a report by the California Taxpayers Association. Nine cities are seeking the cash for a specific function, which require the approval of two-thirds of the electorate. The rest need support of a majority because the money isn't being tied to a particular goal. Some campaigns say the effect on taxpayers will be softened because the state's sales tax will decline by 0.25 percentage points in January, when a temporary increase is set to expire.

Retirement costs are a major reason for rising expenses. Among the cities with tax-increase measures, almost four dozen are expected to see double-digit percentage jumps in their annual pension bills by 2020, according to data compiled by Marc Joffe, research director at the California Policy Center, a nonprofit that has criticized public pensions. That's assuming the state's investments return 7.5 percent annually, a target it hasn't hit in the past two years.

In Redding, pension bills are just one of the burdens facing the community with 92,000 residents more than 200 miles north of San Francisco. Its retirement contributions are slated to rise by almost 55 percent to $25.5 million by fiscal 2019-2020.

The city has reduced its police force to about 98 officers from more than 120 before the recession, said Weaver, the vice mayor. That has led to an increase in emergency call response times, he said. If voters sign off, the additional proceeds would be used to hire 33 officers and 10 firefighters, he said.

For Colusa, a farming community of about 6,000 residents 100 miles to the south, a sales-tax increase could help stave off insolvency. The city has drawn down its savings, said Randy Dunn, fire chief and interim city manager, and employment costs are rising. Federal grants are disappearing, as well as revenue tied to Indian casinos. Its projected 2020 pension contribution will rise 62 percent to $636,000.

“At this rate, we’re going to deplete reserves,” he said. “In about four years, we’re looking at a serious possibility of a bankruptcy.”

Bloomberg Markets

by Romy Varghese

October 13, 2016 — 2:00 AM PDT Updated on October 13, 2016 — 11:03 AM PDT

TAX - WASHINGTON

City of Spokane v. Horton

Court of Appeals of Washington, Division 3 - September 22, 2016 - P.3d - 2016 WL 5342591

City brought mandamus action against county assessor, county treasurer, and Department of Revenue (DOR), seeking to compel county to implement ordinance which would provide certain disabled or low-income citizens with real property tax exemption.

The Spokane Superior Court granted mandamus relief. Assessor, treasurer, and DOR appealed.

The Court of Appeals held that:

- Section of state constitution allowing legislature to grant property tax exemption to retired property owners does not grant authority to legislature to confer authority on municipal corporations to grant same exception, and
- City’s statutory power to assess and collect taxes did not provide authority for ordinance.

City’s statutory power to assess and collect taxes did not provide authority for city ordinance granting real property tax exemption to low-income seniors, persons with permanent disabilities, and disabled veterans. State constitution prohibited municipalities from assessing and collecting nonuniform taxes, and legislature explicitly qualified statutory taxing power with the caveat that such power was subject to constitutional limitations.

TAX - NORTH CAROLINA

Henkel v. Triangle Homes, Inc.

Court of Appeals of North Carolina - September 20, 2016 - S.E.2d - 2016 WL 5076152

Purchaser at federal tax lien foreclosure sale brought action to quiet title to the property after upset bidder at village’s prior tax foreclosure sale recorded commissioner’s deed to the property.

The Superior Court quiet title in purchaser, and upset bidder appealed.

The Court of Appeals held that federal tax lien foreclosure sale purchaser had title to property.

Claim to parcel by holder of quitclaim deed issued following upset bid at village’s tax sale was subordinate to federal tax sale purchaser’s claim to the property based on superior federal tax lien such that recordation statute did not apply and federal tax sale purchaser had title to property. As village's foreclosure action and sale violated federal law by failing to provide notice to United States or join it as a party and occurred prior to the federal tax lien foreclosure sale, quitclaim deed was conveyed subject to the federal tax lien, and quitclaim deed holder was put on notice of the federal tax lien foreclosure sale but failed to redeem the parcel from the federal tax foreclosure sale within 180 days.

NABL: TEB Releases Work Plan for FY 2017.

The Internal Revenue Service (IRS) Tax Exempt and Government Entities (TE/GE) Division, including the Office of Tax-Exempt Bonds (TEB), has released its work plan for fiscal year (FY) 2017. TEB's highest priority examination cases are claims and returns that have been identified because of evidence of noncompliance, such as referrals. TEB receives two types of claims: claims for a return of an overpayment of rebate and claims for direct pay bonds. In FY 2016, TEB revised its direct pay bond refund process, and as a result, in FY 2017, TEB expects to receive fewer direct pay bond referrals, but these referrals will be returns that likely have a higher risk of noncompliance than found generally in returns referred under the prior process. The next priority is returns having issues for which past information, including past examinations and VCAPs, indicate a higher risk of noncompliance. This initiative began in FY 2016 and includes examinations of returns for prison financings and small issue bonds. TEB will also devote resources to identifying new issues and fact patterns with a higher risk of noncompliance, and developing methods to find these new issues. TEB will use methods, including market scans and data analytics, to identify new areas of noncompliance for examination.

The IRS TE/GE work plan is available here (note that the TEB section begins on page 21).

NABL: Ohio Senators Oppose Political Subdivision Regs.

Senators Rob Portman (R-OH) and Sherrod Brown (D-OH) sent a letter to Internal Revenue Service (IRS) Commissioner Koskinen, opposing the current form of the IRS proposed political subdivision regulations (REG-129067-15). The senators expressed concern that the definition is overly broad and risks denying tax exempt financing to "valid and vital political subdivisions" such as sewer districts, port authorities and airport authorities. The senators specifically point to the government control test's application to multi-jurisdictional entities and to the replacement of the private activity tests in section 141 with a "vague and malleable public purpose standard."

The letter is available here.

Just in Case You Didn't Notice – Rev. Proc. 2016-44 Treats as Compensation under a Management Contract the Reimbursement of Amounts Paid by the Manager to its Employees.

Revenue Procedure 2016-44 is laudable because it significantly expands the scope of management contracts that can satisfy the safe harbor from private business use of facilities financed with proceeds of tax-advantaged bonds. It also makes much more feasible the use of tax-advantaged bonds in public-private partnership arrangements. Revenue Procedure 2016-44 does, however, effect one curious change of uncertain implication from its predecessor, Revenue Procedure 97-13.

The management contract safe harbors set forth in Revenue Procedure 97-13 provide that the reimbursement by the "qualified user"[1] of direct expenses paid by the manager to unrelated parties is not treated as compensation of the manager under the management contract. Consequently, such expense reimbursement is not taken into account in determining whether the management contract satisfies a Revenue Procedure 97-13 safe harbor from private business use. The Internal Revenue Service held in Private Letter Ruling 200222006 (Feb. 19, 2002) and Private Letter Ruling 201145005 (Aug. 4, 2011) that the payment of compensation by the manager to its non-executive employees (in the case of the former private letter ruling) and to its employees that do not have an ownership interest in the manager entity (in the case of the latter ruling) was the payment of direct expenses to unrelated parties, the reimbursement of which would not be considered compensation under Revenue Procedure 97-13.

Revenue Procedure 2016-44 changes this result. The reasons for, and implications of, this change are not immediately evident.

Under Revenue Procedure 2016-44, a manager is treated as receiving compensation from the qualified user if the qualified user reimburses the actual and direct expenses (and related administrative overhead expenses) paid by the manager. Revenue Procedure 2016-44 further provides that the reimbursement of actual and direct expenses paid by the manager to unrelated parties is disregarded as compensation for purposes of determining whether the management contract attempts an impermissible sharing of net profits of the bond-financed facility through the payment of compensation that takes into account both the revenues and expenses of the managed facility. However, in direct contrast to Revenue Procedure 97-13, as interpreted by Private Letter Rulings 200222006 and 201145005, Revenue Procedure 2016-44 expressly provides that an employee of the manager is not an unrelated party to the manager.

If the reimbursement of the manager's employee compensation expenses constitutes compensation under the management contract, does this mean that in the not-uncommon arrangement where a manager receives a percentage of the managed facility's gross revenues and is reimbursed for its employee expenses the manager obtains a share of the net profits of the managed facility, which would result in private business use of the tax-advantaged bonds that financed the managed facility? This would be a bizarre result, as illustrated by the following examples.

Assume that a manager contracts with a qualified user to provide counseling services in the qualified user's tax-advantaged bond-financed facility. Assume further that (i) employee compensation is the sole variable expense of the managed facility, (ii) the manager is paid 100% of the facility's gross revenues and is reimbursed for the compensation it pays its employees, and (iii) the management contract otherwise satisfies the elements of Revenue Procedure 2016-44. Under this arrangement, the manager ultimately realizes only the gross revenues, not the net profit or loss, of the managed facility. If gross revenues in a given year are $1,000,000 and the compensation paid to the manager's employees is $500,000, the manager realizes only the $1,000,000 of gross revenues, because the $500,000 of employee compensation expense reimbursement offsets the amounts paid by the manager to its employees. The same is true if the gross revenues of the managed facility are $1,000,000 and the compensation paid to the manager's employees is $1,500,000 – the reimbursement of the manager's employee compensation expense leaves the manager with the gross revenues of the managed facility and with no portion of the $500,000 loss.

Now let's assume that we are dealing with the same management contract, except that the qualified user does not reimburse the manager for the manager's employee compensation expenses. This agreement at least facially complies with Revenue Procedure 2016-44, because the only element of compensation paid to the manager is the gross revenues of the managed facility. Unlike the arrangement where the qualified user reimburses the manager's employee compensation expenses, however, the lack of such reimbursement causes the manager ultimately to realize something other than the gross revenues of the managed facility. Where the gross revenues of the facility exceed the manager's employee compensation expenses, the manager is left with the surplus (which will by definition be less than the facility's gross revenues), and where the manager's employee compensation expenses exceed the facility's gross revenues, the manager will bear the loss.

This is not to say that a management contract results in the impermissible sharing of net profits and losses of the managed facility where the manager is paid a percentage of the facility's gross revenues and is not reimbursed for its employee compensation expenses. This is instead meant to highlight the absurdity of a literal application of Revenue Procedure 2016-44 where the manager is paid a percentage of the gross revenues of the managed facility and is reimbursed for its employee compensation expenses. In such a case, the manager ultimately receives only its percentage of the gross revenues, and the cost of operating the managed facility (in other words, the entrepreneurial risk associated with the facility) remains where it should – with the qualified user.

To avoid unwarranted confusion, the IRS should amend Revenue Procedure 2016-44 so that it accords with Revenue Procedure 97-13, as interpreted by Private Letter Rulings 200222006 and 201145005, to make clear that the reimbursement of a manager's direct and actual employee compensation expense is disregarded as compensation in determining whether the manager and qualified user have entered into an arrangement to share the net profits and losses of the tax-advantaged bond-financed facility.

[1] A qualified user of tax-advantaged bond-financed facilities is any state or local governmental unit or instrumentality thereof, and, in the case of qualified 501(c)(3) bonds, a 501(c)(3) organization if the bond-financed property is not used in an unrelated trade or business of such an organization.

Squire Patton Boggs

The Public Finance Tax Blog

By Michael Cullers on September 27, 2016

Following Revenue Procedure 2016-44, Is There Still a 'Facts and Circumstances' Test for Private Business Use?

As we have discussed in previous posts (here), most practitioners treat a management contract for services at bond-financed property that does not fit within a safe harbor from private business use as giving rise to private business use of the bonds for tax purposes. However, the Treasury Regulations provide that whether or not a management contract gives rise to private business use is based on all the facts and circumstances surrounding the contract.[1] A number of IRS private letter rulings, though they technically cannot be relied on as precedent, rule that various management contracts that don't fit within a safe harbor do not give rise to private business use (discussed here).[2]

In Revenue Procedure 2016-44 (discussed here) the IRS replaced the longstanding safe harbors for management contracts under Rev. Proc. 97-13[3] with a "one-size-fits-all" type safe harbor for all management contracts. This post will discuss the evolution of the policy behind the private business use rules and show that the relevance of the "facts and circumstances" analysis following Rev. Proc. 2016-44 may be diminished. The cause of the diminished value is attributable to the fact that Rev. Proc. 2016-44 has, in effect, imported many of the considerations that previously existed in the facts and circumstances test in the Treasury Regulations into the new safe harbor. As a result, many agreements that fail to qualify for the new safe harbor will no longer be eligible for the facts and circumstances test because the agreements convey a leasehold or ownership interest in bond-financed property (and are therefore not management contracts).

History

Prior to the first appearance of private business use safe harbors for management contracts in Rev. Proc. 82-14, , in 1978, the IRS released General Counsel Memoranda 37641 (the "**1978 Memo**") which includes a thorough discussion of the facts and circumstances that the IRS considered to be necessary for a management contract to be excluded from private business use.[4] Specifically, the 1978 Memo says the following:

> "The regulations are not clear as to the result where a bond-financed facility is owned by the political subdivision or exempt person but is operated by a nonexempt person under a contract. Obviously, the mere fact that a nonexempt person makes a profit, in his trade or business, with respect to certain aspects of bond-financed facilities, is not fatal. The architect who designs a state office building, and the contractor who constructs it, no doubt make a profit, but their activity ordinarily does not constitute a 'use' of the facility that will satisfy the 'trade or business' test. Often, bonds are issued to enable a political subdivision or exempt person to finance aspects of their governmental or exempt function. Sometimes the governmental or exempt function is carried out by way of contract with a nonexempt person who provides a commodity or service. Such arrangements do not necessarily amount to a 'use' of bond proceeds within the meaning of the 'trade or business' test. **We believe the test to be applied where a manager operates a bond-financed facility is whether the nonexempt person is merely providing a service or commodity to the political subdivision that owns or is responsible for the operation of the facility, or whether the nonexempt person is itself operating the facility as a proprietor** . . . . In the obvious and typical situations where the facilities are **leased** or sold to a nonexempt person, such person 'uses' the facility in the capacity of a proprietor . . . . On the other hand, a nonexempt person that . . . provides a service to the political subdivision may benefit from the facility in an indirect economic sense, but this does not amount to 'use' within the meaning of the 'trade or business' test, unless the involvement, whether direct or indirect, amounts to a proprietary use of the facility."[5]

To determine whether a service provider is merely providing a service, or is instead operating a bond-financed facility in a proprietary capacity, the 1978 Memo instructs taxpayers to consider (i) which party controls the use of the bond-financed facility, (ii) the term of the agreement, and (iii) compensation to the provider. Look familiar?

The 1978 Memo acknowledged that a management contract could convey a proprietary interest in a bond-financed facility if, for example, the service provider uses a bond-financed facility for its own benefit and not for the benefit of the owner of the facility. Unfortunately, there is no discussion of how to determine whether a service provider uses a bond-financed facility for its own benefit. In any event, the 1978 Memo strongly suggests that a proprietary interest is necessary for an agreement to result in private business use.

In Revenue Procedure 93-19, the IRS backed away from some of its assertions in the 1978 Memo. Likely emboldened by a 1986 acknowledgement by Congress that a management contract (as well as a lease) could result in private business use,[6] in Rev. Proc. 93-19 the IRS said that "[a] management or other service contract that gives a nongovernmental service provider a proprietary interest in the operation of a facility is not the only situation in which a contract may result in private business use of the facility."

In response to proposed private business use regulations promulgated in 1994,[7] commentators requested that the Treasury Department backtrack from the pronouncement in Rev. Proc. 93-19 and promulgate final regulations that conclude that a management contract should only give rise to private business use if it transfers a proprietary interest in financed property to the service provider. When Treasury finalized these regulations in 1997, the preamble explicitly rejected that request:

> "The final regulations . . . continue to reflect the view that Congress intended that a management contract can give rise to private business use even if it does not in substance transfer a leasehold or ownership interest to a nongovernmental person for general federal income tax purposes. Thus, the final regulations do not adopt the rule that a management contract gives rise to private business use only if it transfers a proprietary interest to a nongovernmental service provider. The final regulations provide that the determination of whether a management contract that does not meet the qualified management contract safe harbors gives rise to private business use is based on all the facts and circumstances."[8]

These 1997 regulations, read together with the 1978 Memo, make clear that a management contract can result in private business use based on all the facts and circumstances even if it (a) does not convey a proprietary interest to the service provider and (b) is not properly characterized as a lease.

Prior to Rev. Proc. 2016-44, it was much easier to identify certain management contracts that did not result in private business use based on all the facts and circumstances even though the contract did not qualify for one of the private business use safe harbors in Rev. Proc. 97-13.[9] Following Rev. Proc. 2016-44, the application of the facts and circumstances standard is significantly limited because contracts that do not fit within the Rev. Proc. 2016-44 safe harbor will often be characterized as lease agreements, which are not eligible for the fall-back facts and circumstances analysis.

Rev. Proc. 2016-44

A more comprehensive analysis of Rev. Proc. 2016-44 is here. Under Rev. Proc. 2016-44, a management contract fits within a private business use safe harbor if it meets the following criteria:

- The service provider's compensation is reasonable, and it isn't based on net losses or net profits of the bond-financed facility.
- The term of the contract is within permitted time limits.
- Control over the managed property generally remains with the owner.
- Risk of loss of the managed property generally remains with the owner.
- The service provider must take tax positions consistent with it being a manager and not a lessee of

the bond-financed facility.
- There are no circumstances substantially limiting the qualified user's ability to exercise its rights.

Certain of these criteria should look familiar. For example, control over managed property and risk of loss are two of the criteria explicitly mentioned in the 1997 private business use regulations as factors that distinguish management contracts from lease agreements.[10] Put another way, a management contract that conveyed too much control or the risk of loss to the service provider is not eligible to meet the "facts and circumstances" test because it is not a management contract. Furthermore, the ability to substantially limit a qualified user's ability to exercise its rights is another form of control, so arguably failing that requirement could also cause the agreement to be considered a lease.[11]

That leaves the following facts and circumstances criteria that are not already encapsulated by Rev. Proc. 2016-44:

- Reasonable compensation (incl. no net profits or net losses)
- Term of the contract
- Consistent tax positions

Although not drafted with tax-exempt bonds in mind, Section 7701(e) provides certain relevant criteria to distinguish a lease from a management contract. One of those criteria is whether the service provider has a significant economic interest in the property. In a 2015 letter to the IRS discussing the impact of Section 141 of the Code on public/private arrangements, the ABA Taxation Section interpreted Section 7701(e) and relevant case law as standing for the proposition that a "contract should be treated as a lease (as contrasted with a mere service contract), based upon . . . the operator's ability to share in both the combined revenues and expenses of the applicable enterprise."[12]

That leaves the following facts and circumstances criteria that are not already encapsulated by Rev. Proc. 2016-44:

- Term of the contract
- Consistent tax positions

The 1978 Memo indicates that when the term of a contract is "unreasonable," the continued possession and operation of the bond-financed facility may amount to de facto control and virtual ownership regardless of any provisions in the contract that give the qualified user supervisory control. Furthermore, long-term contracts that exceed the permitted length in Rev. Proc. 2016-44 may raise an inference that the contract conveys an ownership interest in the bond-financed facility which results in private business use without regard to any facts and circumstances.[13] In addition, for qualified 501(c)(3) bonds, another byproduct of a contract term in excess of the permitted length in Rev. Proc. 2016-44 is the possibility that the contract results in a violation of the ownership requirement in Section 145(a)(1).

Finally, a management contract will not run afoul of the consistent tax position requirement if the manager agrees "not to take any depreciation or amortization, investment tax credit, or deduction for any payment as rent with respect to the managed property." To the extent that the manager fails this requirement, it is very likely that the provider's interest in the bond-financed facility is greater than that of a service provider and that the contract is not properly treated as a management contract.

In sum, Rev. Proc. 2016-44 has, in effect, swallowed up many of the considerations that previously existed in the facts and circumstances test in the Treasury Regulations, and they have been instead imported into Rev. Proc. 2016-44's bigger safe harbor.

Conclusion

Following the release of Rev. Proc. 2016-44, many of the contracts that fail to qualify for the new safe harbor will likely be considered to convey a leasehold or ownership interest in the bond-financed facility for federal income tax purposes. Because agreements that convey a leasehold interest or an ownership interest may not be excluded from private business use based on all facts and circumstances, the relevance of the facts and circumstances test is diminished (maybe significantly) by Rev. Proc. 2016-44.

[1] Treas. Reg. § 1.141-3(b)(4)(i).

[2] PLR 201228029 (although compensation was not within Original Safe Harbors, it was not based on net profits so, based on facts and circumstances, the management contract did not result in Private Business Use); PLR 201145005 (although the term of the agreement exceeded what was permitted to qualify for the Original Safe Harbors, based on facts and circumstances, the management contract did not result in Private Business Use); PLR 200813016 (although compensation was not within Original Safe Harbors, it was not based on net profits so, based on facts and circumstances, the management contract did not result in Private Business Use); PLR 200330010; PLR 200222006

[3] As amplified by Rev. Proc. 2001-39 and Notice 2014-67 discussed here and here.

[4] The "facts and circumstances" test was not included in the Treasury Regulations until the Final Regulations (defined herein) were promulgated in 1997. Practically speaking, as illustrated in the detailed factual analysis in the 1978 Memo, even before the facts and circumstances test appeared in the Treasury Regulations, the IRS has always applied it.

[5] Emphasis added.

[6] Conference Report for the Tax Reform Act of 1986, H.R. Conf. Rep. No. 841, 99th Cong. 2d Sess. II-687, 1986-3 (Vol. 4) C.B. 687-88.

[7] 59 FR 67658.

[8] 62 FR 2275.

[9] See footnote 2.

[10] Treas. Reg. 1.141-3(b)(3)(i) and (ii).

[11] A valid argument could be made that the ability to "substantially limit" the exercise of the owner's rights and the "control" requirement are two separate requirements; however, consider the following language in the 1978 Memo: "[This control] requirement will be met if the [qualified user] retains control or a veto power over the decisions of the management company. To effectuate this requirement there should be no common or related members of the governing body or board of directors of the [qualified user] and the manager."

[12] Available here.

[13] Treas. Reg. § 1.141-3(b)(2).

Squire Patton Boggs

The Public Finance Tax Blog

By Joel Swearingen on September 23, 2016

IRS Says Florida Jail Bonds May Be Taxable.

WASHINGTON – The Internal Revenue Service has informally advised the Baker Correctional Development Corp. in Florida that $45 million of first mortgage revenue bonds it issued in 2008 are taxable.

BCDC disclosed the IRS' stance in a material event notice posted on the Municipal Securities Rulemaking Board's EMMA website this week.

Jeffrey Cox, finance director for the Baker County Sheriff's Office, said Thursday that the IRS audit found the bonds failed to meet the private payment use test due to the jail's large federal inmate population.

"From what I can gather from speaking with the IRS and our attorneys, it's a revenue problem," Cox said.

BCDC is currently exploring options to refinance the tax-exempt bonds ahead of an IRS potential adverse determination, according to the event notice.

Because BCDC has not received anything in writing from the IRS, Cox said it does not have any definitive plans on how and when it will refinance the bonds. It is relying on communication between its attorneys and the IRS.

"From those conversations, the IRS is wanting us to pull the bonds off the market as quickly as we can," Cox said. "We've interpreted that to be 60-90 days."

As of Thursday, the Baker County Detention Center, located in Macclenny, Fla., has 480 inmates, roughly 350 of which are federal.

The detention center, which opened in Sept. 2009 and is roughly 30 miles west of Jacksonville, is owned by BCDC and operated by the Baker County Sheriff's Office. BCDC was formed as a nonprofit in 2006 to acquire, construct, maintain and/or operate one or more jails in Baker County.

Jails in border states often have contracts to house inmates from the U.S. Citizenship and Immigration Service or the U.S. Marshals Service. The U.S. Immigration and Customs Enforcement's (ICE) enforcement and removal operations division began housing detainees at Baker County Detention Center in 2009 under an intergovernmental service agreement with Baker County, according to ICE.

Tax-exempt bonds become private activity bonds if more than 10% of the proceeds are used for private use and more than 10% of the debt service payments are from or secured by private parties. Under the federal tax code, PABs are only exempt if they are issued for "qualified" purposes; jails do not fall under a qualified category.

On average, the jail is comprised of roughly 60-70% federal inmates, Cox said, making it more than six times as high as the private payment test allows. That ratio has been relatively consistent over the past six years. The federal government pays BCDC $84.72 per day for each federal inmate it houses, Cox said.

The IRS opened its audit of BCDC's bonds a little over a year ago, according to Cox.

The IRS began a widespread audit of tax-exempt bond-financed jails about three years ago, especially those that housed a large amount of federal inmates. The federal government is deemed a private entity in under the federal tax code, while state and local governments are classified as governments.

BCDC's material event notice said that the jail has cooperated in the audit and is in discussions to resolve the issues raised, but added there "can be no assurance as to the ultimate outcome."

Peter Dame, a partner at Akerman, tax counsel for BCDC, told the bondholders Tuesday in a conference call that he and the IRS have set a "joint target date" to wrap up the audit by the end of October.

"The IRS has not been confrontational about this but obviously something needs to get done to resolve their audit. I think at this point they have all the information they need," he said.

Dame said Baker is considering refunding the jail bonds with a bank loan, but no letters of interest have been sought yet. PFM has been hired to advise the issuer on the refinancing.

According to the bonds' official statement, the Series 2008 first mortgage revenue bonds were issued to finance the acquisition of roughly 90 acres of land to use as the jail site, as well as the construction of a 512-bed jail facility to house inmates, administrative offices for the Baker County Sheriff's Office. Sell & Melton in Macon, Ga., served as bond counsel for the issue and Bergen Capital, a division of Scott & Stringfellow in Hasbrouck Heights, N.J., served as underwriter.

In 2011, BCDC entered a forbearance agreement for principal payments on the $45 million bond issuance in 2008. The move came after the jail had lower-than-projected inmate counts and higher-than-expected startup costs.

The 508-bed jail was constructed after the county's existing 132-bed jail reached its capacity and was in need of replacement, according to the OS for the bonds.

The Bond Buyer

By Evan Fallor

September 29, 2016

Shelly Sigo contributed to this story.

Fitch on Dedicated Tax Bonds.

Palomar Health, CA – Impact of Pledged Special Revenue Analysis on GO Bonds

Amy Laskey, Jim LeBuhn and Tom McCormick on Monday, September 26th discussed Palomar Health and Fitch's views on dedicated tax bonds.

Listen to the Audio.

S&P U.S. Not-For-Profit Health Care Stand-Alone Hospital Median Financial Ratios - 2015 vs. 2014

Similar to the overall medians for stand-alone hospitals and health care systems combined, we saw stronger operating margins for stand-alone hospitals in 2015 at each rating category, offset by consistently softer non-operating revenue compared to 2014.

Continue reading.

Sep. 21, 2016

S&P U.S. Not-For-Profit Health Care System Median Financial Ratios - 2015 vs. 2014

System medians, similar to the stand-alone medians, demonstrated operating margin improvement in 2015, which when combined with softer non-operating income produced modest coverage gains in the higher rating categories, with slight declines in the lower rating categories.

Continue reading.

Sep. 21, 2016

S&P U.S. Not-For-Profit Acute Health Care Speculative Grade Median Financial Ratios.

Speculative grade ratings are defined as those rated ‘BB+’ or below. Within speculative grade, a majority of the health care organizations are rated in the ‘BB’ category with fewer in the ‘B’ and ‘CCC’ categories.

Continue reading.

Sep. 21, 2016

S&P U.S. Not-For-Profit Health Care Small Stand-Alone Hospital Median Financial Ratios.

S&P Global Ratings defines a small stand-alone acute care hospital, which is a subset of our stand-alone hospital universe, as one having net patient service revenue below $125 million.

Continue reading.

Sep. 21, 2016

[S&P: U.S. Not-For-Profit Acute Health Care Ratios Are Calm On The Surface But Turbulent Underneath.]

The overall financial performance of U.S. not-for-profit acute health care organizations rated by S&P Global Ratings continued the improvement we saw last year when we returned the sector outlook to stable from negative, albeit at a more reserved pace.

Continue reading.

Sep. 21, 2016

S&P U.S. Not-For-Profit Health Care Children's Hospital Median Financial Ratios.

Children's hospital ratios are generally rated higher on the rating spectrum than stand-alone hospitals and more in line with health care systems even though most are stand-alone providers.

Continue reading.

Sep. 21, 2016

NABL: Minnesota Delegation Sends Letter to IRS on Political Subdivisions.

The members of the Minnesota congressional delegation from both parties sent a letter to Treasury Secretary Lew and Internal Revenue Service (IRS) Commissioner Koskinen, criticizing the IRS's proposed rule on the definition of political subdivision (REG-129067-15). The delegation expressed concern that the proposed rule would affect the diverse array of entities that provide essential services to Minnesota communities. The delegation specifically pointed to the "incidental private benefit" portion of the proposed rule and the unclear provisions regarding voter control of a political subdivision, saying those provisions could bar many entities from accessing tax-exempt financing for community projects.

The letter is available here.

TAX - VIRGINIA

Miller & Rhoads Building, L.L.C. v. City of Richmond

Supreme Court of Virginia - September 15, 2016 - S.E.2d - 2016 WL 4864888

Property owner brought action against city, claiming city failed to properly calculate and apply real estate tax exemption.

The Circuit Court determined that the exemption did not apply to the special district tax. Owner appealed.

The Supreme Court of Virginia held that the special district tax was not subject to the exemption.

City's annual special district tax on building was not subject to city's real estate tax exemption, under maxim of expressio unius est exclusio alterius, where city code provision regarding special district tax made tax subject to specifically mentioned sections, and sections providing for exemption were omitted.

Try These Weird Tricks to Split a Bond Issue Into Separate Portions: Squire Patton Boggs

Many of the tax-exempt bond rules apply to an "issue" of bonds. With a few exceptions, an issue of bonds includes all bonds sold by an issuer less than 15 days apart under the same plan of financing, if the debt service on those bonds is reasonably expected to be paid from the same source of funds. If an issuer wants to keep two sets of bonds separate, the usual technique is to sell them 15 days apart. But this can expose the bonds to market movements. Where an issuer does not want to take these risks, if bonds are treated as part of the same issue under this rule, what can be done to separate them?

Issuers may want to divide a bond issue into separate portions for many reasons. The most frequently encountered reason is to allow issuers to divide an issue into bonds that have been part of an advance refunding and bonds that haven't, to simplify how the one-advance-refunding rule applies to the issue and allow the issuer to advance refund complete maturities or complete portions of maturities, as opposed to advance refunding only a portion of all of the maturities.

Issuers can use several techniques by themselves or in combination to separate an issue into separate portions for many, if not all, purposes.

First, two important notes:

1. **Designating the bonds as separate series ("Series A" and "Series B") is neither necessary <u>nor sufficient</u> to separate a bond issue into separate portions for tax purposes.** Giving separate names to the separate series will help everyone track the separate purposes, and will make it easier for everyone to explain the separate purposes to people (like an IRS agent) who take an interest in the bond issue after it is issued. But the tax law – not the series designation – governs whether or not an issuer can separate the bonds of the issue into different portions.
2. We're **not** talking about the question of "allocating" different sources of funds to various expenditures for a bond-financed project. Different question, different rules, different consequences.

Separate Issue Treatment under Reg. 1.150-1(c)(3). The first technique for separating an issue of bonds is contained in Reg. 1.150-1(c)(3) (incidentally the same subsection of the regulations that defines an "issue" of bonds in the first place). The issuer can allocate bonds, proceeds, and investments to "separate purposes" of the issue, which means separate loans to conduit borrowers, refunding separate prior issues, truly separate capital projects, etc. This allocation must be made in writing on or before the issue date. (One common reason to make the separate issue election under

Reg. 1.150-1(c)(3) is to facilitate compliance with the $150 million nonhospital bond limitation imposed on qualified 501(c)(3) bonds.)

Unfortunately, the Reg. 1.150-1(c)(3) election does not apply for purposes of many of the big-ticket tax-exempt bond requirements. Specifically, it does not apply for purposes of the private business use rules, the arbitrage yield restriction and rebate rules, the advance refunding rules, the rules in Code Section 144(a) regarding small issue industrial development bonds, and the hedge bond rules. For those purposes, we use another technique.

Multipurpose Issue Allocation. If an issuer needs to separate an issue of bonds into separate purposes for certain arbitrage purposes (or, more often, for purposes of the one-advance-refunding rules), then the issuer can allocate those bonds (and their proceeds and investments of those proceeds) under the terms of Reg. 1.148-9. These rules allow an issuer to split the issue into separate portions for almost all purposes of the arbitrage rules, except for calculating the yield on the bonds (with limited exceptions), calculating the rebate amount, determining the minor portion and determining the portion of the issue eligible for investment in investments that can earn arbitrage as part of a reserve fund. The separate portions must, as in the technique under Reg. 1.150-1(c)(3), correspond to truly separate purposes of the issue. The most common example is separating an issue into new money and refunding portions (typically with a separate refunding portion for each refunded prior issue), but an issuer can further subdivide the new money portion of an issue into separate new money portions if, generally, the new money projects financed are not integrated or functionally related. The multipurpose issue allocation rules generally apply for purposes of the private business use rules (see Reg. 1.141-13(d) and Reg. 1.141-13(g), Example 5) and, most importantly, the one advance refunding rule (see Reg. 1.149(d)-1).

Unlike the election under Reg. 1.150-1(c)(3), a multipurpose issue allocation "may be made at any time, but once made may not be changed." Reg. 1.148-9(h)(2)(i). But, the rule always applies, although it has no effect until the issuer/borrower makes the allocation. This is why you will often see language regarding the multipurpose issue allocation in a tax certificate that says something to the effect of "no allocation is being made at this time, but at the future option of the issuer, the issuer can make an allocation according to [x]."

Special rules apply to the refunding portion of the issue. If an issuer wants to specify certain bonds of the issue as the refunding bonds (and avoid a pro rata piece of each bond being treated as a refunding bond), then those bonds must meet one of the following requirements. First, the refunding portion must reflect aggregate debt service that is "less than, equal to, or proportionate to" the debt service on the prior issue in each bond year. This is often called the "debt service savings" test, although, as the quoted language shows, you don't have to show savings. The rationale for this requirement is not abundantly clear from the regulations or their history, but it appears to be that refunding bonds are usually issued to capture debt service savings, and, "if it looks like a duck and sounds like a duck," then it must be a duck/refunding bond.

If the "debt service savings" test cannot be met, then an issuer can specify certain bonds as the refunding bonds if the weighted average maturity of the refunding bonds has the same ratio to the remaining economic life of the refunded assets as the ratio of the weighted average maturity of the new money bonds has to the remaining economic life of the new money assets. (As you can tell from reading the previous sentence, it's difficult to rely on this test, and it's basically impossible to meet this requirement by happenstance.) Finally, if the bonds that the issuer wants to specify as the refunding bonds can't meet either of these tests, the issuer must be able to show that it cannot meet these tests because of a state law prohibition or that the bonds were issued under certain old indentures; not that it will likely matter, but the regulations say that this one is "strictly construed." Failing that, the issuer is stuck with the conclusion that each group of substantially identical bonds (for example, bonds having the same maturity date) has a pro rata flavor swirl of the various portions of the issue. A number of other detailed rules apply to figure out the precise amount of proceeds allocated to each of the portions and to allocate common costs of the various portions among the portions.

To emphasize again, when an issuer wants to separate a bond issue into various portions, the issuer must meet the above requirements, whether or not it designates the refunding bonds as a separate series for securities purposes.

Other separation techniques exist. For example, an issuer of bonds to finance facilities that will be used in part by governmental entities and in part by 501(c)(3) organizations that are technically part of a single issue can treat them as separate issues of governmental use bonds and 501(c)(3) bonds if the separate portions, treated as separate issues, satisfy the tax-exempt bond requirements separately. The Conference Report for the Tax Reform Act of 1986 states that "the conferees intend that, where an issue consists of two components – governmental financing and qualified 501(c)(3) financing – and the two components, **viewed as separate issues**, satisfy all requirements for tax-exemption. . . ." Conf. Rpt. 99-841, at II-726. (Emphasis added.)

Below is a diagram to illustrate how some of these rules overlap, using a simple example of an issue of bonds that an issuer wants to separate into a new money portion and a refunding portion.

Click here to view the image.

Squire Patton Boggs – John W. Hutchinson

USA September 15 2016

Tax Incentive Evaluation in 2016 - in Law and Practice.

Many states have made progress in recent years toward regular, rigorous evaluations of their economic development tax incentives. In the 2016 legislative session, Alabama, Colorado, Hawaii, Virginia, and Utah enacted laws requiring regular evaluation, while several other states made progress to implement evaluation laws passed in previous years. As a result, lawmakers in numerous states will soon have evidence on the results of their incentives—information that they can use to improve the effectiveness of the programs.

Continue reading.

The Pew Charitable Trusts

September 14, 2016 | Economic Development Tax Incentives | By Josh Goodman and John Hamman

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Hawkins Advisory (Modifications to Qualified Management Contract Rules)

This issue of the Hawkins Advisory summarizes IRS Revenue Procedure 2016-44, issued on August 22, 2016. The Revenue Procedure purports to modify and supersede existing IRS safe harbors for management contracts involving property financed with tax-exempt bond proceeds.

Read the Advisory.

9/22/2016

NASACT Responds to IRS Proposal on Amending the Definition of Political Subdivision for Municipal Bond Purposes.

Read the NASACT's letter.

IRS Requests Comments on Private Activity Bond Election Form 8328.

The IRS has asked for public comment on Form 8328, "Carryforward Election of Unused Private Activity Bond Volume Cap."

Comments are due by November 14.

Brookings Stadium Study Draws Criticisms.

WASHINGTON – A Brookings Institution study claiming professional sports stadiums built or renovated with tax-exempt bonds during the last 16 years have cost the federal government $3.7 billion has drawn some criticism from a sports consultant and municipal market participants.

The 28-page study – Tax-Exempt Municipal Bonds and the Financing of Professional Sports Stadiums – recommends that tax-exempt financing be prohibited or limited for professional sports stadiums.

The study, authored by Brookings economists Ted Gayer and Austin Drukker, as well as researcher Alexander Gold, focuses on professional football, baseball, basketball and hockey stadiums built, significantly renovated, or under construction since 2000. Of the 45 stadiums that fit this description, 36 were funded, at least in part, by tax-exempt bonds.

The total principal amount of the tax-exempt bonds used for the stadiums was $13.0 billion, according to the study.

The authors found the federal subsidies to issuers totaled $3.2 billion, based on interest rate spreads between tax-exempt and taxable bonds, at present value using a 3% discount rate and 2014 dollars. They said the federal government suffered additional revenue losses of $500 million due the "windfall tax break[s]" from the bonds for high-income earners, also assuming a 3% discount rate and 2014 dollars.

The authors claim there are no studies that provide evidence that such stadiums benefit local economies.

"The evidence for these spillover gains is weak," they said. "Academic studies consistently find no discernible positive relationship between sports facility construction and local economic development, income growth or job creation."

But Bob Boland, with Boland Sports Practice who is also executive-in-residence and director, Master of Sports Administration and MBA/MSA dual-degree programs at Ohio University, suggested the study is flawed because it's impossible to paint sports facilities with a broad brush. Stadiums should instead be examined on a case-by-case basis, he said.

Boland said the Brookings study fails to take into account the economic development that has occurred in areas surrounding some professional sports stadiums.

He cited as an example the Verizon Center sports and entertainment arena used by the National Basketball Association's Wizards and the National Hockey League's Capitals that revitalized the Gallery Place and Chinatown areas of D.C. with many new restaurants and retail stores.

In Indianapolis, the Lucas Oil Stadium used by the National Football League's Colts and the Bankers Life Fieldhouse used by the NBA's Pacers have spurred economic development in that city's downtown area. Also, the new Yankee Stadium in New York City supported a neighborhood in the south Bronx that was starting to deteriorate, he said.

Jessica Giroux, general counsel and managing director of federal regulatory policy at Bond Dealers of America said the report ignores some of the benefits munis provide to states and localities.

"One of the most important aspects of tax-exempt bonds is that state and local governments have the ability to prioritize which projects to spend their revenue and tax dollars on without having to go through the federal process," she said. "The report ignores this aspect of tax-exempt financing and also misses the point that the true beneficiaries of the tax exemption, which are the local taxpayers who benefit from the financed projects and reduced borrowing costs associated with the usage of tax-exempt bonds to finance necessary infrastructure projects."

George Friedlander, managing director, Municipal Macro Policy and Strategy at Citigroup, Inc., said the study authors note the federal government can't control what projects get done. "They're calling that an evil, but state and local governments would call that a benefit."

Because state and local governments are spending their own money, they are more likely to finance good, he said.

Friedlander, who stressed he doesn't have a view on tax-exempt financing of stadiums, said that in his view the study is flawed in making the case for eliminating or limiting tax exemption.

"One of the things they do wrong," he said, is that they base their findings in part on the interest rate spreads between munis and corporates.

"Everyone else in the entire world, including [the Joint Committee on Taxation] has done it on a ratio basis," he said. They compare muni bond yields as a percentage of corporate bond yields.

He said that in his view the Brookings researchers should not have merely compared Moody's Investors Service's muni and corporate indices. "That doesn't tell you what a muni yield would have to be if it were taxable," he said.

The researchers, in addition to using a ratio, should have figured in at least three other factors to get an "apples-to-apples comparison," he said.

First, he said, the authors should have realized that the corporate bonds in the corporate index are typically a very large size, extremely liquid and show narrow bid/offer spreads. In contrast, the munis in the muni index, tend to be small and less liquid, with larger bid/offer spreads.

Second, “the call right has to be priced in,” he said. The study looks at 20-year or longer munis and corporates. Corporates typically have “make whole calls,” which discourage issuers from calling them. Munis, in contrast, have 10-year call dates, and issuers often benefit from calling the bonds.

Finally, there are more stringent disclosure requirements for corporate bonds. Investors would want a little extra yield for munis, which don’t have as stringent disclosure requirements.

“In an apples-to-apples comparison the ratio would be about 71% for large issuers and 68% for small issuers,” showing munis are “vastly more efficient than what [Brookings] is showing,” Friedlander said. A smaller ratio means that a larger part of the benefit is going to issuers not investors, he said.

The study recommends that tax-exempt financing be prohibited or limited for professional sports stadiums.

Bonds can be eliminated, the authors said, by removing the so-called “private use test” for stadium financings, as proposed by President Obama in recent budget proposals.

“The simplest and most direct way to address this inefficient federal subsidy would be to eliminate the private payment test for sports stadiums,” the study’s authors said. Stadiums would never be able to meet the private use test, they said.

“An alternative approach would limit the federal tax subsidy by classifying stadium bonds as qualified private activity bonds, which would make them subject to a state-wide volume cap, place additional restrictions on their use, and allow financing of the bonds through taxes directed at the beneficiaries of the stadiums,” the study said.

Currently these state volume caps equal $100 per capita or $302.88 million, whichever is greater, for each state and the District of Columbia.

According to the study, for the first half of the twentieth century, local professional sports franchises funded the construction of most stadiums, it said. The Revenue and Expenditure Control Act of 1958 restricted the projects involving private parties that could be financed with tax-exempt bonds. Under that law, bonds would be taxable if more than 25% of the proceeds were used by a private party and more than 25% of the debt was paid for or secured by a private party. But the law exempted sports stadiums from those restrictions.

The Tax Reform Act of 1986 eliminated sports stadiums from being exempt from the private use and payment tests, while also reducing those tests to 10% from 25%. But this backfired, according to the study. To be eligible for tax-exempt financing, stadium bond issues had to be structured so that no more than 10% of their debt was used or secured by private sports franchises.

“This sets up a kind of matching incentive, an ‘artificial financing structure’ whereby federal tax exemption is granted if the state or local government is willing to finance at least 90% of the debt service for the bonds,” the study said. “Additionally, since this 90% of financing cannot come even indirectly from private activity if tax exemption is to be maintained, the state or local government cannot rely on stadium generated revenue, such as a tax on entry tickets to the stadium or event, or even rent collected from the team as tenants.”

The Tax Reform Act of 1986 “effectively requires that, in order to receive the federal subsidy, a state or local government must finance the bulk of the stadium, and it must rely on tax revenue unrelated to the stadium for the financing, such as general sales taxes, property taxes, income taxes, lotteries, or taxes on alcohol or cigarettes,” the study said.

The Bond Buyer

By Lynn Hume and Evan Fallor

September 14, 2016

TAX - VERMONT

TransCanada Hydro Northeast Inc. v. Town of Rockingham

Supreme Court of Vermont - September 9, 2016 - A.3d - 2016 WL 4718020 - 2016 VT 100

Taxpayer, which was an independent wholesale power producer, sought judicial review of town board of civil authority's valuation of hydroelectric facility for property taxation purposes.

State intervened on behalf of town. Following a bench trial, the Superior Court entered judgment setting value of facility at $130,000,000. Taxpayer appealed.

The Supreme Court of Vermont held that:

- Trial court did not err in relying on debt rate proffered by town's expert appraiser, as element of discounted cash flow (DCF) method for determining fair market value of facility;
- Trial court acted within its discretion in relying on calculation of capital expenses proffered by town's expert appraiser, as element of DCF method for determining fair market value of facility;
- Trial court acted within its discretion in relying on estimate of cost of federal relicensing for facility, as element of DCF method for determining fair market value of facility;
- Record supported trial court's finding that three upward adjustments from computed average values were warranted under comparable sale method for determining fair market value of facility; and
- Offer and sale announcement of other hydroelectric facilities were not reliable evidence of fair market value, and thus could not be used in comparable sale method for determining fair market value of facility.

Trial court did not err in relying on 6% debt rate proffered by town's expert appraiser as appropriate calculation of debt-rate element of discounted cash flow method for determining fair market value of taxpayer's hydroelectric facility for property tax purposes, though taxpayer asserted 6% rate was below-market debt rate. Expert calculated 6% debt rate based on taxpayer's own reported debt payments as well as those made by similar corporations, taxpayer did not demonstrate that expert's debt rate was invalid and failed to produce data to contradict calculation, and trial court found that expert was able to demonstrate market basis for his debt rate, which it found to represent sound estimates and valid inputs.

Trial court acted within its discretion in relying on calculation of capital expenses proffered by town's expert appraiser, as part of projected expenses for net revenue element of discounted cash flow method for determining fair market value of taxpayer's hydroelectric facility for property tax purposes, and rejecting approach by taxpayer's expert, though taxpayer asserted calculation by town's expert, including assignment of 1% of value of facility per year to long-term capital improvements, ignored future capital costs for necessary and planned capital improvements, including overhaul of turbines; town's expert explained his analysis and treatment of capital expenditures, and trial court carefully explained its decision process and how it was influenced by parties' expert testimony.

Trial court acted within its discretion in relying on estimate by town's expert appraiser of cost of federal relicensing for taxpayer's hydroelectric facility, and rejecting approach by taxpayer's expert appraiser, as part of projected expenses for net revenue element of discounted cash flow method for determining fair market value of facility for property tax purposes. Trial court considered both parties' estimates for cost of relicensing, finding taxpayer's expert offered little support for its estimates and calculations and that town's expert offered more plausible estimate of likely costs and risks associated with relicensing, and trial court explained its decision-making process and how it was influenced by experts' testimony.

Record supported trial court's findings that three upward adjustments from computed average values for other hydroelectric facilities, based on-peak and off-peak power generation, ancillary revenue, and premium for taxpayer's facility, were warranted under comparable sale method for determining fair market value of taxpayer's facility for property tax purposes, where town's expert appraiser explained basis for his adjustments, including features of river and taxpayer's facility that elevated it above the average hydroelectric facility, such as amount of water on river, taxpayer's control over that water, ability of facility to use water, and river head and marketplace which taxpayer could sell into.

Sale announcement and offer for other hydroelectric facilities could not be relied upon in determining fair market value of taxpayer's hydroelectric facility for property tax purposes under comparable sales method of valuation, since announcement reflected mere hope rather than price which property would bring when offered for sale, and, though offer represented what property would bring in market if sale was completed, it did not rise to level of reliability demanded to estimate fair market value.

TAX - OHIO

Evans v. Avon

Court of Appeals of Ohio, Ninth District, Lorain County - August 22, 2016 - N.E.3d - 2016 WL 4426407 - 2016 -Ohio- 5460

Hotel patron brought action against city and its finance director, asserting additional 3% lodging tax in ordinance was illegal, and seeking to enjoin city or its agents from collecting the tax.

The Court of Common Pleas entered judgment declaring ordinance illegal, and granting patron injunctive relief. Defendants appealed.

The Court of Appeals held that:

- City ordinance that imposed an additional 3% excise tax to fund a newly established visitors bureau was illegal, and could not be collected by the city or its finance director, and
- City ordinance was not a lawful exercise of city's home rule authority.

Statutory provision that only allowed the levying of an additional 3% excise tax on all hotel and motel lodging when the county had not yet enacted its own lodging tax applied to both corporate municipalities and townships located within the county, and thus, city ordinance that imposed an additional 3% excise tax to fund a newly established visitors bureau was illegal, and could not be collected by the city or its finance director, where county had already enacted its own lodging tax.

Statute governing which subdivisions may levy an excise tax on lodging of transient guests preempted city ordinance that purported to impose an additional 3% lodging tax, and thus, city ordinance was not a lawful exercise of city's home rule authority. The statute specifically stated that a municipal corporation or township could only levy a lodging tax if it was not located in a county that had in effect a resolution that already levied an excise tax.

State constitution's grant of authority to exercise all powers of local government includes the power of taxation. However, while municipal governments have plenary taxing power, the General Assembly has the authority to impose specific limits on that power.

TAX - OREGON

Falls Apartments, LLC v. Multnomah County Assessor

Oregon Tax Court, Magistrate Division, Property Tax - August 4, 2016 - 2016 WL 4167515

Plaintiff appealed the real market value of its property for the 2015–16 tax year.

The subject property is part of a Construction In Process ('CIP') exemption in which the improvements on the subject property are not subject to taxation. Therefore, only the land valuation is being taxed for the 2015/2016 tax year. The subject property's 2015–16 tax roll real market value was $3,917,000. Plaintiff requested that the subject property's 2015–16 real market value be reduced to $3,773,655, based on the its actual cost.

The County Assessor moved for dismissal because Plaintiff's 2015–16 requested real market value would not provide any sort of tax savings as a result of the CIP.

The issue presented was whether Plaintiff is aggrieved under ORS 305.275(1)(a) for the 2015–16 tax year. Under ORS 305.275(1)(a), a taxpayer "must be aggrieved by and affected by an act, omission, order or determination of" a county board of property tax appeals or a county assessor, among others. Generally, so long as the property's maximum assessed value is less than its real market value, a taxpayer is not aggrieved.

Plaintiff conceded that it's requested 2015-16 real market value would not result in a reduction of the subject property's 2015-16 assessed value or property taxes because the subject property is under the CIP exemption. Plaintiff argued that it is nevertheless aggrieved for the 2015–16 tax year because of a protection afforded taxpayers under Article XI, section 11(2) of the Oregon Constitution, which states in part:

> "After disqualification from partial exemption or special assessment, any additional taxes authorized by law may be imposed, but in the aggregate may not exceed the amount that would have been imposed under this section had the property not been partially exempt or specially assessed for the years for which the additional taxes are being collected."

Under Plaintiff's reading of that constitutional provision, Plaintiff had the right to 'lock in' the assessed value for 2015–16 as it would have been if it had been valued correctly without the exemption.

The Tax Court ruled that Plaintiff was not aggrieved under ORS 305.275(1)(a) for the 2015–16 tax year.

The Court agreed with the County Assessor that Plaintiff may assert a claim when the subject property is no longer exempt under the CIP program. At that point, the subject property's maximum assessed value will be determined taking into account the new improvements and Plaintiff may appeal if it disagrees with the assessment.

GFOA, NABL Issue Guidance on Post-Issuance Tax-Compliance.

The Government Finance Officers Association ("GFOA") and the National Association of Bond Lawyers ("NABL") have issued guidance to issuers and their counsel on developing policies to maximize continuing compliance with the tax-exempt bond rules after the issuance of tax-advantaged bonds. The two organizations cooperated on the issuance of separate but complementary guidance to their respective members.

Post-issuance tax compliance procedures describe the courses of action to be taken by an organization to maximize the likelihood that tax rules applicable to tax-advantaged bonds – tax-exempt bonds, tax credit bonds and direct pay bonds – are followed after the bonds are issued and while the bonds remain outstanding. Post-issuance tax compliance procedures have two fundamental purposes: to enhance the likelihood of compliance with rules and to facilitate and streamline the organization's administrative functions.

Broadly speaking, the tax rules applicable to tax-advantaged bonds address four principal categories: (1) expenditure of proceeds; (2) use of financed assets; (3) investment of proceeds; and (4) recordkeeping.

GFOA's alert, *Developing and Implementing Procedures for Post-Issuance Tax Compliance for Issuers of Governmental Bonds*, is available here. NABL's *Considerations for Developing Post-Issuance Tax Compliance Procedures* is available here.

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Developing and Implementing Procedures for Post-Issuance Tax Compliance for Issuers of Governmental Bonds.

Introduction

State and local government issuers of tax-exempt bonds must comply with federal tax rules both at the time the bonds are issued and during the entire period the bonds are outstanding in order for the bonds to maintain tax-exempt status.1 For the last decade, the Internal Revenue Service (IRS) has engaged in extensive enforcement of these rules for tax-exempt bonds through a variety of activities including random audits. If an issuer fails to meet applicable federal tax rules, the IRS can declare the interest on the bonds to be taxable, although the IRS has not frequently done so.2 In connection with these enforcement efforts, the IRS has encouraged issuers to develop post-issuance compliance policies and procedures to help detect and correct potential violations of federal tax law on a timely basis.

The National Association of Bond Lawyers (NABL) released together with this GFOA Alert a white paper entitled "Considerations For Developing Post-Issuance Tax Compliance Procedures" (the "NABL Considerations"), which presents an in-depth discussion of post-issuance tax compliance and the applicable tax requirements that must be satisfied. This Alert provides a general overview of post-issuance tax compliance and highlights points that may be discussed in greater detail in the NABL Considerations or other publications.3 The Alert focuses on compliance for "governmental bonds," (i.e., bonds issued for governmental use and purposes) but can be helpful for complying with qualified 501(c)(3) or other types of private activity bonds.

What is Post-Issuance Compliance?

Post-issuance compliance consists of practices and procedures designed to assist an issuer of governmental bonds in complying with the federal tax requirements that apply from the date the bonds are issued until the date the bonds, or any refunding bonds, are no longer outstanding. The substantive rules can be categorized as: (a) arbitrage and rebate; and (b) use of bond proceeds and of bond financed facilities. Compliance with these rules must be documented by records that meet IRS requirements.

Why Implement Post-Issuance Compliance?

The IRS has encouraged issuers to adopt post-issuance compliance procedures in order to assist in preventing, identifying and correcting possible tax violations that may occur during the term that tax-exempt bonds are outstanding. These procedures help an issuer prevent or correct violations so the IRS does not have a reason to either declare the bonds taxable or negotiate a settlement. The IRS Forms 8038 that must be filed when bonds are issued ask whether the issuer had written procedures and the IRS previously offered issuers with written procedures the possibility of a lower settlement amount in connection tax violations discovered by the issuer for which the issuer sought a closing agreement pursuant to the IRS's Voluntary Closing Agreement Program (VCAP). More recently, the IRS is offering a lower settlement amount if the issuer has "effective" procedures (whether or not written).4 Procedures may also prove helpful in providing information and documentation in the event that the IRS audits an issue. See "Why are Post-Issuance Tax Compliance Procedures Important" in the NABL Considerations.

What Rules Need To Be Monitored?

For governmental bonds, i.e., bonds issued by state and local governments to finance public purpose projects, in the broadest terms, the tax requirements can be grouped into two categories: (a) arbitrage and rebate; and (b) use of bond proceeds and of bond-financed facilities. Each of these categories involve many rules that make it advisable for an issuer to adopt practices that track how bond proceeds are invested and how and when bond proceeds are spent.

Arbitrage and Rebate

Federal tax law and regulations restrict the amount of "arbitrage" an issuer can earn and retain from investing proceeds of a tax-exempt bond.5 As applied to tax-exempt bonds, "arbitrage" generally refers to the profit earned from taxable investments purchased with proceeds of bonds bearing interest at tax-exempt rates. There are two main categories of requirements – yield restriction and rebate. If ***either*** the yield restriction requirements ***or*** the rebate requirements are not satisfied, tax-exempt bonds become "arbitrage bonds" and lose their tax-exempt status.*6*

Yield Restriction

The general rule of "yield restriction" is that bond proceeds may not be invested at a "materially higher" yield than the yield on the bonds.7 Exceptions to this rule apply during "temporary periods" such as the 3-year temporary period that is available for proceeds that an issuer expects to spend on construction or acquisition of capital projects under certain circumstances.8 Additional exceptions including other temporary periods of varying length may apply.9 If there is no exception or a temporary period ends and proceeds remain unspent, either the investments must be yield restricted or a "yield reduction payment" must be made to the federal government.

Rebate

The general rule is that any actual earnings in excess of the yield on the bonds must be paid as "rebate" to the federal government. There are a number of possible exceptions including the $5,000,000 "small issuer" exception for issuers with general taxing powers who do not issue more than $5,000,000 in bonds during a calendar year, and limited exceptions for earnings on a reasonably required debt service reserve fund and on a bona fide debt service fund. There is also an exception for tax and revenue anticipation notes, for proceeds invested in other tax-exempt obligations and exceptions that apply if proceeds are spent within 6-months, 18-months or 2 years for construction.10 Rebate, if any, is due every 5 years or when bonds are paid off, either at maturity or redemption. If there is no rebate exception, it is necessary to determine whether any rebate is due. The calculation depends on a number of factors including whether the bonds are fixed or variable rate and whether there are any hedges (e.g., interest rate swaps) that must be taken into account.

To comply with both the yield restriction and rebate rules an issuer needs to have procedures that identify the type of, and return on, investments made with bond proceeds and when proceeds are spent.

Use of Proceeds and of Bond-Financed Facilities

The general rule for governmental bonds is that no more than 10% of bond proceeds may be used in a private business use and no more than 10% of debt service on the bonds may be paid or secured by payments arising from or related to private business use. The 10% limit is reduced to 5% in the case of unrelated private business use or related business use which is disproportionate. No more than 5% of bond proceeds may be used for and no more than 5% of debt service on the bonds may be paid or secured by payments in respect of, unrelated private business use or disproportionate related business use. In addition, with certain exceptions, no more than the lesser of 5% of bond proceeds or $5,000,000 may be used to finance direct or indirect loans to non-governmental persons.11

To monitor compliance with this requirement, an issuer needs to have procedures to identify who is a private "nonqualified user" and what constitutes private business use. For governmental bonds, any user other than a state or local government is a "nonqualified user". This means that individuals, for-profit entities, non-profits including section 501(c)(3) organizations and the federal government are "nonqualified users," and use by users in any of these categories must be analyzed to determine whether it is "private business use". Use in the trade or business of any non-qualified user is "private business use". Use by the general public is not typically business use. "Private business use" can be created by a lease or license of a bond financed facility. It can also be created through a management or service contract between the issuer (or other qualified user) and a non-qualified user on terms that do not meet a safe-harbor recognized by the IRS12 that gives the non-qualified user a share in the net profits from the use of the facility. Research agreements or special arrangements that give a non-qualified user priority or a benefit not available to the general public may also create private business use.

When are Procedures Effective?

To be effective, procedures should address the substantive issues necessary to assure tax and other legal and contractual compliance. Procedures should also be implementable, manageable, and diligently followed by the issuer. The design and implementation should take into account the issuer's size, organizational structure, frequency of bond issuance and budget/staffing resources.

If implemented properly, the following elements should assist an issuer with effective oversight of tax rules relating to tax-exempt bonds: (1) identify the individual or individuals responsible for coordinating activities; (2) provide for due diligence review at regular intervals; (3) facilitate training for responsible individuals; (4) describe retention of adequate records to substantiate compliance; (5) accommodate review that identifies areas that are most susceptible to noncompliance; and (6) include procedures to correct identified noncompliance in a timely manner.

Designing a Post-Issuance Compliance Program

General Considerations

A post-issuance compliance program should reflect an issuer's size, resources and borrowing pattern. An issuer may decide to handle compliance in-house or to engage bond counsel or other third-party provider for some or all compliance activities including arbitrage, rebate and monitoring of private business use and payments. In either case, the post-issuance compliance program should have the following elements. The following is a summary of the considerations for designing a post-issuance compliance program. More detail is provided under the heading "Characteristics of Effective Procedures" in the NABL Considerations.

Responsible Staff Should Be Assigned

Whether an issuer will conduct compliance in-house or will engage providers, a "chief compliance officer" with overall responsibility for implementation of the program should be assigned. In a large organization, there may be staff in addition to the chief compliance officer that can be assigned specific responsibilities or the chief compliance officer can have authority to delegate where appropriate. If third-party providers will be engaged to perform some or all of the activities, the program should specify how the providers will be engaged and monitored. The chief compliance officer or officers should be designated by job title rather than name to assure continuity.

Identify the Source of the Tax Requirements Being Monitored

It will be helpful to identify the documents that set forth the tax requirements being monitored so that the compliance officer(s) can find details if necessary.

Identify the Frequency of the Actions to Be Undertaken

The IRS has recommended at least an annual review as a general matter. However, it may be advisable to provide for a review when specific events occur, such as renewal of management contracts, or other events that may result in private business use. A program should also provide for a final allocation of bond proceeds as required by tax regulations.13

Establish a Deadline Reminder System

Where deadlines exist, a reminder system should be established and a back-up reminder is helpful in avoiding an oversight. Examples of deadlines include ending of temporary periods for yield restriction and deadlines for meeting spend down exceptions for rebate compliance, paying rebate if applicable, and making final allocations.

Identify Records to be Maintained and the Record Retention Period

Records necessary to assure and document compliance should be maintained for the required time periods. The issuer should list the records being maintained and where or by whom. Tax records must be maintained until full payment of the bonds and any refunding bonds plus three years. In addition, state or local record retention requirements need to be considered. In some cases, an issuer may need to seek approval for changes in its record retention policy in order to keep tax or other records for periods longer than otherwise permitted under state law.

Specific to tax-exemption compliance, the following records should be maintained.

1. The bond transcript for each bond issue (which includes among other documents, the trust indenture, loan, lease, or other financing agreement, the relevant IRS Form 8038 (including Forms 8038-G or 8038, as applicable) with proof of filing, the bond counsel opinion and the tax agreement including all attachments, exhibits and any verification report).
2. Records of debt service payments for each issue of bonds.
3. Documentation evidencing the expenditure of bond proceeds, such as construction or contractor invoices and receipts for equipment and furnishings, bond trustee requisitions and project completion certificates, as well as records of any special allocations made for tax purposes including post-issuance changes in allocations.
4. Documentation evidencing the lease or use of bond-financed property by public and private sources, including, but not limited to, service, vendor, and management contracts, research agreements, licenses to use bond-financed property, or naming rights agreements.
5. Documentation pertaining to investment of bond proceeds, including the yield calculations for each class of investments, actual investment income received from the investment of proceeds, investment agreements, payments made pursuant to investment agreements and rebate calculations and copies of any 8038-T or 8038-R filed with respect to the bonds.
6. Documentation pertaining to remedial action and other change-of-use records.
7. Amendments and other changes to the bond Documents (including interest rate conversions and defeasances).
8. Letters of credit and other guarantees for bond issues.
9. Interest rate swaps and other derivatives that are related to bond issues.

Require Training for Responsible Officers

Periodic training for compliance officers should be identified and documented. The issuer should also determine whether the training can be done in-house or whether third-party conferences, courses or providers are appropriate.

Describe Procedures to Identify and Correct Violations

The policy should describe the review process to assure compliance and describe what actions will be taken to correct any non-compliance. Corrective strategies may require engaging counsel or third-party advisors to assist in the remedial action.

Address Other Substantive Issues for Tax-Advantaged Bond Compliance

The policy should also consider other substantive matters that should be included in a post-issuance compliance program for tax-advantaged bonds such as yield restriction, rebate and tracking possible private business use.

How Should A Post-Issuance Program Be Adopted and Reflected?

An issuer's post-issuance compliance procedures can be included in its general debt management policies or be stated separately. Procedures may be adopted by formal action of the issuer's governing board or be developed independently by management.

Conclusion

GFOA recommends that state and local governments adopt comprehensive written debt management policies, in so doing, the GFOA and NABL work together to provide tools for the state and local government to use in managing these policies, such as the Post Issuance Compliance Checklist. This Alert provides a general overview of the NABL white paper "*Considerations for Developing Post-Issuance Tax Compliance Procedures*" and in so doing, this Alert brings additional awareness to post-issuance tax compliance for issuers within the parameters of federal tax rules. Compliance with federal tax rules both at the time a state or local government issues bonds and during the entire period the bonds are outstanding is necessary in order for the bonds to maintain their tax-exempt status is enforced through current federal tax rules.

Footnotes

1. State and local governments may also issue tax-credit and taxable direct-pay bonds that must satisfy federal tax rules on a continuing basis to retain tax-advantaged status. References herein to tax-exempt bonds also refer to tax-advantaged bonds.
2. If bonds are declared taxable, the tax must be collected from bondholders. The IRS has chosen in most instances to negotiate settlements with the issuers.
3. This Alert together with the NABL Considerations updates information about this topic previously provided through the joint publication with the National Association of Bond Lawyers (NABL) in 2007 of the NABL/GFOA Post-Issuance Compliance Checklist (the "Checklist") and in GFOA's best practices for debt management policies released in 2012. The debt management policies best practices publication is available online.
4. See Internal Revenue Manual ("IRM") 7.2.3.4.4 relating to the IRS's Voluntary Closing Agreement Program (VCAP), which was released in September 2015. This IRM states: "Under this revision of the IRM, post issuance compliance procedures are not required to be in any other pre-specified format. To obtain a TEB VCAP, however, an issuer is required to provide evidence that it has implemented a change to its procedures that is reasonably expected to prevent the same type of violation from happening in any of its bond issues. This change to the procedures is being made to allow issuers to develop their own best practices for post-issuance compliance procedures and to measure the benefit of those procedures by their effectiveness, that is, whether they enable the issuer to capture a violation quickly. TEB continues to strongly encourage issuers to have post-issuance compliance procedures that effectively monitor compliance with all of the IRC and Regulations requirements applicable to the bonds." (Emphasis added).
5. Internal Revenue Code §148 and regulations thereunder.
6. See "Tax Exempt Bonds: A Roadmap to Arbitrage Requirements for Tax-Exempt Governmental Bonds and Qualified Section 501(c)(3) Bonds of Smaller Issuers and Conduit Borrowers", 2013 Report of the Advisory Committee to Tax-Exempt and Governmental Entities (referred to herein as "Twelfth ACT Report").
7. For "new money" bonds, as a general rule, "materially higher" means 1/8 of 1% and for advance refunding bonds, "materially higher" is 1/1000 of 1%. Treas. Reg. §§1.148-2(d)(2)(i) and (ii).
8. This exception applies if, at the time of bond issuance, the issuer reasonably expects to become obligated to spend at least 5% of bond proceeds within 6 months, to allocate at least 85% of proceeds on the financed project within 3 years and to complete the project with due diligence.

Treas. Reg. §1.148-2(e)(2)(i)(A)(B) and (C).

9. Temporary period exceptions of varying lengths are also available for bona fide debt service funds, investment proceeds, working capital and refundings. See Treas. Reg. §1.148 -2 (2 and 1.148-9 (d). In addition, there are exceptions for a reasonably required debt service reserve fund and a "minor portion" of the lesser of $100,000 or 5% and for investments in other tax-exempt obligations. Treas. Reg. §1.148-2(d)(2)(v), (f) and (g).
10. See "Exceptions to Rebate", Section VC of the Twelfth ACT Report, supra for a discussion of the exceptions to rebate.
11. Issuers should consult bond counsel for detailed information about the rules that apply to private business use and payments in respect of private business use.
12. Rev. Proc. 97-13 as modified by Rev. Proc. 2001-39 and as amplified by Notice 2014-67, and Rev. Proc. 97-14 as modified by 2007-47 provide safe harbors against "private business use" for management contracts and research agreements
13. Treas. Reg. §1.148-6(d) requires that expenditures be allocated to bond proceeds no later than 18 months after the later of the date the expenditure is made or the project is placed in service and in no event later than 60 days after the 5th anniversary of the date the bonds are issued or retired, if earlier.

IRS Publishes New Management Contract Safe Harbors For Property Financed With Tax-Exempt Bonds: Foley & Lardner

On August 22, 2016, the Internal Revenue Service (IRS) released Rev. Proc. 2016-44, which provides new guidance on the treatment of "management contracts" for purposes of the restrictions on use of property financed with tax-exempt bonds. This published guidance provides for new safe harbors under which the IRS will not treat management contracts as giving rise to private business use.

The new guidance applies to tax-exempt bonds that are governmental bonds issued for the benefit of state and local governments and to qualified 501(c)(3) bonds issued for the benefit of section 501(c)(3) organizations. This guidance also applies to certain qualified tax credit bonds, such as Build America Bonds, that are subject to the same private business use rules. Although the guidance nominally refers to "management contracts," it applies to most types of service contracts. The new guidance is a significant development for those types of bond issues.

Highlights

- The new guidance establishes new safe harbors that are in some ways much more liberal and flexible than the Rev. Proc. 97-13 safe harbors, but in other respects stricter.
- The new safe harbors reflect a reconceived framework and will replace the Rev. Proc. 97-13 safe harbors. Issuers and borrowers generally may continue to rely on the Rev. Proc. 97-13 safe harbors for management contracts entered into before February 18, 2017, and certain extensions of those contracts pursuant to their term.
- The new safe harbors permit almost any type of variable or fixed compensation and abandon the Rev. Proc. 97-13 framework focusing on fixed fees.
- The new safe harbors rely much more heavily on the rule that "net profits arrangements" are not permitted under the safe harbors.
- The new guidance permits management contracts having a term up to 30 years, but retain a rule limiting the term to no more than 80 percent of the weighted economic life of the managed property.
- The new guidance establishes new safe harbor requirements relating to control of the managed

property, bearing of net losses, risk of loss and consistency of tax positions.

- In general, the new safe harbors are more "principles-based," and provide fewer bright lines than the Rev. Proc. 97-13 safe harbors. Accordingly, more interpretive questions may arise than under the Rev. Proc. 97-13 safe harbors, particularly with respect to the new requirements. Also, the question of whether a management contract that does not exactly meet all of safe harbor requirements should still be treated as not resulting in private business use may arise more commonly than under the Rev. Proc. 97-13 standards.
- Many management contracts that have been customarily treated as within the Rev. Proc. 97-13 safe harbors may not exactly meet the new safe harbors.
- In general, the new safe harbors may be particularly helpful for certain long-term management contracts for infrastructure. Certain shorter term management contracts in particular, however, will be subject to new standards that may involve compliance burdens.
- Many issuers and borrowers may need to consider implementing new practices to review management contracts relating to tax-exempt bond financed property that are entered into, materially modified, or in certain cases renewed after February 17, 2017.

Description of the New Safe Harbors

"Safe Harbor" Guidance. The new guidance provides for revised "safe harbors" in the form of a new revenue procedure. It does not change the substantive rules in the IRS regulations for when a management contract gives rise to private business use. Accordingly, the new guidance would not properly be used adversely against issuers and borrowers by the IRS in examinations, but rather sets forth standards that are intended to provide a basis for conservative tax positions of issuers and borrowers.

Immediate Permissive Application. The new guidance may be applied immediately to either new or existing management contracts.

Relationship to IRS Rev. Proc. 97-13, As Amended. The new guidance supersedes Rev. Proc. 97-13, including the portions of Notice 2014-67 that amend Rev. Proc. 97-13. Issuers and borrowers may continue to rely on Rev. Proc. 97-13, as amended, to a management contract that is entered into before February 18, 2017, unless it is materially modified or in certain cases extended on or after that date. An additional effective date rule also grandfathers extensions of a management contract entered into before February 18, 2017 if the extension is pursuant to a "renewal option" provided in the contract. A renewal option is defined as a provision under which either party has a legally enforceable right to renew the contract. Accordingly, during a long transitional period, an important consideration in reviewing certain management contract extensions likely will be whether the extension is pursuant to the terms of the contract.

Because Rev. Proc. 97-13 is superseded, "Rev. Proc. 97-13 compliance" will now be referred to as "Rev. Proc. 2016-44 compliance."

The new guidance is in response to public comment requests for more flexible safe harbors for management contracts having a term greater than five years. It states that it builds upon the amplifications in IRS Notice 2014-67 that provide for flexible safe harbors for contracts having a term up to five years.

Notably, however, the new guidance reframes and in many respects reconceives the safe harbors for management contracts. Although the new guidance responds to industry calls for more flexible safe harbors, one important question raised is whether certain management contracts that currently qualify for safe harbor treatment will no longer so qualify, as is discussed further below. In general, public comments to the IRS requested additional safe harbors, not new safe harbors that displaced the existing ones; the IRS and Treasury Department did not adopt that approach.

Safe Harbor Framework Restated. The new guidance states that it provides for a "more flexible and less formulaic approach toward variable compensation for longer-term management contracts" and "applies a more principles-based approach focusing on governmental control over projects, governmental bearing of risk of loss, economic lives of managed projects, and consistency of tax positions taken by the service provider."

The new guidance provides a general safe harbor and another safe harbor for "eligible expense reimbursement arrangements." The references in this description to the "new safe harbor" refer to the new general safe harbor when context requires.

Term Up to 30 Years Permitted. If a management contract meets the other requirements for the new safe harbor, the term of the contract may have a term that is no greater than the lesser of 30 years or 80% of the "weighted average reasonably expected economic life of the managed property." By comparison, the existing Rev. Proc. 97-13 establishes separate safe harbors for management contracts with terms not exceeding five years, 10 years, 15 years, and, in some cases, 20 years. The new safe harbor applies the 80 percent limit to contracts with any term, although Rev. Proc. 97-13 does not apply the 80 percent limit to contracts having a term not exceeding five years.

The Rev. Proc. 97-13 safe harbors also generally limit the term of longer-term contract to not more than 80 percent of the useful life of the "financed property." The reference to the "managed property" rather than the "financed property" possibly signals a helpful clarification, because the new safe harbor possibly can be read as focusing on the economic life of the property that is managed, and not the assets that are financed by a particular bond issue. New provisions that describe in more detail how the 80 percent limit applies may raise additional questions.

Variable and Fixed Compensation Permitted. If a management contract meets the other requirements of the new safe harbor, almost any type of variable or fixed compensation is permitted. The Rev. Proc. 97-13 safe harbors are based on the extent to which compensation is fixed. That fixed fee framework will no longer apply under Rev. Proc. 2016-44.

No "Net Profits Arrangements." The new guidance relies more heavily on the rule in the IRS regulations that states that a management contract with respect to financed property generally results in private business use of that property if the contract provides for compensation based, in whole or in part, on a share of net profits from the operation of the facility. The new guidance provides an additional gloss on this continuing standard, which may or may not be helpful to issuers and borrowers.

The new guidance states that compensation to the service provider will not be treated as providing a share of net profits if "no element of the compensation takes into account, or is contingent upon, either the managed property's net profits or both the managed property's revenues or expenses for any fiscal period." For this purpose, the elements of compensation are "the eligibility for, the amount of, and the timing of the payment of the compensation."

In general, this appears to be a somewhat strict interpretation of the no "net profits" standard. Because a contract will not qualify for the safe harbor if the "eligibility for" or "timing of" a payment is based on a net profits standard, it appears that any trigger for a payment based on net profits will not qualify. By comparison, in a recently released private letter ruling (PLR 20162203), the IRS concluded that a hotel management contract did not give rise to private business use, even though the contract provided for additional compensation triggered by a benchmark that was "a variant of net profits." In that case, the IRS permitted favorable treatment of the contract, in part because the amount of the payment was not based on net profits. Such a private letter ruling only applies to the specific issuer that requested it, and it is unclear whether its favorable conclusion would still apply under the reframed standards of Rev. Proc. 2016-44.

The new guidance also states that "incentive compensation will not be treated as providing a share of net profits if the eligibility for incentive compensation is determined by the service provider's performance in meeting one or more standards that measure quality of services, performance or productivity," but only if the amount and timing of the payment meets the requirements set forth above.

In general, this reframed "net profits" standard will be one of the most important considerations in reviewing management contracts for private business use compliance. One important point, however, is it appears that the somewhat strict interpretation of the no "net profits" rule in the new guidance applies only for the purposes of the safe harbor, and is not necessarily an interpretation of the substantive rule in the IRS regulations for when a management contract is noncompliant.

No Bearing of Net Losses of the Managed Property. The new guidance provides that a management contract will not meet the safe harbor if it, in substance, imposes on the service provider "the burden of bearing any share of net losses from the operation of the managed property." For this purpose, an arrangement will not be treated as requiring the service provider to bear a share of net losses if: (1) the determination of the amount of the service provider's compensation and the amount of any expenses paid by the service provider (and not reimbursed), separately and collectively, do not take into account either the managed property's net losses or both the managed property's revenues and expenses for any fiscal period; and (2) the timing of the payment of compensation is not contingent upon the managed property's net losses.

The new guidance helpfully provides that, as an example, a service provider whose compensation is reduced by a stated dollar amount (or one of multiple stated dollar amounts) for failure to keep the managed property's expenses below a specified target (or one of multiple specified targets) will not be treated as bearing a share of net losses as a result of this reduction.

This new requirement is not set forth in Rev. Proc. 97-13. In general, it is framed in a manner similar to the provision concerning net profits arrangements.

Control Over Use of the Managed Property. Perhaps the core provision of the new guidance is a requirement that the qualified user "must exercise a significant degree of control over use of the managed property." This new requirement is not set forth in the current Rev. Proc. 97-13, although certain provisions relating to control were set forth in prior versions.

The "qualified user" is the term used in the safe harbors for the state or local government or 501(c)(3) organization that uses the bond-financed property. The qualified user is usually the issuer or the borrower, and may include other users, such as affiliates.

The new guidance states that this control requirement is met if "the contract requires the qualified user to approve the annual budget of the managed property, capital expenditures with respect to the managed property, each disposition of property that is part of the managed property, rates charged for the use of the managed property, and general nature and type of use of the managed property (for example, the type of services)." It is unclear whether the "significant degree of control" requirement can be established in other ways. For example, it is unclear whether a contract including most of this list of control rights, but not all, can still meet the safe harbor.

The new guidance provides some clarification of what is meant by certain of the listed control rights. As an example, a qualified user may show approval of capital expenditures for a managed property by approving an annual budget for capital expenditures described by functional purpose and specific amounts, and may show approval of dispositions of property in a similar manner. Further, a qualified user may show approval of rates charged for use by either expressly approving such rates (or the methodology for setting such rates) or by including in the contract a requirement that the service provider "charge rates that are reasonable and customary as specifically determined by an independent third party."

These new control rights requirements, and in particular the requirement that the qualified user control rates, may raise many questions and require a change in practices for management contracts entered into, materially modified, or in certain cases extended after February 17, 2017. For example, in the case of physician contracts for hospitals financed with tax-exempt bonds, many existing "separate billing" arrangements that have been treated as within the Rev. Proc. 97-13 safe harbors may not be within the new safe harbors, unless the contracts are reframed to reflect these new requirements.

Risk of Loss of the Managed Property. In order to meet the new safe harbor, the qualified user must bear the risk of loss of the managed property (for example, upon force majeure). A qualified user does not fail to meet this risk of loss requirement as a result of insuring against risk of loss through a third party or imposing on the service provider a penalty for failure to operate the managed property in accordance with standards set forth in the management contract. This is another new requirement.

No Inconsistent Tax Position. Another new requirement is that the service provider must agree "that it is not entitled to and will not take any tax position that is inconsistent with being a service provider to the qualified user with respect to the managed property." As an example, the service provider must agree not to take any depreciation or amortization, investment tax credit, or deduction for any payment as rent with respect to the managed property. It appears that this express agreement will need to be included in contracts under the new safe harbor.

This new requirement is another provision that will likely require a change from current prevailing practices for management contracts entered into, materially modified, or in certain cases extended after February 17, 2017. Many existing contracts that are treated as within the Rev. Proc. 97-13 safe harbors do not contain such an express agreement. Specific agreements regarding tax treatment of the type required by the new safe harbor as a matter of prevailing practice may have been included in long-term management contracts, but have been less common in shorter-term contracts because the tax treatment has been regarded as implicit.

No Circumstances Substantially Limiting Exercise of Rights. The new guidance continues the general requirement in Rev. Proc. 97-13 that the service provider must not have any role or relationship with the qualified user that, in effect, substantially limits the qualified user's ability to exercise its rights under the contract.

Like Rev. Proc. 97-13, the new guidance contains a "safe harbor within a safe harbor" for establishing that the service provider has no such role or relationship. This safe harbor continues the general approach of Rev. Proc. 97-13, but is in some respects stricter. The new guidance requires as a safe harbor that (1) no more than 20 percent of the governing body of the qualified user is vested in persons having a role with the service provider; and (2) that the governing body of the qualified user not include the chief executive officer of the service provider (or a person with equivalent management responsibilities) or the chairperson (or equivalent executive) of the service provider's governing body. For the purpose of this safe harbor, "service provider" now expressly includes related parties to the service provider.

Because the specific requirements concerning overlapping board members continue to be framed as a "safe harbor within a safe harbor," it appears that issuers and borrowers could reasonably meet the substantive requirement based on other factors.

Functionally Related and Subordinate Use. The new guidance contains a new helpful provision relating to "functionally related and subordinate use." Under this new rule, a service provider's use of a project that is functionally related and subordinate to performance of its services under a management contract does not result in private business use, if the contract meets all of the requirements of the new guidance. An example is use of storage areas to store equipment used to perform activities under a management contract.

Eligible Expense Reimbursement Arrangements. A separate safe harbor is established for "eligible expense reimbursement arrangements." An "eligible expense reimbursement arrangement" is defined as a management contract under which the only compensation consists of reimbursements of actual and direct expenses paid by the service provider to unrelated parties and reasonable related administrative overhead expenses of the service provider. An eligible expense reimbursement arrangement does not result in private business use, regardless of whether the other requirements of the new guidance are met.

This separate safe harbor is an expansion of an exception set forth in the IRS regulations from private business use that previously applied only to management contracts for public utility property.

Contracts Properly Characterized as Leases. The new guidance recites a rule in the IRS regulations that provides that a lease generally results in private business use and that any arrangement that is properly characterized as a lease for federal income tax purposes is treated as a lease (even if the arrangement is in form a management contract). The new guidance further recites a provision in the IRS regulations to the effect that, in determining whether a management contract is properly characterized as a lease, it is necessary to consider all the facts and circumstances, including (1) the degree of control over the property that is exercised by the service provider; and (2) whether the service provider bears the risk of loss of the financed property.

The new guidance does not otherwise expressly address the question of when a management contract is properly characterized as a lease. As a practical matter, however, it would appear that any management contract meeting the new safe harbor should not ordinarily be subject to characterization as a lease, because many of the new requirements (including requirements relating to control and risk of loss) are also factors relevant to determining whether an arrangement is in substance a lease.

Anti-Abuse Rules. The new guidance does not override any of the provisions of the IRS regulations. Accordingly, it is important to continue to interpret the new guidance in the context of the rules of the IRS regulations. In particular, the anti-abuse rules in the IRS regulations provide that, in certain circumstances, an arrangement that directly or indirectly passes through to private persons the financial benefit of tax-exempt interest rates may result in private business use, even if the arrangement would not otherwise result in private business use under the regulations. This anti-abuse rule will continue to be an important consideration in the consideration of certain management contracts.

Expected Future Developments. The new guidance does not request any further public comments. We expect that public comments may be submitted, however, particularly in light of the reconceived nature of the new safe harbor and its many new requirements. One likely request will be to permit issuers and borrowers to continue to rely on the Rev. Proc. 97-13 safe harbors, at least for a period longer than six months. There is no current indication, however, that the IRS and the Treasury Department would respond to any such public comments. We expect, however, that officials of the IRS and the Treasury Department will make clarifying public statements before February 18, 2017.

Last Updated: September 2 2016

Article by Michael G. Bailey, David Y. Bannard, Dana M. Lach, Chauncey W. Lever and Mark T. Schieble

Foley & Lardner

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.

GFOA, NABL Publish Guidance on PostIssuance Tax Compliance.

WASHINGTON – The National Association of Bond Lawyers and the Government Finance Officers Association on Thursday each issued guidance to issuers and counsel on how to comply with tax-exempt bond rules after the issuance of tax-advantaged bonds.

The guidance came after three years of research, according to Matthias Edrich, an attorney with Kutak Rock in Denver and chair of NABL's tax law committee.

Edrich, who authored NABL's 14-page publication, said the groups issued the guidance because of the Internal Revenue Service's focus on the need for issuers to have good policies and procedures in recent years.

"The IRS is telling them today we hope you have effective policies in place, but what means effective is up to you," Edrich said. "We recommend policies that contain certain elements, but they are not penalized if they don't have these elements."

NABL cited several suggestions that the IRS had for issuers in March, including that they: identify those responsible for coordinating post-issuance tax compliance; provide for due diligence reviews at regular intervals; address the timely identification of noncompliance; and promote the retention of adequate records.

"Procedures assist the entity in complying with tax and document covenants, in the transfer of knowledge and to streamline the entity's financing operations, all for the purpose of maintaining the tax benefits associated with the bonds," NABL officials wrote.

The IRS oversees and enforces the post-issuance compliance of tax-advantaged bonds, and NABL said the agency has increased its efforts to encourage issuers and conduit borrowers to adopt effective procedures.

Though it provides oversight, the agency does not dictate to an issuer what elements need to be in a policy, Edrich said. The guidance was written as tips for what an issuer could consider without proposing best practices, he said.

"It's written fairly broad and supposed to be a guide for issuer boards to be able to think about what are best practices," Edrich said. "It's a paper that I hope will be useful for years to come."

Procedures suggest courses of action an entity can take to maximize the likelihood that rules applicable to tax-advantaged bonds are followed after the bonds are issued and remain outstanding.

A bond is considered tax-advantaged if it is tax-exempt and interest on the bond is excluded from gross income to the bondholder, if it is a taxable tax credit bond and the holder receives federal tax credits, or if it is a direct-pay, taxable bond and the issuer receives federal subsidies from the Treasury Department.

The four principal categories that tax compliance rules address, according to NABL, are the expenditure of bond proceeds, the use of bond-financed assets, the investment of bond proceeds, and the gathering and maintenance of records relating to the bonds.

The two groups added that issuers should consult with bond counsel and other professionals on post-issuance tax compliance as tax laws, rules and practices continue to change.

Emily Brock, director of GFOA's federal liaison center, said the guidance stems from enforcement actions and settlements, including those reached under the IRS Office of TaxExempt Bonds' Voluntary Closing Agreement Program (VCAP) as well as other IRS settlements. The IRS has said if such procedures are in place, then it will consider them when issuing orders, she added.

"It's so important that issuers know and understand all of these compliance procedures so that they can prevent and correct any tax violations while tax-exempt bonds are outstanding," Brock said. "We just really wanted to make sure the issuer and counsel are informed of the procedures."

GFOA and NABL issued separate publications, though they were produced as complementary guidance to their respective members.

The guidance was published separately because GFOA wanted to glean those things most important to issuers, while issuers can share the "significantly comprehensive" NABL publication with counsel, Brock said.

"The project taken together is a way for NABL and GFOA to reach an even broader community," she said.

As of Thursday afternoon, Edrich said he had not received any feedback from NABL members or IRS officials.

NABL officials also said that Congress may develop new types of tax-advantaged bonds in the future that will be subject to additional special tax rules. This could need to be addressed in revisions to the entity's post-issuance tax compliance procedures, they said.

The Bond Buyer

By Evan Fallor

September 8, 2016

Study Shows Broncos' Mile High Stadium Cost Federal Taxpayers $54 Million.

Sports Authority Field at Mile High, the home of the Super Bowl 50 champions, has shortchanged federal tax collectors by $54 million, a Brookings Institution analysis says.

In the first-of-its-kind study, Brookings looked at 36 professional football, baseball, basketball and hockey stadiums built or renovated since 2000 using $13 billion in tax-exempt municipal bonds and concluded the work resulted in a $3.2 billion federal subsidy, and $3.7 billion loss in federal tax revenue.

It's one thing when local taxpayers pay for stadiums in their hometowns. Front Range residents in 2002 assumed about $300 million of the $400 million cost to build the Broncos' new stadium in the parking lot of the old Mile High Stadium. The tax-free municipal bonds that funded the new stadium were paid off in 2012.

If those bonds had not been not tax-exempt, the federal government would have collected $49 million in taxes. Then taxpayers who held those bonds got a federal income tax break that saved them estimated $5 million, adding up to a $54 million total loss to the federal taxpayers since 2002, according to the Brookings study.

"I love sports. If I want to pay for sports in my town, I have a weak-but-plausible argument that my local community should subsidize a stadium," said Brookings senior fellow Ted Gayer, who co-wrote the study. "But the weakest and most implausible argument is that someone in Montana should be subsidizing whether or not a football team relocates from St. Louis to Los Angeles. A federal subsidy should have federal benefits. There is no benefit to me whether the Broncos play in Denver or Austin."

The Broncos are hardly the largest beneficiaries of tax-exempt municipal bonds. That crown belongs to the New York Yankees, which spent $2.5 billion on Yankee Stadium in 2009, $1.7 billion of which was financed by tax-exempt municipal bonds issued by New York City. The interest earned on those bonds is tax-exempt, resulting in a federal subsidy of $431 million. Bondholders who used the bonds to lower their tax liability received $61 million in tax breaks, creating a total revenue loss of $492 million.

The researchers at Brookings concluded that beyond some hard-to-measure local benefits, federal taxpayers saw no economic benefit for their tax dollars spent on stadiums in Indianapolis, Chicago, Cincinnati, Houston, Miami, Milwaukee, Washington, D.C. and Seattle.

It didn't used to be that way. Stadiums once were private affairs. But in 1953, the era of public financing for stadiums began when Milwaukee lured the Boston Braves with a new stadium built with tax dollars. In the mid-1980s, Congress passed the Tax Reform Act, which meant to curtail federal subsidies by tying them to municipal financing deals.

That legislation required that municipalities finance a large chunk of the stadium and said governments can't pay for that financing with taxes harvested from the stadium. Instead, cities typically rely on taxes on hotels, rental cars and "tourist taxes" to support new stadiums and still qualify for federal subsidies in the form of tax-free bonds. Taxing visitors is a good way to convince local taxpayers they won't be alone in shouldering the burden of paying off the new stadium.

"That doesn't make sense," Gayer said. "If you want to collect revenue, you should collect from the people who are gaining the most from the new stadium: the people who are actually using the stadium, not my aunt across town who doesn't care about football."

Gayer and his fellow researchers conclude that Congress should end tax-exempt financing for private businesses like professional sports stadiums. Or, at least, the researchers said, limit tax subsidies by offering “qualified private activity bonds” that are subject to statewide caps. A state cap would mean that New York would not get $860 million federal subsidies for homes for its Yankees, Mets, Nets and Islanders and Texas could not get $446 million in federal subsidies for its Astros, Texans, Cowboys, Rockets, Spurs and Stars.

The researchers say the evidence of economic benefits of new stadiums spilling into local communities is “weak.”

“Academic studies consistently find no discernible positive relationship between sports facility construction and local economic development, income growth or job creation,” reads the study.

Jon Caldara, the Independence Institute chief who has long railed against stadium financing schemes he calls “corporate welfare,” said booing a new stadium in Bronco Country does not bolster his popularity. But he does it anyway.

“As much as sports fans might be grateful, I don’t think they realize they are on the hook for other people’s entertainment. Even if everything the economic development guys say is true — that for every dollar spent it spurs $20 or something in spending in the community, which, by that logic, we should be building five stadiums — it’s still wrong because you have the government picking winners and losers,” Caldara said. “The money they are playing with is our money, and they are taking chances with our money. We need to recognize we are subsidizing private-sector entertainment.

“At what point do the teams belong to the city?” Caldara asked. “If we are going into debt, and our kids are taking on all this long-term risk, at what point does the mayor get to choose the starting lineup?”

THE DENVER POST

By JASON BLEVINS | jblevins@denverpost.com

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Study Shows Stadiums and Arenas Received $3.2B in Federal Tax Breaks.

A new study from the Brookings Institution, which looked at 45 stadiums and arenas in the four major sports leagues that have been built or renovated in that time, reveals the those stadiums and arenas received $3.2 billion in federal tax breaks.

Those stadiums were financed in part with municipal bonds, which are issued by local governments. Interest on those bonds is exempt from federal taxes. Brookings calculates that the federal government lost $3.2 billion in tax revenue – and $3.7 billion if you count the windfall that high-income bondholders get.

Yankee Stadium, which opened in 2009 and cost $2.5 billion to build, topped the list of those entities getting the tax breaks. It received a federal subsidy of $431 million, and the federal government lost a total of $492 million in possible revenue.

The NFL has built or renovated 13 stadiums using tax-exempt bonds since 2000. Major League

Baseball has used bonds for 12 stadiums. The NBA has built seven arenas with them, and the NHL has built four.

Brookings says that stadiums and arenas provide few economic benefits – undercutting a main argument that teams use to persuade cities to finance stadiums.

Because the tax breaks are federal, taxpayers in other states helped fund construction of the stadiums and arenas in other parts of the country. That means that people who live near teams are paying for stadium construction whether they're fans or not.

In order to qualify for federal tax exemption, cities and states can pay back only 10% of the bonds with money that comes from the stadium, such as ticket sales or the rent that the team pays to use the stadium.

Stadiums were largely built without federal funding until 1953. When baseball's Boston Braves moved to Milwaukee, they received a new publicly funded stadium. Using federal money for construction became a trend, despite attempts by Congress to stop it.

More on the effort to build a 65,000-seat Las Vegas-area stadium to house the proposed LV Raiders in Tuesday's print edition and on line at GamingToday.com.

September 10, 2016 9:48 AM

by Robert Mann

TAX - NEW YORK

Joon Management One Corp. v. Town of Ramapo

Supreme Court, Appellate Division, Second Department, New York - August 17, 2016 - N.Y.S.3d - 2016 WL 4371715 - 2016 N.Y. Slip Op. 05795

Property owner brought action against town seeking a judgment declaring that property's tax assessment was overstated and erroneous.

The Supreme Court, Rockland County, granted town's motion for summary judgment and denied property's owner's motion for leave to amend or to enforce settlement agreement. Property owner appealed.

The Supreme Court, Appellate Division, held that:

- Statute of limitations for tax certiorari proceedings applied to action;
- Town's motion for summary judgment was not premature;
- Supreme Court properly denied property owner's motion for leave to amend; and
- Supreme Court properly denied property owner's cross-motion to enforce alleged settlement agreement.

Statute of limitations for tax certiorari proceedings, which required such proceedings to be commenced after exhaustion of administrative grievance remedies and within 30 days after filing of the final assessment roll, applied to property owner's against town seeking judgment declaring that its property's tax assessment was overstated and erroneous, where gravamen of property owner's claim was that its property was overtaxed.

Town's motion for summary judgment on property owner's claim that its property tax assessment was overstated and erroneous was not premature, despite property owner's assertion to the contrary, where property owner failed to demonstrate how discovery might have lead to relevant evidence or that the facts essential to justify opposition to the motion were exclusively within the knowledge and control of the town.

Supreme Court properly denied property owner's motion for leave to amend its complaint against town challenging tax assessment, where property owner's proposed amendments, which were to add causes of action to recover money had and received and to recover damages pursuant to § 1983 for violation of constitutional rights, were devoid of merit.

Supreme Court properly denied property owner's cross-motion to enforce alleged settlement agreement between owner and town with regard to owner's action against town challenging its property tax assessment, where stipulation of settlement was never approved by town board, thus never becoming binding upon town.

TAX - NEW YORK

Nearpass v. Seneca County Indus. Development Agency

Supreme Court, Seneca County, New York - August 18, 2016 - N.Y.S.3d - 2016 WL 4419135 - 2016 N.Y. Slip Op. 26264

Property owners commenced Article 78 proceeding claiming that resolution by county industrial development agency (IDA) to provide tax benefits to developer of casino being built in county was void under New York State Industrial Development Act (IDA Act), impermissibly provided public assistance for private purpose, unlawfully failed to specify amount of tax benefit, materially miscalculated and misstated amount of tax benefit, and was null due to attorney conflicts of interest, and that IDA usurped town assessor's authority to value property improvements.

The Supreme Court, Seneca County, held that:

- Casino was a commercial project and recreation facility within the meaning of the IDA;
- IDA's decision to grant tax benefits to casino was not arbitrary and capricious;
- IDA was not required to specify amount of tax abatement;
- IDA's failure to adopt critique of appraisal report on casino's value was not arbitrary and capricious; and
- Powers of town assessor were not preempted by tax agreement.

IRS Releases Updated Safe Harbors For Management Contracts In Tax-Exempt Bond-Financed Projects: Thompson Coburn

On August 22, 2016, the Internal Revenue Service released Revenue Procedure 2016-44. The purpose of this revenue procedure is to provide revised and broader "safe harbors" under which certain private management contracts will not result in private business use of projects that were financed with the proceeds of tax-exempt governmental or qualified 501(c)(3) bonds.

Potentially impacted issuers and conduit borrowers include governmental and nonprofit healthcare, higher educational and other entities. Market participants have expressed the belief that the more flexible safe harbor provisions may also help facilitate the structuring of public-private partnership (P3) transactions.

The revised safe harbors set forth in the revenue procedure build upon the existing safe harbors originally set forth in Revenue Procedure 97-13, which were in turn modified by Revenue Procedure 2001-39, and amplified by Notice 2014-67. The existing guidance sets forth conditions under which a management contract does not result in private business use, which conditions include constraints on net profits arrangements, the permitted term of the management contract, the types of compensation provided under the arrangement, and the relationship between the parties. Under such existing guidance, the extent to which the compensation to the private party is a fixed amount is key, in that the greater the percentage of fixed compensation, the longer the term of the management contract is permitted to be. Notice 2014-67 provided additional flexibility within the safe harbors by allowing a broader range of variable compensation arrangements for shorter-term (i.e., up to five year) management contracts.

Continue reading.

Last Updated: August 31 2016

Article by Steve Mitchell and Henry Bettendorf

Thompson Coburn LLP

Baltimore Project Would Include Largest TIF District in City History.

WASHINGTON – The proposed $6.9 billion Port Covington development project in Baltimore would include the largest tax increment financing district in the city's history and would be financed in part with $660 million of bonds backed by the increased property tax revenues.

The project, proposed by Under Armour CEO Kevin Plank, would include a new global headquarters for the sports apparel company as well as residential and retail facilities within a development district.

A new 50-acre, 3.9 million-square-foot headquarters for Under Armour would serve as the project's anchor, and would be flanked by roughly 11 million square feet of mixed-use development.

The project would be owned by Sagamore Development Company, a Baltimore-based real estate firm founded in 2013 by Plank and developer Marc Weller. Development would take place on Port Covington, a 260-acre industrial area roughly two miles south of downtown Baltimore between I-95 and the Middle Branch of the Patapsco River.

The project would be partly financed by $535 million of increased property tax revenue to be collected within a tax increment financing district. Those funds would go toward the construction of infrastructure, including roads and public spaces. None of the TIF revenues would go toward the Under Armour headquarters.

The total bond cost would be $660 million including issuance costs and other costs not associated with construction, according to Baltimore Deputy Finance Director Stephen Kraus.

Kraus said the bonds would be issued by the city of Baltimore Department of Finance in four-to-five phases over the next 12 years. Construction is expected to be developed in phases over roughly 25 years, according to plans.

The $535 million of expected increased property tax revenue, combined with an additional $349.5 million from the state and $224.2 from the federal government would total almost $1.2 billion in city, state and federal subsidies. Private funding provided by Sagamore is roughly $327.8 million. Of the private and governmental funding of roughly $1.4 billion, $115 million would go toward land acquisition costs, $138 million would go toward site work and $1.2 billion would be used for infrastructure.

The bonds would be paid back by incremental tax revenue generated by the development, as is customary in TIF districts. Tax increment financing secures tax-exempt borrowing by anticipated increases in tax revenues within a defined development district.

The Baltimore Development Corporation, the private nonprofit that grants TIFs for the city, approved the TIF application in March, and it is now before the City Council's Taxation, Finance and Economic Development Committee. The committee has held three hearings regarding the project, but moved a work session originally scheduled for Monday to Sept. 8.

At the time of the application, Baltimore had 14 TIF districts with outstanding debt of $147.2 million.

"One risk is that the developer may not move forward with the development once the tax increment financing district and documents authorizing the issuance of bonds have been approved by the city," officials wrote in the TIF application. "Provided that is the case, the tax increment financing district would remain in place but the bonds would not be issued and debt would not be incurred."

According to plans, the first tranche of TIF bonds would be issued in June 2017 for $62 million, followed by a second tranche of $208.3 million in 2018. A third tranche of $169.7 million would be issued in 2023, and a fourth tranche of $218.7 million would be issued in 2028.

The developer would initially purchase the bonds, which are projected to be outstanding between 2046 and 2058.

Proponents claim the project will bring roughly 8,000 jobs to Baltimore and will revitalize a largely vacant three-mile section of waterfront.

"An area essentially cut off from Baltimore's downtown neighborhoods by the elevated structure of I-95 and the adjacent CSX rail yard will become a dynamic, innovative, mixed-use experience and destination," officials wrote in the application. "As one of the largest urban revitalization projects in the United States, the redevelopment of Port Covington will provide extraordinary economic growth and job opportunities for both the city and the greater region."

Mark Pollak, a partner with Ballard Spahr in Baltimore who is serving as counsel for the developers, said project officials hope to have the initial financing occur in early 2017. Pollak, who described the project as "one of the greatest opportunities the city has ever had," said TIF funding would be phased in over an initial period. He did not comment on what the length of that period may be, and said it was dependent on the growth of Under Armour among other factors.

As among the largest TIF deals in U.S. history, the process could take a while, he said.

"I think everybody recognizes it as a potential transformative project for the city because of the scope," Pollak said, adding that Baltimore Mayor Stephanie Rawlings-Blake has expressed support for the proposed plan. "Clearly Under Armour has the opportunity to grow in many places and we and the city would hope that they can keep the growth in this city."

Still, he said there has been discussion in regards to the TIF size and negotiations to provide benefits to other parts of the city.

Some of those concerns have been expressed by Baltimoreans United in Leadership Development (BUILD), which in July called for a TIF agreement to include local hiring mandates of 51% for all future businesses in the TIF district. Should that mandate not be met, BUILD officials said the city should invoke "substantial financial penalties" on the parties responsible.

"BUILD calls on the City Council, Sagamore Development, and Mr. Plank to not agree to any city-wide benefits agreement without the city conducting a comprehensive independent analysis of the deal," said BUILD co-chair Rev. Andrew Foster Connors. "If after the analysis the city concludes that the costs associated with the development can be managed, then any agreement must treat the city of Baltimore as a 'first in' investor."

Pollak said the cost of the project is $5.5 billion, but rises to $6.9 billion when accounting for infrastructure costs. Estimates have placed Port Covington's assessed value after construction at $2.6 billion.

In addition to the new Under Armour headquarters, the completed Port Covington project as proposed would include: 1.5 million square feet of retail and entertainment space, more than 7,500 rental and for-sale residential units, 500,000 square feet of industrial/light manufacturing space, 200 hotel rooms, 1.5 million square feet of office space, and 41 acres of public parks and waterfront space, according to the TIF application.

BDC president and CEO William Cole said the group's TIF recommendation was contingent on five factors, which are that: returns to the city exceed the city's hurdle rate, a profit-sharing agreement is negotiated, there is federal and state participation in infrastructure, there is no adverse effect on school funding, and there is no adverse effect on the city's bonding capacity.

If and when the proposal clears the City Council's Taxation, Finance and Economic Development Committee, it will then go before the full City Council for consideration.

Under Armour's headquarters is expected to be built over 15-plus years, according to plans. The Baltimore-based company currently has headquarters in the Tide Point neighborhood of Baltimore, where it has been for 18 years.

In January, Under Armour completed a $40 million office space that houses more than 600 employees, marking the first new building to be opened on the Port Covington campus. Plank's Sagamore Development Company has also completed a reuse of a city garage in Port Covington and the construction of the Sagamore Spirit Distillery in the same neighborhood.

The Bond Buyer

By Evan Fallor

August 30, 2016

Big-Box Stores Battle Local Governments Over Property Taxes.

The retailers are deploying a 'dark store' strategy that's hurting cities and counties around the country.

On Michigan's sparsely populated Upper Peninsula, big-box stores are a modern necessity. Where towns are spaced far apart and winters are long, one-stop shopping to load up on supplies adds a crucial convenience to what can be — at least for many — a rugged existence.

Landing one large retailer is a coup. Having more than one can make a city or town a regional shopping destination. Marquette Township, a small community adjacent to the larger city of Marquette, is in the unique position of having a handful of big-box chain stores. Taking advantage of the fact that the city of Marquette was mostly built out, the township began encouraging large-scale commercial development on its western edge early in the 2000s.

The town now boasts the only Lowe's on the Upper Peninsula, and the only PetSmart, Target and Best Buy. A Menards home improvement store and a Walmart Superstore are there as well. The flurry of new building and retail was so great that the township's tax revenue never took a hit during the Great Recession, even at a time when most small towns on the peninsula and elsewhere in Michigan were struggling.

But recently, the township suffered a dramatic drop in its property tax revenue. It had to cut back on spending, trim employee benefits and reduce library hours. The impact has reached up to surrounding Marquette County, which earlier this year closed a youth home to save money. The reason for the lost revenue isn't declining consumer demand. It's a series of rulings by the Michigan Tax Tribunal that have allowed large retailers to reduce their property tax assessments, in many cases by as much as half.

Big-box retailers argue that the market value of their commercial property should be the sale price of similarly sized but vacant retail buildings. They point out that these buildings are extremely hard to sell as-is once the retailer moves out. They tend to sit empty for long periods. Thus, the assertion is, they aren't worth nearly as much as local tax assessors have traditionally assumed in valuing the property.

This appeals approach was first largely successful in the Detroit area following the recession, when nearly all retailers were dealing with depressed property values. But since then, it has spread across otherwise thriving areas in Michigan to the point where it is difficult to find a county that hasn't been challenged on the issue. The assessment community has even given it a name, dubbing it the "dark-store" strategy.

Local governments, needless to say, aren't buying this. "When you get your house appraised, they're going to look at properties that are occupied," says Steve Currie of the Michigan Association of Counties. "They're not going to look at the foreclosed one because that's not an equitable property. It's the same case here."

Michigan is far from alone in seeing localities take dark-store hits to their property tax base. Counties in Alabama, Florida and Indiana are seeing widespread challenges that make use of the dark-store method. The National Association of Counties says it's an emerging issue in Iowa, North Carolina, Ohio, Tennessee, Washington and Wisconsin.

Still, while these cases have been proceeding for the better part of a decade, it's only been recently that county organizations and public officials have realized the geographical magnitude of the challenge. County assessors forced to respond to it aren't always aware of similar controversies outside their jurisdiction. This is particularly true in places that are geographically isolated and where assessors are part-time employees.

Getting policymakers clued in to the problem has also been tricky. The world of property tax assessments is loaded with definitions and methodology that, to the average outsider, can seem overwhelming. Property appraisal laws vary by state, and arguments that hold water in one state might not in the next. So it's not always clear to lawmakers what — if anything — they can do legislatively to help counties respond to the threat.

Even in places where counties have pieced together a coordinated effort to fend off challenges, response on the state level has varied. The Indiana General Assembly took arguably the strong-est action, passing two laws last year that essentially banned the dark-store tactic. But those laws were repealed and replaced with a weaker law this year. Alabama passed a law that amounted to an administrative change giving counties more legal resources. The Michigan Legislature has considered but not approved bills dealing with how the Tax Tribunal hears assessment challenges. In these places and elsewhere, many are concerned that the longer it takes for a concerted state response, the more money counties and local governments will lose.

Big-box retail stores aren't the first to complain that their property's uniqueness should afford them special consideration when it comes to their taxable value. Nearly a century ago, the owners of the New York Stock Exchange tried to get the building's appraisal value lowered by arguing that the building's unusual — and expensive — design would be of no value to any future buyer. In fact, the argument went, the building actually lowered the value of the land itself because a future buyer would be forced to shell out the money for demolition costs. While the court rejected that argument in 1928, it has become a popular case to make ever since, with varying levels of success.

There are different nuances and different case law in every state, but it can be generally said that appraisers look at three factors in determining the taxable value of property: the sale price of comparable properties, the current cost to build minus depreciation and the income generated by rents charged to tenants. Appraisers can apply a blend of these approaches to arrive at a property's value, or place most of the weight on just a single approach.

When it comes to unique properties like big boxes, finding comparable sales is difficult. Property values differ by market and it's simply not often that an oversized retailer in a market area sells its property. For this reason, appraisers prefer giving more weight to building costs.

But big-box retailers say using the construction costs of a building to determine the assessment artificially inflates the value. And they insist it's unfair to value their retail properties based on their worth to the current user (referred to as "value-in-use") instead of the value the property would have on the open market (called "value-in-exchange"). The appropriate use of the competing valuation methods is a topic of seething debate in the appraisal world. Retail representatives fall decidedly on value-in-exchange. "It's easy to be confused by the presence of a business," says Florida real estate broker Sheila Anderson, whose firm Commercial Property Services has represented owners in scores of appeals. "But a business is not [what needs to be] assessed." In her view, it's only the resale value of the empty building that matters for taxation. And that is nearly always a much smaller amount.

Complicating the matter are deed restrictions the big-box retailers place on the properties they do sell. Typically, a retailer closes a location to open up another store close by, or leaves because the market isn't viable anymore. But just to be sure a competitor doesn't move in and fare better, the deed bars the new owner from operating a similar business. Assessors say this limitation artificially depresses the market value of the property. The retailers consider it insignificant.

The debate leads to real questions about the fairest way to value these prolific but unique properties, says Allen Booth, a former city assessor in Rhode Island without any affiliation to a dark-store case. “The reality is there are very few tenants that will move into the custom building when you’re dealing with these big-box situations,” he says. But, he adds, officials are leery of retail attorneys’ motives because they can profit greatly from the challenges by taking a cut of the tax refund if they win. “You have to wonder,” Booth says, “are these people just being obnoxious or are the properties really overvalued and it’s just that now someone’s looking at it?”

Tax courts in Michigan have generally agreed with retailers that properties were being overvalued. In Marquette Township, Lowe’s successfully used this argument in a 2012 challenge to its property assessment and succeeded in reducing its taxable value from $5.2 million to less than $2 million, even though the store alone cost $10 million to build. The township spent several hundred thousand dollars in legal costs but failed to win in the appeals process. As a result, the ruling applied to other pending challenges. All told, the township’s total property tax collections have fallen nearly 22 percent in just a few years.

Statewide, the results have been similar. According to the International Association of Assessing Officers, the valuation on large retailers across the country is anywhere from $45 to $75 per square foot, depending on the market. After five years of litigation in Michigan, says tax attorney Jack Van Coevering, the average per-square-foot value in the state is $20.

The big-box retailer Meijer brought a case at one of its most successful Indiana locations, in Marion County, after winning reduced assessments in Michigan. The attorney for Meijer went so far as to tell the Indianapolis Business Journal that the appeal in Marion County was a test case because “whatever the value is there would be the upper limit of the value across the state.” The retailer won in late 2014 and got its assessment slashed from $83 per square foot to $30 per square foot. The decision applied retroactively, requiring Marion County to refund Meijer $2.4 million for nine years of back taxes. Indiana county officials estimated that if the decision were to be extended to the more than 17,000 commercial properties across the state, it would mean a loss of $120 million in property tax revenue statewide.

Indiana lawmakers responded quickly. In 2015, the legislature passed two bills: One effectively banned using the dark-store method to value existing businesses, and the other required using the cost method for properties over a certain square footage. But those laws were repealed this year under concerns they violated the uniformity clause in the state’s constitution, which requires all property to be assessed on an equal basis. The Indiana General Assembly then passed a new law that requires assessments to be based on the value of properties that are “similarly situated in the marketplace.”

Other states have tried other tactics. Alabama passed a law this year that allows counties to remove these cases from their district attorney’s jurisdiction and hire outside attorneys to fight them. In Michigan, a bill passed the House that would require the Tax Tribunal to consider all three valuation methods (rather than just the one the retailer is arguing for). It will be considered in the Senate later this fall.

In short, the legislative authority of lawmakers to intervene is murky. “It’s always appropriate for the legislature to try to clarify and remedy a situation when appropriate,” says Joan Youngman, a property tax expert with the Lincoln Institute of Land Policy. “But you want to be sure this is a problem with the existing law.”

In the end, the best way to beat back the challenges is to win in court. But that’s a tough task for counties that don’t have a lot of resources. In Tampa, Fla., Hillsborough County’s director of valuation, Tim Wilmath, says counties in his state have caught on early to the dark-store challenge and have for the most part been able to mount successful defenses. Wilmath co-authored an article in an industry magazine last year advising county assessors on how to challenge the tactic, which has made him a de facto adviser to smaller counties across the country. “They’re looking for advice on how best to go at it,” he says of the calls from outside Florida. “But even when they know all the right things to do, they still settle because they just don’t have the money.”

In Michigan, a recent Court of Appeals ruling may prove to be a turning point. In May, the court overturned a 2015 decision by the Michigan Tax Tribunal that had favored the retailer Menard against the city of Escanaba in a property tax dispute. The court found that Escanaba’s cost-based approach was more reasonable than the retailer’s comparable sales method, which included using dark stores. The case was remanded back to the tribunal with directions to consider all the assessment methods. It may end up setting a precedent for cases in Michigan that are currently open.

Still, for counties and townships that have already lost or settled cases, the damage has been done. And because of limits on how much localities can increase the property tax each year, the previous losses in tax revenue will never be made up. In Marquette Township, that means officials will have to figure out how to replenish the reserves that were drained to pay back Lowe’s, at the same time adjusting permanently to a shrunken tax base.

“The long and short of it,” says Marquette Township Manager Randy Girard, “is that we will not recover.”

GOVERNING.COM

BY LIZ FARMER | SEPTEMBER 2016

NABL: IRS Modifies Rev. Proc. 2016-44 Transition Date.

The IRS has modified the effective date of Rev. Proc. 2016-44 to extend the transition period by 6 months.

The revision allows an issuer to apply the safe harbors in Rev. Proc. 97-13, as modified and amplified, to a management contract entered into before August 18, 2017 and that is not materially modified or extended on or after August 18, 2017 (other than pursuant to a renewal option as defined in sec. 1.141-1(b)).

The August 18, 2017 date is 6 months later than previously announced.

The updated version will be printed in next week’s Internal Revenue Bulletin.

The revised version of Rev. Proc. 2016-44 is available here.

An Obscure, Outrageous Reason Your Property Taxes Are So High.

In many parts of the country, they supply our water, fight our fires and help us get to work, but “special districts” are a form of government that receives very little attention. The lack of media scrutiny and public interest in special districts provides opportunities for insiders to feast on the billions of tax dollars these entities collect each year. One such group of insiders are the intermediaries who help districts issue their bonds.

The Census Bureau counted over 38,000 special districts in its 2012 enumeration of local governments (the next count will be in 2017). The Census also found that these districts had aggregate revenue of $206 billion and debt of $370 billion, representing about 10 percent of the municipal bond market.

In an amusing and informative piece in March, HBO's John Oliver showed viewers the ups and downs of these special districts. One inspiring scene in Oliver's report shows two officials of a New Hampshire mosquito control district conducting a fully by-the-book public meeting with precisely zero members of the public attending.

Less inspiring was the case of a Texas special district formed when a company wheeled a mobile home onto a vacant plot of land and then rented it to a married couple for $150 per month short term. Those two individuals held the entire voting power of the special district – a power they used to authorize $500 million in new bonds to be issued by the district. Those bonds will finance water, sewer and other infrastructure for a new subdivision to be built on the vacant land.

But an electorate of two short-timers lacks the ability and incentive to ensure that the new bonds are issued in a cost-efficient manner. And it appears that underwriters, lawyers, financial advisors and other service providers are raking in outsized shares of these new bond proceeds.

On Aug. 20, James Drew of the *Houston Chronicle* reported on two special districts in Fort Bend County that paid issuance costs of between 9 percent and 11 percent of the face value of the bonds issued (Drew also reported that one of the special districts, MUD 187, was formed when a Houston developer arranged for two people to move their trailer onto what was then an empty field).

The issuance costs paid by these two special districts is well above the national average of 1.02 percent that I calculated in a 2015 study published by the Haas Institute for a Fair and Inclusive Society at UC Berkeley. Issuance costs are to local governments like points are to a consumer taking out a home mortgage. In both cases, the goal should normally be to minimize them.

Subsequently I looked at several bonds issued by special districts in the Dallas suburbs for the Texas Public Policy Institute. Costs of issuance ranged from 11 percent to 15 percent of the face value of the securities. In a number of the Texas cases (both those near Houston and those around Dallas) underwriting fees alone accounted for 3 percent of face value – compared to a national average of about 0.5 percent reported by Bloomberg.

Late last year, the California State Treasurer's Office released a comprehensive database of bonds issued in the Golden State with cost of issuance details. While my study provides data for a nationwide sample of bonds, the California State Treasurer's Office has now posted issuance cost details for all municipal bonds issued statewide. This impressive data set can be found here. The data were collected by the California Debt and Investment Advisory Commission (CDIAC), a unit of the State Treasurer's Office. Under state law, California local governments must report their debt data to CDIAC. The commission had been publishing some of this data, but Treasurer John Chiang, an advocate for transparency, recently decided to publish everything, including details on issuance costs.

A review of the California data shows numerous issuance cost ratios in excess of 10 percent of the issued amount – and even some exceeding 20 percent. Many of the higher issuance cost levels were associated with small bond issues from special districts. Since some of the issuance costs don't vary with issuance size, they can hit small issuers relatively hard.

In 2013, San Jacinto special districts (called Community Facilities Districts) issued two special tax bonds totaling $985,000 and $925,000 respectively. In each case, costs of issuance exceeded 20 percent.

According to the Official Statement for the $925,000 bond, the district received a mere $532,066 of the bond proceeds. The Estimated Sources and Uses of Funds on page 6 of the document show $90,428 being deposited into a reserve fund and a total of $295,890 going to the underwriter, attorneys and other service providers. The remaining $6,616 reflected an original issue discount, arising from the bonds being sold below face value.

The debt service schedule on page 10 of the Official Statement shows that the district will pay $1,240,252 in interest on the $925,000 of bonds through 2043. Total debt service of $2,165,252 over the life of the bond issue is four times the net proceeds received by the district.

Whether high-cost bonds are issued in Texas, California or another state, the victims are homeowners living in or moving into the special district; their property taxes must be increased to service the bonds. Higher tax rates must be levied over the life of these securities – often as long as 30 years – and can lead to depressed property values.

While special district voters may be unable or uninterested in protecting themselves from excessive bond fees, other levels of government can. More states can follow California's lead by making issuance cost data public and readily accessible, facilitating the type of research I have reported here (Texas has a similar resource here).

Also, regulators can take action against unscrupulous bond market providers. Earlier this year, the Financial Industry Regulatory Authority (FINRA) fined a securities firm for charging a 4.3 percent underwriting fee to a Colorado school district, concluding that the fee "was inappropriate given the underwriting work performed." Hopefully FINRA will turn its attention to special districts, thereby protecting the property taxpayers of tomorrow.

The Financial Times

By Marc Joffe

September 2, 2016

IRS Issues Final Price Regulations to Be Addressed in Fall.

The IRS priority guidelines released this month include two regulations of importance to many GFOA members: Issue price regulations and proposed rules on the definition of political subdivisions. The priority guidelines specify regulations that the U.S. Department of the Treasury will work on through June 30, 2017.

According to the guidelines, the final regulations on the definition of issue price for tax-exempt bonds will be released this year. GFOA expressed core concerns including safe harbors for competitive sales in testimony before Treasury and IRS officials in 2015. The priority guidelines also include the proposed regulations defining political subdivisions for purposes of the tax exemption, but are not likely to progress, given the extensive response from the issuer community on the topic. GFOA also spoke in opposition to these proposed rules in 2016, specifically emphasizing that the proposed rules question the legitimacy and authority of the bodies enacting the enabling legislation that created the political subdivisions in the first place.

GFOA's Federal Liaison Center will continue to monitor and report the progress of these projects and communicate GFOA's concerns to IRS and Treasury officials throughout the process.

Government Finance Officers Association

Wednesday, August 31, 2016

TAX - NEW YORK

Joon Management One Corp. v. Town of Ramapo

Supreme Court, Appellate Division, Second Department, New York - August 17, 2016 - N.Y.S.3d - 2016 WL 4371715 - 2016 N.Y. Slip Op. 05795

Property owner brought action against town seeking a judgment declaring that property's tax assessment was overstated and erroneous.

The Supreme Court, Rockland County, granted town's motion for summary judgment and denied property's owner's motion for leave to amend or to enforce settlement agreement. Property owner appealed.

The Supreme Court, Appellate Division, held that:

- Statute of limitations for tax certiorari proceedings applied to action;
- Town's motion for summary judgment was not premature;
- Supreme Court properly denied property owner's motion for leave to amend; and
- Supreme Court properly denied property owner's cross-motion to enforce alleged settlement agreement.

Statute of limitations for tax certiorari proceedings, which required such proceedings to be commenced after exhaustion of administrative grievance remedies and within 30 days after filing of the final assessment roll, applied to property owner's against town seeking judgment declaring that its property's tax assessment was overstated and erroneous, where gravamen of property owner's claim was that its property was overtaxed.

Town's motion for summary judgment on property owner's claim that its property tax assessment was overstated and erroneous was not premature, despite property owner's assertion to the contrary, where property owner failed to demonstrate how discovery might have lead to relevant evidence or that the facts essential to justify opposition to the motion were exclusively within the knowledge and control of the town.

Supreme Court properly denied property owner's motion for leave to amend its complaint against town challenging tax assessment, where property owner's proposed amendments, which were to add causes of action to recover money had and received and to recover damages pursuant to § 1983 for violation of constitutional rights, were devoid of merit.

Supreme Court properly denied property owner's cross-motion to enforce alleged settlement agreement between owner and town with regard to owner's action against town challenging its property tax assessment, where stipulation of settlement was never approved by town board, thus never becoming binding upon town.

IRS Issues New Safe Harbors for Management Contracts to Facilitate P3s.

WASHINGTON – The Internal Revenue Service on Monday released a revenue procedure containing safe harbors for management contracts that allows them to more easily be used in bond-financed infrastructure and other projects involving public-private partnerships.

Rev. Proc. 2016-44 extends terms of long-term management to up to 30 years from the previous 15 years that market participants had complained was too restrictive. It also removes the formulaic fixed fee requirements for manager compensation, allowing for more incentive compensation.

"These safe harbors aim to give municipalities tools to allow more flexible and efficient incentives for longer-term private management of tax-exempt bond financed projects to facilitate infrastructure initiatives," said John Cross, the Treasury Department's associate tax legislative counsel.

The revenue procedure will be published in an Internal Revenue Bulletin on Sept. 6.

The safe harbors apply to any management contract that is entered into on or after Aug. 22, but issuers can also apply the safe harbors to any management contract that was entered into before that date.

Issuers also have the option of applying the more restrictive safe harbors in Rev. Proc. 97-13, issued in 2013, to a management contract that is entered into before Feb. 18, 2017 and not materially modified or extended after that date.

Rev. Proc. 97-13 established safe harbors for long-term management contracts, providing safe harbors under which a contract of up to 10 years would require at least 80% of the manager's annual compensation to be based on a fixed fee. Fifteen-year contracts would require at least 95% of the annual compensation be based on a fixed fee.

But bond lawyers and other market participants complained that the safe harbors were too restrictive and had not kept pace with recent market practices, such as attempts to use bonds to help finance projects with P3s, where private parties join together with state or local governments to develop, build, and operate infrastructure projects. P3s involve long-term management contracts.

Historically, the IRS has found that bond-financed projects have private business use that may jeopardize the tax-exempt status of bonds if there is private ownership or a private lease of a building or other facility.

This new Rev. Proc. 2016-44 contains three provisions containing limits that ensure there is no private ownership or leases.

The first is that a state or local government "must exercise a significant degree of control of the use of the managed property." Second, the state or local government "must bear the risk loss upon damage or destruction of the managed property."

Third, the private party "must agree that it is not entitled to, and will not take any tax position that is consistent with the state or local government with respect to the managed property. The private party must not take any depreciation or amortization, investment tax credit, or deduction for any rent payment for the property.

The revenue procedure also carries over some restrictions from the previous one such as that there must be no net profit-sharing arrangements.

The procedure is receiving praise from many bond and tax lawyers, some of whom had submitted suggestions to Treasury and IRS on how to how to liberalize management contract safe harbors and clear up points of confusion.

Stefano Taverna, an attorney with McCall, Parkhurst & Horton in Dallas, and the chair of the American Bar Association's tax-exempt financing committee, called the new safe harbors "very significant," adding that they may help facilitate P3s. "I think Treasury did a terrific job at understanding the industry and what it will require in the future and tried to address these concerns," Taverna said. "All in all, I think the industry will welcome what Treasury put forward. It seems to be a lot more flexible and very reasonable."

Carol Lew, a shareholder at Stradling at Newport Beach, Calif., said the prior time limits and compensation structure for management contracts were "too rigid" and called the new rules "much more practical and pragmatic." The new revenue procedure is more representative of how the municipal bond industry has evolved, she said.

"It looks like Treasury and the IRS listened to comments from the industry on how to make the rules achieve IRS objectives and meet the needs of state and local governments," Lew said.

"I think this a helpful rule that can facilitate more public-private partnerships," she said. "It should be a good thing for issuers."

A management contract is defined by the IRS as a "management, service or incentive payment contract between a qualified user and a service provider under which the service provider provides services for a managed property." The contract term limit does not include the portion of a contract for services before a managed property is placed in service, such as construction design or management.

In Jan. 2015, the IRS released Notice 2014-67, which expanded the type of productivity rewards that could be used in management contracts. The notice also said that a management contract would not result in private business use if it is five years or less and compensation for services is based on a stated amount, periodic fixed fee, capitation fee, per-unit fee or any combination.

David Caprera, an attorney with Kutak Rock in Denver, said that this most recent update to management contracts acknowledges that a property manager is not supposed to be the economic equivalent of an owner of the bond-financed property, which he called a "fundamental principle."

"An owner is one who shares in the profits and losses of the business," Caprera said. "If the manager's compensation is reasonable and not tied to profits or losses, the Rev. Proc. recognizes that the manager is not an owner."

"The new rules allow long-term contracts for long-lived projects, and short-term contracts for short-lived assets so long as the compensation is reasonable and not tied to profits or losses," he added. "In particular, the '4 H's' of housing, healthcare, highways and hotels are going to be the beneficiaries, in that long-term assets can now be managed properly on a long-term basis."

Monday's revised Rev. Proc. comes one week after Treasury and IRS released their 2016-17 priority guidance plan, which included six projects for tax-exempt bonds the agencies plan to allocate resources toward through June. Asked about the plan, Cross had said that the most immediate short-term projects were to update management contract safe harbors and issue final regulations on issue price.

The Bond Buyer

By Evan Fallor

August 22, 2016

TAX - MICHIGAN
United States v. Detroit Medical Center
United States Court of Appeals, Sixth Circuit - August 17, 2016 - F.3d - 2016 WL 4376431

United States brought action against not-for-profit hospital corporation to collect Federal Insurance Contributions Act (FICA) taxes on stipends that hospital corporation paid to medical residents.

The United States District Court for the Eastern District of Michigan granted summary judgment to United States. Hospital corporation appealed. The Court of Appeals affirmed in part, vacated in part, and remanded.

IRS issued administrative ruling that medical residents were students who were exempt from FICA taxes, and issued refunds to hospital corporation.

Hospital corporation sought $9.1 million in additional interest on employer portion refunds, contending it was not "corporation" subject to lower interest rate on refunds.

The District Court granted summary judgment to United States. Hospital corporation appealed.

The Court of Appeals held that hospital corporation was "corporation" subject to lower interest on refund of employer portion of FICA taxes.

Not-for-profit hospital corporation was "corporation" under Internal Revenue Code that was subject to lower interest on refund of employer portion of Federal Insurance Contributions Act (FICA) taxes it paid for medical residents whom IRS subsequently determined were students exempt from FICA taxes. In keeping with common-law definition of "corporation," Internal Revenue Code consistently used "corporation" to include nonprofit corporations organized under state law as well as for-profit corporations, and, contrary to hospital corporation's contention, refund provision's cross-reference to subsection dealing with tax payments by C corporations was to define "taxable period," not corporations subject to lower interest rates on refunds.

Rev. Proc. 2016-44 Greatly Expands Rev. Proc. 97-13 Safe Harbor for Management Contracts, Opening the Door for Long-Term Management Contracts.

The IRS has released new management contract safe harbors that profoundly change the prior rules under Rev. Proc. 97-13. The new revenue procedure, Rev. Proc. 2016-44, which was released August 22 by the IRS, appears on first glance to have brought many favorable changes to the safe harbor rules. Unlike the prior guidance under Rev. Proc. 97-13, Rev. Proc. 2001-39, and Notice 2014-67, the new safe harbor under Rev. Proc. 2016-44 applies more principles-based tests rather than mechanical tests based on the length of the contract.

The new safe harbor takes effect immediately, but during an initial transition period running until February 18, 2017, issuers and borrowers can apply either the prior safe harbors or the new safe harbor. More specifically, the new safe harbor of Rev. Proc. 2016-44 applies to management contracts entered into on or after August 22, 2016. In addition, issuers may elect to apply the new safe harbor to management contracts entered into earlier. The prior safe harbors may continue to be applied to any contract entered into before February 18, 2017, that is not materially amended or modified on or after February 18, 2017, except pursuant to certain renewal options.

The safe harbor provided by Rev. Proc. 2016-44 is generally available to management contracts that satisfy the following six requirements:

1. General financial requirements. A contract (i) must provide only for "reasonable compensation" (ii), must not give the service provider "a share of net profits," and (iii) must not impose the burden of sharing any of the net losses on the service provider. 5.02.
2. Term of the contract. The contract term, including renewal options, must not be longer than the lesser of 30 years or 80% of the weighted average reasonably expected economic life of the "managed property" (the portion of the project to which the services relate). If contract terms relevant to the safe harbor analysis are "materially modified," the contract must be retested as a new contract. § 5.03.
3. Control over the managed property. The "qualified user" (depending on the project, this is either a governmental person or a 501(c)(3) organization) must exercise a "significant degree of control" over the managed property. § 5.04.
4. Risk of loss of the managed property. The qualified user must bear the risk of loss upon damage or destruction of the property. § 5.05.
5. Consistent tax positions. The service provider must agree "not [to] take any tax position that is inconsistent with being a service provider," e.g., by claiming depreciation with respect to (and presumably, ownership of) the managed property, or by claiming a deduction for a payment as rent (and presumably classifying itself as a lessee of some or all of the managed property). § 5.06.
6. No circumstances substantially limiting the qualified user's ability to exercise its rights. The service provider must not have any role or relationship with the qualified user that acts to substantially limit the qualified user's ability to exercise its rights under the contract. This safe harbor requirement may be satisfied by its own mini-safe harbor that requires showing: (i) that certain individuals affiliated with the service provider (e.g., directors and officers) do not control 20% or more of the vote of the qualified user's governing body, (ii) the qualified user's governing body doesn't include the service provider's chief executive officer ("CEO") or its chairperson (or the equivalents), and (iii) the CEO of the service provider is not the CEO of the qualified user (or CEO of any entity related to the qualified user). § 5.07.

Management contracts also do not result in private business use if they are an "eligible expense reimbursement arrangement." § 5.01. An "eligible expense reimbursement arrangement" means "a management contract under which the only compensation consists of reimbursements of actual and direct expenses paid by the service provider to unrelated parties and reasonable related administrative overhead expenses of the service provider." § 4.01.

Also, use by a service provider that is "functionally related and subordinate to" a management contract that meets the safe harbor requirements does not result in private business use. The functionally related/subordinate use rule is clarified by an example: Storage areas to store equipment used to perform activities required under a management contract that complies with Rev. Proc. 2016-44 does not result in private business use (and presumably would mean that such space would not be treated as leased to the service provider).

A few key points to note:

- The new safe harbor may require certain special provisions that might not otherwise appear in a management contract and might not have been required under 97-13. Where does the service provider have to memorialize its agreement not to take inconsistent tax positions? The logical place is in the text of the management contract itself. Likewise, the qualified user must document its control over the managed property through budgetary control and rate-setting powers – these also may require special contract provisions.
- Under the new safe harbor, we no longer have to examine the termination provisions of a management contract.
- We also no longer have to categorize compensation into various buckets (per unit fee, periodic fixed fee, etc.).
- The greatly expanded permitted term opens the door to tax-exempt financing for a whole new world of P3 projects with long-term concession contracts

The summary above does not include all of the specifics. The summary also does not include the full definitions of various terms in Rev. Proc. 2016-44 (most of which are in Section 4 of Rev. Proc. 2016-44).

Squire Patton Boggs

by Alexios S. Hadji

USA August 24 2016

Some Lawyers Have Questions About New Management Contract Safe Harbors.

WASHINGTON – While the Internal Revenue Service's revenue procedure on management contracts received widespread praise from many bond and tax lawyers who felt it would help facilitate bond financing in public-private partnerships, several attorneys also had questions or concerns about it.

Rev. Proc. 201644, released by the IRS on Monday, contains safe harbors for long-term management contracts of up to 30 years from the previous 15-year limit and also removes the formulaic fixed fee requirements for manager compensation.

The new safe harbor under which a management contract does not result in private business use allows for the contracts to be more accessibly used in funding bond-financed infrastructure projects and public-private partnerships as well as for more incentive-based compensation.

Dave Caprera, an attorney with Kutak Rock in Denver, said the revenue procedure is "simpler, [and] easier to understand and apply" than the prior one. He felt the previous formulaic approach involving fixed fees under Rev. Proc. 9713 released in 2013 was ineffective in addressing compensation and term length. The new safe harbors allow longer-term contracts for long-lived projects and short-term contracts for short-lived assets as long as the compensation is reasonable and not tied to profits or losses.

“The deal guys in my office are partying in the hallway,” he said.

Still, Caprera wanted to know if the term or economic life of a contract is retested when a contract is modified or a new contract is entered into.

The new revenue procedure adopts the existing tax law that treats a term which exceeds 80% of the reasonably expected economic life of a facility as being the equivalent of ownership.

“So, I have a 40-year property and I entered into a 30-year contract,” Caprera said hypothetically. “But the contract is terminated at the end of 15 years. I want a new contract. Can it be 30 years? 20 years, something else? What if the property is in bad repair and is only going to last 10 more years?”

Section 5.03 of the new revenue procedure under “Term of the Contract and Revisions” states that, “[a] contract that is materially modified with respect to any matters relevant to this section 5 is retested under this section 5 as a new contract as of the date of the material modification.”

The new revenue procedure amends Rev. Proc. 9713, which provided safe harbors under which a contract of up to 10 years would require at least 80% of the manager’s annual compensation to be based on a fixed fee. Fifteen-year contracts under Rev. Proc. 9713 required at least 95% of annual compensation to be based on a fixed fee.

The new guidance will supersede the safe harbors under Rev. Proc. 9713, which Michael Bailey, a partner with Foley and Lardner in Chicago, said will “raise many questions regarding whether certain contracts that were within the Rec. Proc. 9713 safe harbors will continue to be within the new safe harbors.”

The new rules generally require state or local governments to control rates, but many contracts under the existing safe harbors do not have that requirement, Bailey said. A major example of this is the separate billing arrangements that are often used in hospital management contracts.

Section 7 of the revenue procedure states that the new safe harbors apply to any “management contract that is entered into or after Aug. 22, 2016 and an issuer may apply these safe harbors to any management contract that was entered into before Aug. 22, 2016.”

But it adds that issuers also have the option of applying the safe harbors in Rev. Proc. 9713 “to a management contract that is entered into before Feb. 18, 2017 and that is not materially modified or extended on or after [that date].”

“For contracts entered into after that date, there could be problems,” Bailey said.

While the new guidance is more liberal than Rec. Proc. 9713 in some cases, such as long-term management contracts for public infrastructure projects, it is “not necessarily true in many other cases,” Bailey said.

He called this a “major issue” that he said will likely need to be addressed in comments submitted to the IRS and the Treasury Department.

Scott Lilienthal, a partner at Hogan Lovells in Washington, said on Wednesday that the new rules are helpful in allowing longer terms and greater flexibility for variable compensation, but had a similar analysis as Bailey.

“The revenue procedure also introduces some new conditions, such as requiring a certain amount of control over the managed facility by the qualified user, and it may take some time to see whether those new conditions may be problematic when applied to specific types of agreements,” Lilienthal said.

The new revenue procedure includes several requirements that must be met under a safe harbor in order for a management contract to avoid resulting in private business use. Similar to 9713, payments cannot be based on a share of net profits.

But the procedure also includes three new requirements to ensure there is no private ownership or lease of a project. A state or local government “must exercise a significant degree of control of the use of the managed property” and “must bear the risk of loss upon damage or destruction of the managed property.” In addition, the private party “must agree that it is not entitled to, and will not take any tax position that is consistent with the state or local government with respect to the managed property. The private party must not take any depreciation or amortization, investment tax credit, or deduction for any rent payment for the property.

Christie Martin and Maxwell Solet, attorneys with Mintz Levin in Boston, said that Rev. Proc. 2016-44 “substantially increases flexibility” for an issuer to work with private parties without jeopardizing the tax-exempt status of bonds.

In a post published on the firm’s website Wednesday, Martin and Solet wrote, “The overall impact of Rev. Proc. 201644 would seem to be an increase in the ability of bond issuers and tax-exempt users of bond-financed facilities to use for-profit contractors at bond-financed facilities. However, practitioners have already noted that the increased flexibility comes with less certainty and more facts and circumstances analysis with respect to many aspects of the safe harbor.”

“One area in which flexibility may be diminished is in the conditions under which payments may be subordinated or deferred, as the guidance indicates that timing of payment may not be conditioned on tests involving both the managed property’s revenues and expenses for any fiscal period,” they added.

Several other bond attorneys also told The Bond Buyer on Monday that it is clear the IRS and Treasury listened to industry concerns in constructing the new rules, which they said will foster more public-private partnerships.

Many market participants felt the prior rules were too restrictive regarding their ability to use tax-exempt bonds to help finance P3s, where private parties join with state or local governments to develop infrastructure projects under long-term management contracts.

The Bond Buyer

By Evan Fallor

August 24, 2016

Hawkins Advisory: 2016 Final Arbitrage Regulations

Read the Advisory.

Hawkins Delafield & Wood LLP

August 23, 2016

TAX - ILLINOIS

[State ex rel. Schad v. National Business Furniture, LLC]

Appellate Court of Illinois, First District, First Division - August 1, 2016 - N.E.3d - 2016 IL App (1st) 150526 - 2016 WL 4126773

Relator brought qui tam action under False Claims Act (FCA) against retailer, alleging that retailer knowingly failed to collect and remit use taxes on shipping charges for internet and catalog sales.

Following bench trial, the Circuit Court entered judgment in favor of retailer. Relator appealed.

The Appellate Court held that determination that retailer did not act with reckless disregard in failing to collect and remit tax was not against manifest weight of the evidence.

Trial court's determination that retailer did not act with reckless disregard in failing to collect and remit use taxes on shipping charges for internet and catalog sales was not against manifest weight of evidence in relator's qui tam action under False Claims Act (FCA). Retailer's employees testified regarding their practices in ensuring retailer's compliance with law, audit by Illinois Department of Revenue (IDOR) did not indicate that retailer's policies and practices regarding use taxes were not in compliance with law, and relator presented no evidence to show that retailer's employees were anything other than forthright with auditor.

NABL: IRS Issues New Management Contract Safe Harbors.

The IRS has released Rev. Proc. 2016-44, which provides revised management contract safe harbors under which a private management contract does not result in impermissible private business use of projects financed with tax-exempt bonds. Rev. Proc. 2016-44 will be published in Internal Revenue Bulletin Number 2016-36, dated September 6, 2016.

These revised safe harbors give State and local governments the ability to enter into management contracts with private entities to manage or operate tax-exempt bond financed projects with more flexibility for incentives in reasonable compensation arrangements and longer terms of up to 30 years (subject to an economic life limit). The revised safe harbors remove the previous requirements for prescribed percentages of fixed compensation for management contracts for different time periods.

The revised safe harbors continue a longstanding existing prohibition against sharing of net profits. The revised safe harbors add certain new principles-based constraints (governmental control, governmental risk of loss, and no inconsistent tax positions by private service providers).

The revised safe harbors are effective for any management contract that is entered into on or after August 22, 2016, and an issuer may apply these safe harbors to any management contract that was entered into before August 22, 2016. In addition, an issuer may apply the safe harbors in Rev. Proc. 97-13, as modified by Rev. Proc. 2001-39 and amplified by Notice 2014-67, to a management contract that is entered into before February 18, 2017 and that is not materially modified or extended on or after February 18, 2017 (other than pursuant to a renewal option as defined in § 1.141-1(b)).

Revenue Procedure 2016-44 is available here.

NABL: IRS Issues Corrections to Final Regulations on Non-Issue Price Arbitrage Regulations.

The Internal Revenue Service (IRS) published today in the Federal Register two documents relating to the final regulations on arbitrage restrictions under section 148 of the Internal Revenue Code that were published July 18, 2016. One document makes two corrections to the preamble and the other corrects two dates in the regulation itself.

The corrections are available here.

Not-For-Profits and the New Revenue Recognition Standard.

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU 2014-09 – Revenue from Contracts with Customers. The Standard was originally effective for annual reporting periods beginning after December 15, 2016 for public entities, and for annual reporting periods beginning after December 15, 2017 for all other entities. However, during August of 2015, the FASB issued ASU 2015-14, which deferred the effective date by one year. Public business entities, certain not-fo--profit entities and certain employee benefit plans should apply the guidance in Update 2014-09 to annual reporting periods beginning after December 15, 2017. All other entities should apply the guidance in Update 2014-09 to annual reporting periods beginning after December 15, 2018.

Is a not-for-profit organization considered a "public entity?" Possibly. A not-for-profit organization that has issued, or is a conduit bond obligor for, securities that are traded, listed or quoted on an exchange or an over-the-counter market is considered a public entity and is therefore required to implement the new standard at the earlier implementation date.

Under the new standard, an entity should recognize revenue to reflect the transfer of goods or services to customers in the amount that represents the consideration to which the entity expects to be entitled for those goods or services. An entity should apply a five-step process to determine when revenue should be recognized:

1. Identify the contract(s) with a customer.
2. Identify the performances obligations in the contract.
3. Determine the transaction price.
4. Allocate the transaction price to the performance obligations in the contract.
5. Recognize revenue when (or as) the entity satisfies a performance obligation.

Specific guidance about these steps is outside the scope of this article.

Does the new revenue recognition standard affect not-for-profit organizations? It does, if the not-fo--profit receives revenue or support that is considered to be a contract. A contract is defined as an agreement between two or more parties that creates enforceable rights and obligations. Based on this definition, donations and contributions are not within the scope of the new standard. However, not-for profit organizations have many other types of revenue and support that may qualify as contracts, such as program service revenue, membership dues and tuition, to name a few examples.

Although specific guidance of how this new standard affects certain types of organizations has not yet been finalized, the AICPA is working towards publishing audit guides for various industries to assist in determining when to recognize revenue.

On June 5, 2016, the AICPA's Financial Reporting Executive Committee (FinREC) published working drafts of interpretive guidance to address specific implementation issues for the FASB's revenue recognition standard. The implementation issues are the result of work performed by 16 industry task forces assigned by the FinREC with the task of developing guidance for a revenue recognition guide the AICPA plans to publish in January 2017. Included in the 16 task forces is the Not-for-Profit Revenue Recognition Task Force, which has issued three exposure drafts to date: 1) tuition and housing revenue, 2) contributions and 3) bifurcation of transactions between contribution and exchanges components. These exposure drafts are out for comment until September 1, 2016. The FinREC is also working on an exposure draft to provide guidance for revenue recognition related to subscriptions and membership dues, which has not yet been released.

Last Updated: August 24 2016
Article by Barbara Miller

Ostrow Reisin Berk & Abrams

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.

IRS TE/GE Advisory Committee Requests Applications.

The IRS has requested applications for members to serve on its Advisory Committee on Tax Exempt and Government Entities, which will have vacancies in June 2017; applications are due by September 26, 2016.

Click here to learn more and to apply.

NABL Submits Suggested Revisions to the Internal Revenue Manual.

On August 26, 2016, The National Association of Bond Lawyers submitted comments and recommendations for further revisions to the provisions of the Internal Revenue Manual regarding bond examinations and technical advice in an attempt to make those provisions more clear, efficient and useful both for the Internal Revenue Service and for municipal bond issuers.

The comments were prepared by an ad hoc task force of NABL members, led by Thomas Vander Molen, Dorsey & Whitney LLP, with substantial input from individual members of the NABL Board of Directors.

TAX - MAINE

Petrin v. Town of Scarborough

Supreme Judicial Court of Maine - August 16, 2016 - A.3d - 2016 WL 4367255 - 2016 ME 136

Taxpayers filed a complaint appealing the decision of the town board of assessment review denying taxpayers' applications for abatements.

The Superior Court concluded that taxpayer did not have standing to assert one of their challenges but otherwise affirmed the board's decision. Taxpayers appealed.

The Supreme Judicial Court of Maine held that:

- Taxpayers established sufficient particularized injury for standing;
- Allowing abutting properties to be treated as a single parcel violated equal protection and the state constitution;
- Allowing abutting properties to be treated as a single parcel violated statutory requirement that each parcel of real estate must be assessed separately;
- Assessing portions of larger single lots at a rate that is lower than the rate applied to the "base" portion of the lots did not violate equal protection and the state constitution; and
- Board of assessment acted within its discretion in finding that partial revaluation of waterfront and water-influenced property improved equity of town's assessments.

Sun Burn: Solar Tax Credits Scorch State Budgets.

Solar power can burn a hole in a state's budget, but a well-designed plan can bring benefits

When it comes to solar power policy, the line from "Field of Dreams" is worth taking into account: "Build it, and they will come."

Demand for residential or rooftop solar power, spurred in part by state incentives, is growing rapidly. But if incentives are not well-designed, they can overwhelm a state's budget.

Regulators and utility officials in several states have been surprised – not always in a positive way – by the effects of their solar power policies.

Louisiana is one of the more recent, and more dramatic, examples.

In mid-July, Louisiana's Department of Revenue said it was almost $30 million short of funds to pay already submitted claims for rooftop solar systems and that there were no funds to pay future claims, even though the program is not scheduled to end until Dec. 31, 2017.

A 2015 law capped the state's solar tax credit program at $10 million each for 2015-16 and 2016-17 and at $5 million for 2017-18. The state already has $9.3 million in approved credits and $29.6 million in estimated pending claims for 2015-16.

The credit, put in place in 2008, was one of the more generous among state solar tax credits, covering 50% of system costs and capped at $25,000 for an individual system.

That credit has been one of the drivers of solar power in Louisiana. According to the Solar Energy Industries Association, 32 MW of solar power – almost all of its residential – was installed in Louisiana in 2015, a 3% increase over the previous year, and the trade organization expected another 208 MW of installations over the next five years.

Industry experts say part of the reason Louisiana implemented such a generous 50% tax credit was as an effort to compensate for a residential rate structure that did not make solar power attractive.

Louisiana has a declining block rate structure, meaning that the first increment or tier of power used costs the most, with rates then dropping for customers who use more electricity.

In states like California, which has an inclining block rate structure, customers who use the least electricity pay the lowest rates. That structure creates an incentive for customers in the higher tiers to install solar panels in order to reduce their usage and rates. In states, such as Louisiana, with a declining block rate, that rate reduction strategy is not as compelling.

Louisiana's solar tax credit also had a provision that allowed a cash payment for customers who did not have enough income to use all their credits. The state's incentives were very attractive, but when lawmakers moved to rein them in, they went as far to the other side, reducing the cap while the program was still under way and by making the reduction retroactive.

Those sort of policy decisions, and resulting market disruptions, are becoming increasingly common nationwide.

Tax credits fuel Western solar boom

The sudden removal of Louisiana's tax credits may have made things worse for homeowners there, but it is not the only state where booming solar power is creating problems in the state capital.

New Mexico has also ended its solar tax credit. The state implemented its tax credit in 2008 with a 2016 sunset date. But the state set a $3 million a year cap on the program, and has hit that limit in each of the last four years, according to Mark Gaiser, a clean energy program manager with the state's Energy, Minerals and Natural Resources Department.

"New Mexico's tax credit has been running out of money every year at a faster and faster pace," said Noah Long, western energy project director with the National Resources Defense Council.

There have been two attempts to bring the tax credit back, but both have failed in the legislature. And, with the lower house of the legislature controlled by Republicans and the upper house controlled by Democrats, the chances of passing a new solar tax credit into law are slim, Long said.

In retrospect, it looks like putting a cap on the program "was kind of wise," Gaiser said. "It didn't allow for over reach."

Another western state is facing similar problems, but for now the solar tax credit program is still running in Utah, where solar power is booming.

The state saw 3,000 rooftop solar installations in 2015, and the Governor's Office of Energy Development expects to process 12,000 applications this year. If all those applications turn into installations, it would mean more rooftop solar would be installed in 2016 than in all prior years combined.

The boom has been driven by the falling costs of solar panels, as well as at least three different state solar incentives. In addition to a state solar tax credit, Utah has a net metering program and the state's largest utility, Rocky Mountain Power, until recently offered a rebate on the cost of installing solar power.

The utility rebate was about 1.5 cents per watt of installed rooftop solar. The program was set up as a lottery under a five year program and was very popular. Over four years, the utility provided $40 million in rebates.

But in March the state legislature signed off on Rocky Mountain Power's proposal to end the program in its fourth year and switch it to a broader initiative, the Sustainable Energy and Transport Program, which includes incentives for transportation and energy storage, as well as for solar power.

"We think the solar industry is no longer an unknown quantity," Rocky Mountain Power spokesman Paul Murphy said. "So, we don't think it needs additional incentives. We would rather use the funds for all customers."

Utah also provides a solar tax credit equal to 25% of the cost of a system, capped at $2,000 per system. But the rapid growth of rooftop solar in the state is raising concerns among lawmakers.

When the tax credit was created in 2012, it was a $1 million program, this year it is going to hit $25 million or $40 million, Jeffrey Barrett, deputy director of the Governor's Office of Energy Development, said. "The word 'exponential growth' was created for this sort of thing."

"The legislature is worried as hell about the fiscal impact," Barrett said. "I think new legislation is being drafted right now."

What form that legislation will take is still unknown, he said. It could be a cap or a cap and a phase out, but "in the future, it will be a completely different program."

By law, Utah's the tax credit comes up for review in 2017.

State funding struggles a trend

Overall, the expiration of state solar tax credits has become a national trend.

"I think that it is due in part to budgetary problems, but also due to solar's increasing maturity," Autumn Proudlove, senior policy analyst at NC Clean Energy Technology Center at North Carolina State University, said.

Many of the tax credit programs were put in place to help solar power get off the ground, but with the growing penetration of solar, some states are letting those programs expire.

At the beginning of 2015, 15 states had residential solar tax credits. Now, 11 states have them, and programs are set to expire in Iowa at the end of 2016, in Louisiana and Oregon at the end of 2017, and in Maryland at the end of 2018, according to the Database of State Incentives for Renewables and Efficiency (DSIRE).

In part this a reflection of the natural life span of a tax credit. Tax credits are often put in place to help a technology transit to commercial viability. In some states, legislators are letting them expire because they believe the technology has advanced far enough that tax credits are no longer necessary.

North Carolina is an interesting example, Proudlove said. The state tax credit really helped develop the state's utility-scale solar market, but the residential and commercial solar markets are still small and have really dropped off since the tax credit expired, she said.

According to a survey conducted by the Utah Solar Energy Association, 80% of the respondent said that the tax credit was "important" of "very important" in their decision to install solar panels on their rooves, Ryan Evans, president of the trade group said.

Reducing or capping Utah's solar tax credit "would not send the right message right now," Evans said. "After all, there are only so many Utahans. The boom can't last forever." Eventually everyone who wants solar power will have it or all the roofs will have solar panels, he said.

The other factor that needs to be considered, Evan said, is that tax credits bring in business. "My guess is that the state gets their money back" through increased sales tax and corporate taxes.

According to a report by the North Carolina Sustainable Energy Association, North Carolina energy projects generated $1.54 of state and local government tax revenue for every $1.00 taken in tax credit.

But, as Evans pointed out, "Not all tax credits are created equal." And there is a fair amount of variety when it comes to solar tax incentives. California uses a tax exemption for solar equipment instead of a credit on a tax return. Other states also give an adjustment or deduction on property taxes, but can lead to problems.

Not only do property values change, they are very local, and "it is difficult for developers to know the value," said Sean Gallagher vice president for state affairs at the Solar Energy Industries Association.

Gallagher noted that most tax credits are designed with sunset dates or budget caps. "It is not unusual for them to have a limit,"

In a well-designed system, there needs to be a recognition of the importance of planning, from the perspective of the state, as well as that of the homeowner and the developer. The simplest way to do that is to have a clear expiration date for the tax credit and clear definitions of qualifying factors such as construction start dates.

Other features, such as reserve funds and triggers, can also be helpful tools. They let consumers know when the credits are close to expiration or near capacity.

It's best to design programs with a budget cap or an expiration date, "people need to be able to plan for it," Gallagher said. The worst thing to do, though, is to change the tax credit or lower the cap retroactively. In those situations people stand to lose their investment, Gallagher said.

Utility Dive

By Peter Maloney | August 17, 2016

Philadelphia Business Taxes: Incentives and Exemptions.

Like many cities, Philadelphia does not regularly evaluate whether tax breaks achieve their goals

Overview

Philadelphia business tax rates are among the highest of any large city in the nation, and the tax structure is frequently cited as one reason for the city's relatively weak job-creation record over the past several decades. A key element of that structure is the business income and receipts tax (BIRT), which taxes profits and revenue of businesses located in the city. Only 11 of the nation's 30 largest cities impose levies on corporate profits or revenue, and only Philadelphia does so on both.

To make these business taxes less onerous, Philadelphia's leaders have created a large and varied group of tax incentives and exemptions. Known as tax expenditures, they constitute an integral but little-understood aspect of the city's business tax policy. Supporters view the expenditures—which do not appear in the city's budget or financial statements—as investments in growing, maintaining, and attracting businesses, thereby enhancing the tax base. Critics see them as drains on public resources that have little accountability, haphazard goals, and scant proof that they pay off in business growth or future tax revenue.

To help policymakers and the public better understand the role that these measures play in Philadelphia's overall tax policy, The Pew Charitable Trusts sought to quantify the city's tax expenditures and compare them with those of other major cities. In Philadelphia, the analysis looked at two types of tax expenditures: incentives to spur companies to take specific actions, such as hiring more workers or investing in neighborhoods; and industrywide exemptions to support particular business sectors deemed by policymakers to merit special treatment. The study covered two periods, 2001-03 and 2010-12, in order to show change over time; the 2010-12 data were the most recent for which information was complete.

The research found that Philadelphia has 21 city-approved business tax reduction programs or provisions, the most among the nation's 30 largest cities. Eight of those reductions took effect after 2012, too late for their impact to be included in this analysis.

The research also found that from 2010 to 2012, the tax incentive programs resulted in an average of $109.6 million per year in forgone revenue for the city and the school district—a 634 percent increase from 2001- 03, when the average annual inflation-adjusted amount was $14.9 million. This report describes revenue as "forgone" rather than "lost," in part because repealing the tax incentives would not necessarily restore an equivalent amount of money to local coffers; businesses probably would alter their operations to reduce their tax liabilities.

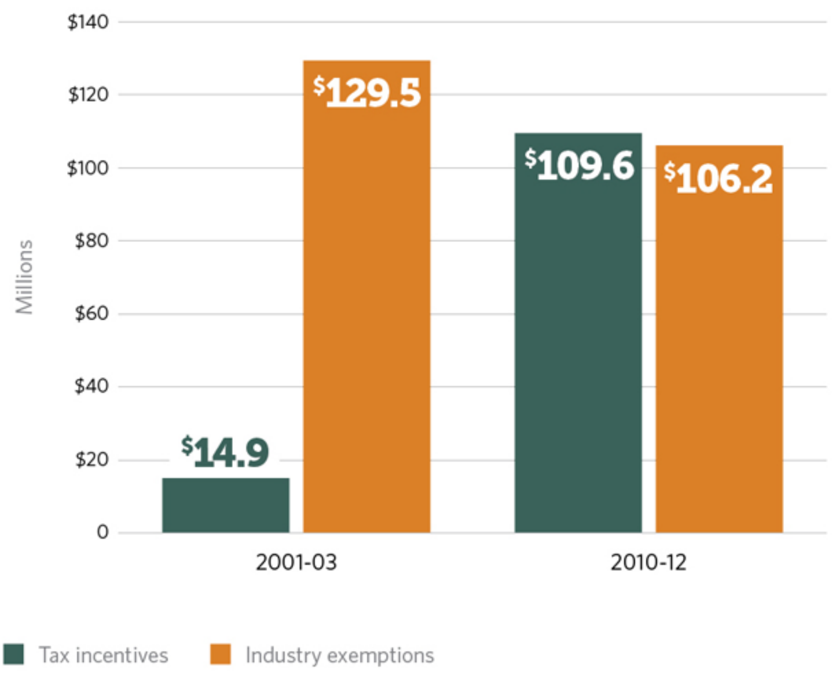
The vast majority of the $109.6 million stemmed from two programs: the 10-year property tax abatement on new construction and building improvements for commercial and industrial property, and the Keystone Opportunity Zone initiative, which exempts businesses within designated areas from state and local business taxation. Like all tax incentives, both of these programs require companies to commit to making new investments in the city and are in effect for limited periods of time.

The other main source of tax expenditures—industrywide exemptions primarily for finance, insurance, utilities, and port-related firms—produced at least $106.2 million in forgone revenue annually from 2010 to 2012. The amount was 18 percent less than in 2001-03, adjusted for inflation. Unlike tax incentives, exceptions are granted to individual companies without any time limits. Companies determine their eligibility in tax filings, which city auditors can challenge. (See Figure 1.)

Figure 1

Forgone Business Tax Revenue in Philadelphia

Annual average, in millions



From 2001-03 to 2010-12, Philadelphia's forgone business taxes grew primarily as the result of expanded use of tax incentives meant to retain and attract businesses and to spur real estate development, hiring, community reinvestment, and other commercial activity. The average annual amount of forgone revenue from tax incentives increased by 634 percent. Industry-specific exemptions declined 18 percent. All figures are inflation-adjusted to 2012 dollars.

Note: See Appendix D for list of credits, abatements, and exceptions.

Source: Pew analysis of Philadelphia Department of Revenue and Office of Property Assessment records

Whether these tax expenditures have paid off for Philadelphia is hard to say. There is no question that there have been benefits, in terms of jobs created and buildings constructed. The issue is whether those benefits outweigh the costs.

Philadelphia reports on some of its smallest tax-expenditure programs but does not conduct comprehensive analyses of how much all the tax expenditures cost or whether they achieve their purposes—and is not required by law to do so. Only a few cities, including New York and Washington, require that kind of reporting. For those reasons, this report does not compare forgone revenue for the city of Philadelphia and the school district with other jurisdictions.

In 2012, the staff of the Pennsylvania Intergovernmental Cooperation Authority (PICA), a state agency that oversees Philadelphia's finances, called on the city to clarify and evaluate specific tax expenditures, concluding: "A lack of detailed accounting prevents a systematic process of evaluating whether the costs of these policies are justified in relation to their benefits."

This study does not attempt to determine whether Philadelphia business tax expenditures have met their goals, but it does look at ways that cities can design programs to include evaluations. According to public finance and policy analysts, measuring the impact of tax benefits and setting clear rules for receiving them are key steps toward an effective and equitable tax system that fosters economic development and generates needed revenue.

Conclusion

For several decades, business leaders and tax experts have called for transformation of the city's entire tax structure in order to improve Philadelphia's competitiveness with its suburbs and other large cities. The recent overhaul of the city's property tax system, the Actual Value Initiative, was viewed as an important first step in laying the groundwork for comprehensive change.

Given the increase in forgone taxes over the past decade, tax expenditures merit a place in Philadelphia's tax policy discussion. Knowing how much these tax exceptions cost, and whether they are meeting their goals, is a key component of a coherent and equitable city tax policy.

Download the full report.

The Pew Charitable Trusts

TAX - ALASKA

Bingman v. City Of Dillingham

Supreme Court of Alaska - August 12, 2016 - P.3d - 2016 WL 4257176

City petitioned for foreclosure of taxpayer's property. Taxpayer intervened.

The Superior Court entered judgment and decree of foreclosure, and taxpayer appealed.

The Supreme Court of Alaska held that:

- City did not accept taxpayer's proposal to redeem his foreclosed property, and
- Taxpayer did not satisfy statutory requirements for repurchasing his foreclosed property.

City did not accept taxpayer's proposal to redeem his foreclosed property by offering city promissory note for amount due, without interest, that would mature 20 years later, even though proposal stated that silence would be treated as acceptance, and city did not reject offer in manner outlined in taxpayer's proposal, where city sent letter rejecting offer, never recorded taxpayer's redemption, and did not issue certificate indicating that he had redeemed property, but instead published notice of expiration of redemption period, and moved for properties to be transferred by tax deed.

Taxpayer did not satisfy statutory requirements for repurchasing his foreclosed property by offering city promissory note for amount due, without interest, that would mature 20 years later, where offer was made before tax deeds transferred property to city, and failed to meet statutory provisions for calculating purchase price.

Why a Judge Allowed a Challenge to a Private Activity Bond Allocation.

BRADENTON, Fla. — Two Florida counties can move forward with the first lawsuits ever to challenge a private activity bond allocation from the U.S. Department of Transportation.

In a 39-page ruling late Tuesday, U.S. District Judge Christopher R. Cooper sided with Martin and Indian River counties, both of which objected to the USDOT's award of $1.75 billion in private activity bonds for the All Aboard Florida passenger train project.

The planned passenger trains would pass through the two counties on their route between Miami and Orlando.

Cooper said that the counties proved that the bond allocation should have been considered in a federal environmental review process. He denied motions to dismiss the case by the USDOT and All Aboard Florida.

“Martin County is very pleased with the decision and believes that the public will have more information as a result of the court action than they’ve ever had before about the project,” said Stephen Ryan, a partner with McDermott Will & Emery LLP, which represents Martin County.

Cooper said that the counties had legal standing to proceed with their challenges because they demonstrated that the $3.5 billion train project likely will not be built without tax-exempt financing — a reversal from a decision in June 2015.

Cooper said information produced during discovery raised “legitimate questions” about All Aboard Florida’s commitment to completing the second phase of its project, from West Palm Beach to Orlando, without the use of private activity bonds.

“First of all, PAB-based financing is not just the ‘current financing plan’ for the project – it appears to be the only financing plan,” Cooper wrote. “This strikes the court as unusual given the uncertainty surrounding the PAB issue, particularly for a company that has expressed its concern” about keeping the project on schedule and avoiding losses due to delays.

Cooper said the issue “casts some doubt as to whether AAF is truly serious about moving forward with phase 2 of the project regardless of the outcome of this lawsuit.”

“It also indicates that AAF may have simply assumed that alternative financing would be available,” he said.

The ruling is a “really significant victory,” said Indian River County Attorney Dylan Reingold.

He said that information the counties produced in discovery convinced the judge to change his mind about whether AAF needed bond financing for Phase 2 of the project.

“The judge told us we have standing, and we met that burden,” he said.

USDOT referred questions to the U.S. Department of Justice, which did not immediately respond to requests for comment.

All Aboard Florida did not immediately respond to requests for comment.

AAF, which is owned by Fortress Investments Group, is attempting to create a privately funded and operated passenger train service, the nation’s first in decades.

Private financing is in place for its first phase, linking Miami, Fort Lauderdale and West Palm Beach, where stations are under construction, according to court documents.

In Phase 2, Martin and Indian River counties have cited potential harm to public services and archaeological sites from 32 planned high-speed trains daily in separate suits filed in the District of Columbia.

Both cases contended that USDOT’s December 2014 allocation of bonds should have been considered as part of federal agency reviews under the National Environmental Policy Act.

USDOT and All Aboard Florida argued that the approval of private activity bonds was not a major federal action that would trigger a NEPA review.

The judge disagreed.

Cooper compared the benefits of the $1.75 billion PAB allocation with a $1.6 billion low-interest loan that All Aboard Florida applied for from the Railroad Rehabilitation and Improvement Financing program.

Under federal rules, the RRIF loan is considered a major federal action that triggered a NEPA review, although AAF has not completed the loan process.

"In the court's view, then, if the amount of federal assistance conferred by the RRIF loan can support a finding of major federal action, so too can the amount of federal assistance conferred by the PAB-allocation decision," Cooper said.

Cooper also said the fact that USDOT, as a condition of receiving the PAB financing, required All Aboard Florida to comply with an "extensive" list of mitigation measures imposed by the final environmental impact statement indicated that USDOT had "the requisite degree of control called for by NEPA and related statutes so as to implicate major federal action."

Cooper refused to dismiss claims by the counties that the bond allocation violated NEPA, the National Historic Preservation Act and the Department of Transportation Act.

"I see this as a big game changer as to where this case proceeds," Reingold said.

Ryan and Reingold said they would confer on the next stage of the litigation, which could be a trial or a ruling on summary judgment.

All Aboard Florida has said it plans to begin the first phase of train service – which it has branded as "Brightline" — next year.

The company tried and failed to privately place the unrated, uninsured bonds after the Florida Development Finance Corp. agreed to be the conduit issuer last year.

The company blamed the tight bond market, as volatility increased and high-yield investor demand dried up in the months before the Fed increased the borrowing rate 25 basis points in December.

The delayed sale led the USDOT in December to grant AAF an extension of time to issue the bonds and agree to allow the debt to be sold in multiple offerings, rather than issuing all $1.75 billion at one time.

In Tuesday's ruling, Cooper examined difficulties AAF had issuing the PABs as part of his analysis about whether the company could avail itself of other types of financing.

AAF's first tried to sell the PABs in August at an interest rate of 6% for a single tranche of up to $1.75 billion, Cooper said, adding, "AAF found that it could not sell all its PABs at that rate on the terms it wanted."

In September, deal was structured at a higher 7.5% interest rate with bonds in two tranches, one for $1.35 billion and the other for $400 million.

"Again, there was insufficient interest from investors for AAF to close on the sales on AAF's terms," Cooper said.

In November, after issuing a third supplement to the offering memorandum, AAF kept the projected interest rate at 7.5% but added additional terms "that were arguably more favorable to investors," he wrote.

"Each time [AAF] was either unable to conclude a deal or chose not to do so, depending on whose framing of the issue one prefers," Cooper said. "Either way, the fact remains that the AAF project repeatedly did not generate sufficient interest to result in a sale of all bonds at the 7.5% rate."

All Aboard has argued that it would use other forms of financing for the project, including taxable bonds, but the judge was skeptical of its ability to do so.

"It strikes the court as reasonable that a full sale of the PABs would require an interest rate of at least 8% in the present market, which would bump the interest rate for taxable bonds into the range that AAF acknowledged is unacceptable."

A banker familiar with the PAB deal, who asked not to be identified, said he was told that AAF decided to postpone the offering until all legal issues were cleared up.

All Aboard Florida has until Jan. 1 to issue the bonds, according to the USDOT.

In a statement Wednesday, CARE FL, a local anti-train organization, said that although AAF claims that it is a privately funded project the court ruling proves that AAF is dependent on public support from the tax benefit provided by allowing tax-exemption on its bonds.

The group's steering committee chairman, Brent Hanlon said AAF would travel through heavily populated Treasure Coast areas and require residents to bear additional financial burdens and safety risks.

"We especially applaud the Martin County and Indian River Board of County Commissioners and legal teams for their leadership and steadfast commitment in the fight against AAF," Hanlon said.

The Bond Buyer

By Shelly Sigo

August 17, 2016

An Under-the-Radar Tax Benefit in Muni-Bond Funds.

Funds treated differently from individual munis, allowing investors to claim a tax loss

It's common knowledge among many investors that interest from municipal-bond funds are generally free of income taxes. What is not such common knowledge is that, if used right, muni-bond funds may have a negative tax rate.

That is to say, in addition to tax-free income, investors may be able to take a tax loss without actually incurring an economic loss. Because muni investors are typically in a high tax bracket, this strategy may have broad appeal.

The idea revolves around the fact that interest rates have declined and muni-bond coupon payments are higher than the so-called SEC yield. The SEC yield, created by the Securities and Exchange

Commission to help comparisons among bond funds, represents the fund's true income and carves out any return of capital that is included in the distribution yield. This creates a potential opportunity, according to Joel Dickson, global head of investment research and development at Vanguard Group.

How the Strategy Works

Muni bonds are typically issued at a premium in excess of the face amount of the bond. Because rates have declined, the premiums are now even greater. For example, if you bought a muni bond (not a fund) at $110 that would mature at $100 in five years, roughly $2 a year is just return of your own principal, though the regulator, the Municipal Securities Rulemaking Board, allows it to be called income. After a year, your $110 cost basis would be adjusted to about $108, and you would see that adjusted cost basis on your brokerage statement. Because the cost basis is adjusted down—something known as amortization of premium—you can't sell it a year later at a loss because you were paid back that principal and have no economic loss.

Bond funds, however, are treated differently than owning the bond directly. The amortization of premium doesn't impact the cost basis and thus losses can be claimed even though none were incurred.

Here's how it can work for you or your client, using the example of a muni fund from Mr. Dickson's firm:

Say the Vanguard Intermediate-Term Tax-Exempt Admiral fund has an SEC yield of 1.35%. Though this is the true income, the total distribution yield is 2.79%, meaning 1.44 percentage points is return of principal from an economic perspective. If this continued for a year, an estimated loss of the net asset value of 1.44 percentage points could occur.

The Tax Benefits

For a $100,000 investment over a year under this scenario, the investor would have been paid $2,790 in cash, with $1,350 of that in income and $1,440 in return of principal. You could then sell the fund to recognize the $1,440 tax loss and buy a different low-cost muni-bond fund. This capital loss can be used up to the Internal Revenue Service limit of $3,000 a year or an unlimited amount to the extent you have capital gains this loss could offset.

If you have short-term capital gains , you save at an ordinary income-tax rate. Yet even if a long-term capital gain, you may save 25% or more after taking into account the alternative minimum tax and the Medicare tax that affect so many of the higher-taxed investors who typically own munis.

So the tax loss of 1.44 percentage points on a $100,000 investment at a 25% marginal tax rate translates to a 0.36% tax benefit, or a $360 savings. This may not seem like much, but frame the extra 0.36% with the 1.35% SEC yield to give you a 1.71% tax-free benefit.

Pitfalls to Ponder

Tax laws are complex and Mike Piper, author of "Taxes Made Simple," points out that the fund must be held for six months or the losses could be disallowed according to IRS rules. 852(b)(4)(B).

Also, the actual loss is going to vary based on other factors, such as the direction of interest rates, what investor perceptions are of muni-bond risks, and the muni-bond fund used to execute the strategy.

While these factors will result in the loss being either more or less than estimated, the same factors are also likely to be present if an investor owned the muni bonds directly rather than through a fund. And, of course, muni bonds also have risks of real losses whether owned directly or through a fund. But if you decide munis are right for part of a portfolio, the low-cost muni-bond fund can be superior to bonds from a tax perspective.

And beyond a tax perspective, there are 5 other reasons bond funds are superior to owning the bonds directly. When it comes to muni bonds, there are now 6 reasons funds are superior.

THE WALL STREET JOURNAL

By ALLAN S. ROTH

Aug. 19, 2016 10:54 a.m. ET

—Allan S. Roth is the founder of Wealth Logic, an hourly-based financial-planning firm in Colorado Springs, Colo. His contributions aren't meant to convey specific investment advice.

IL Taxpayers Can Sue to Block Business Tax Credit Program Costing the State Too Much: Panel

An Illinois appeals panel in Springfield, in overturning a lower court decision, has ruled taxpayers have the right to try to block a state commerce agency from administering a business development tax credit program the group of taxpayers has argued is actually an alleged illegal state tax improperly eating up public funds.

The Aug. 2 opinion was penned by Justice Thomas Appleton, of the Illinois Fourth District Appellate Court in Springfield, with concurrence from justices Thomas Harris and Robert Steigmann. The decision upset a ruling by Sangamon County Circuit Court Judge John Madonia, who had tossed a suit by 10 taxpayers against the Illinois Department of Commerce and Economic Opportunity. The case was sent back to circuit court for further proceedings.

The taxpayers brought the action in January 2015, alleging the department overstepped the boundaries of a state law, called the Economic Development for a Growing Economy Tax Credit Act. The Act gives tax breaks to businesses that create new jobs, by giving a tax credit in the amount of the income tax withheld from new employees' paychecks. However, plaintiffs alleged the department is allowing credits in the amount withheld for both new and retained employees.

Plaintiffs argued that as a result, these overindulgent tax credits could diminish the public treasury, with taxpayers having to make up the difference. Apart from that alleged damage, plaintiffs contended they are harmed by the department's misapplication of their tax dollars to administer an illegal regulation. They sought an injunction to halt the tax breaks.

Circuit Judge Madonia ruled plaintiffs lacked standing to pursue the case, because the state had the only interest in the matter and taxpayers suffered no harm. Madonia said the only way plaintiffs could have a stake was for them to claim the tax statute was unconstitutional, not to challenge how the statute was interpreted or how funds were spent. Plaintiffs appealed.

Justice Appleton was not impressed with plaintiffs' contention taxpayers might have to make good the deficiency in tax revenue caused by the excessive tax credits, saying the argument was "speculative and simplistic."

"Can one really predict the legislature will probably raise taxes because of the excessively generous tax credits that defendant will grant?" Appleton asked.

However, Appleton was persuaded by plaintiffs' other argument that "collecting it (an illegal tax) will be a misuse of taxpayer-funded salaries and offices and, as such, a misuse of public funds."

The state maintained, as it did in circuit court, that the suit was improper, because plaintiffs were trying to exercise a right that belonged to the state alone. The state pointed to federal rulings to bolster its position, but Appleton noted Illinois courts are "more generous" in granting legitimacy to citizens bringing tax suits.

"Unless the administration of an illegal regulation is cost-free (and it is difficult to see how it ever would be), the taxpayer has standing to seek an injunction, regardless of whether the regulation would bring a net profit to the state and regardless of whether the cost of administration is small," Appleton observed. "It will always cost something to administer a regulation, including an illegal one. The machinery of the State never runs cost-free."

Appleton cautioned that although taxpayers can challenge the legality of a regulation in court, they cannot attack the regulation on the ground it is "unwise," "inefficient" or "improvident."

Plaintiffs are represented by lawyer Jacob Huebert, of the Liberty Justice Center in Chicago, which says its mission is to "revitalize constitutional restraints on government power." The Illinois Department of Commerce and Economic Opportunity is defended by Illinois Attorney General Lisa Madigan's office.

The Cook County Record

by Dan Churney

Aug. 8, 2016, 4:42pm

TAX - GEORGIA

Columbus, Georgia Board of Tax Assessors v. Medical Center Hospital Authority

Court of Appeals of Georgia - July 7, 2016 - S.E.2d - 2016 WL 3654495

Hospital authority filed action against board of tax assessors, city, and county tax commissioner, seeking a declaration that its leasehold interest in a continuing care retirement facility was public property exempt from ad valorem taxation.

The Superior Court granted summary judgment for the authority. Tax board appealed.

The Court of Appeals held that hospital authority's leasehold interest was public property exempt from ad valorem taxation.

Hospital authority's leasehold interest in a continuing care retirement facility was public property exempt from ad valorem taxation. Revenue bond validation proceedings had conclusively established that the retirement facility furthered a legitimate function of the hospital authority.

Under state constitution, a judgment in a revenue bond validation proceeding is conclusive as to all questions which could and should have been asserted and adjudicated during the bond validation proceedings.

Even the Giants Are Complaining About San Francisco Real Estate.

A prominent tenant with a gorgeous waterfront location in the nation's most expensive city wants a big break on its property tax bill. It may have a case for getting one.

The tenant is the San Francisco Giants, who hold the lease at AT&T Park, where they play baseball. The stadium's location is prime real estate, with stunning bay views and close proximity to downtown, light rail and the Bay Bridge. Home prices have more than doubled in the city since the team built the park 16 years ago. Even though city assessment increases are limited under California law, the land value is expected to rise another 7 percent this year.

Assessor-Recorder Carmen Chu argues that it's only right for the Giants to pay their fair share of the increased worth, just like any homeowner or office building. "At the end of the day," Chu says, "we're talking about real estate values, which fundamentally come down to location. San Francisco and particularly the area of the city that the stadium is in is highly desirable," Chu says. "It's one of the fastest-growing areas."

But the Giants say Chu is asking for way too much. Two years ago, she retroactively doubled the team's property tax bill going back to 2011. The Giants have taken their case to the San Francisco's assessment appeals board. The team argues that its lease on the land is decreasing in value the longer they are tenants. The lease still has 66 years left to go, but the Giants seem to believe the value of the stadium itself is depreciating in the same way a car does.

That argument prevailed a decade ago, when the Giants won an earlier dispute over their property tax bill. But it's a debatable point, says Victor Matheson, a sports economist at College of the Holy Cross. Under income tax rules, the value of a property can depreciate over time. But that's not true under property tax rules. No one could argue that a 100-year-old house in good shape in an upscale neighborhood has no value.

The case for depreciation is undercut by the fact that AT&T Park not only still sparkles but is clearly bringing in lots of money for the team. "It's not like it's now generating half the money that it did when it opened," Matheson says.

The two sides are far apart. But regardless of the appeal's outcome, Chu should take heart from one thing. The Giants may not be paying as much as the assessor thinks is right, but anything at all is more than most sports franchises pay in property taxes. Usually, they're either playing in a municipally owned stadium or they've gotten a break on taxes as part of the initial deal. "They avoid paying taxes almost all over the country," Matheson says.

GOVERNING.COM

BY ALAN GREENBLATT | AUGUST 2016

IRS Ends Eight-Year Audit of Florida's Villages Without Penalty.

The U.S. Internal Revenue Service has closed an eight-year exam of about $300 million of tax-exempt bonds issued for The Villages, one of the world's largest retirement communities, without imposing a penalty, according to a filing by the development districts that issued the debt.

The Village Center Community Development District and the Sumter Landing Community Development District, located about 60 miles (97 kilometers) northwest of Orlando, said the IRS notified them on July 14.

"We were steadfast in maintaining that the districts had followed the law and that there was no factual basis for the IRS examination," wrote district manager Janet Tutt in a July 18 memo listed Wednesday on the Municipal Securities Rulemaking Board's disclosure website. "To have this examination finally closed without penalty is a tremendous victory for our community and vindication of our supervisors and district staff who do a tremendous job serving our residents."

The districts, created by the late billionaire developer H. Gary Morse, issued the bonds to purchase golf courses, recreational centers and other amenities that Morse build. The IRS said that the bonds shouldn't have received tax-exempt status because the boards were appointed by Morse and the majority of the members worked for him. The IRS also maintained the bonds were issued for private, not public, purposes.

"We have concluded that closing this examination without further IRS action supports sound tax administration," wrote Allyson Belsome, an IRS field operations manager for tax-exempt bonds in a July 11 letter to the development districts.

"Federal law prohibits the IRS from discussing specific taxpayers," said IRS spokesman Dean Patterson.

During the course of the audits the district refinanced the bonds in 2014 with taxable bonds to take advantage of lower interest rates.

Bloomberg Business

by Martin Z Braun

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