

OVERVIEW OF FEDERAL TAX LAWS APPLICABLE TO GOVERNMENTAL AND 501(C)(3) BONDS

ALAN BOND, BLX GROUP
BARBARA JANE LEAGUE, ORRICK



Topics

- Why does the IRS care about tax-exempt bonds
- Tax-exempt bonds compliance overview
- What is arbitrage (rebate)
- What is private business use
- Closing thoughts

Why does the IRS care?

- Tax-exemption of the interest payable on your bonds is viewed as a federal subsidy
- IRS cares about ***who gets the benefit of that subsidy*** (private business tests), ***how much subsidy is received*** (arbitrage rules)
- IRS wants to ensure that the federal subsidy is being properly utilized

Why does the IRS care?

- Arbitrage rules are designed to identify situations in which the issuer improperly increases the subsidy received
- Private business tests are designed to identify situations in which too much subsidy is received by nonqualified recipients (entities other than governmental entities, and in the case of 501(c)(3) bonds, 501(c)(3) entities)

Tax-Exempt Bonds Compliance Overview

- Requirements at closing of bond transaction
 - Tax form filings – 8038/8038-G
 - Reasonable expectations
 - Investment of proceeds
 - Expenditure of proceeds
 - Use of property
 - Must certify to these expectations to be able to issue the bonds

Tax-Exempt Bonds Compliance Overview

- Requirements relating to ongoing monitoring after the issuance of the bonds
 - Arbitrage rebate and yield restriction
 - Requires periodic calculations – at least every 5 years and payment of any arbitrage rebate to the IRS
 - Requires monitoring over the life of the bonds to determine whether the yield on investments acquired with bond proceeds are properly restricted

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