



The Stimulus Act of 2009: Alternative Financing Mechanisms

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Bond-Related Provisions Contained in the American Recovery and Reinvestment Act of 2009 (the "Stimulus Act") – the Alphabet Soup

- Marketability Enhancements for Tax-Exempt Bonds
 - Bank-Qualified Eligible Bonds ("BQ Bonds")
 - Changes to Alternative Minimum Tax
- New Categories of Bonds
 - Recovery Zone Bonds:
 - Recovery Zone Economic Development Bonds ("RZEDs")
 - Recovery Zone Facility Bonds ("RZFBs")
 - Build America Bonds ("BABs")
 - Qualified School Construction Bonds ("QSCBs")
 - Tribal Economic Development Bonds

- Expanded Definition of “Manufacturing” for Small Issue Industrial Development Bonds (“IDBs”)
- Modified and Allocations Increased
 - Qualified Zone Academy Bonds (“QZABs”)
 - New Clean Renewable Energy Bonds (“New CREBs”)
 - Qualified Energy Conservation Bonds (“QECBs”)
- Application of Davis-Bacon Act of 1931 (Prevailing Wage Laws) to Certain Bonds

- Enhanced Marketability Provisions
 - BQ Bonds
- Build America Bonds
 - Tax Credit Option
 - “Direct Pay” Option
- Recovery Zone Economic Development Bonds

- Changes in Bank Qualified Eligible Obligations ("BQ Bonds")
- Special rule for financial institutions
 - General Rule: Financial institutions cannot deduct the interest expense to purchase or carry tax-exempt obligations
 - Exception: Financial institutions can deduct 80% of the carrying cost associated with purchase of BQ Bonds
 - Goal: Lower tax-exempt borrowing rate

Pre-Stimulus Act

- BQ Bonds were governmental or 501(c)(3) bonds issued by or on behalf of local governments that did not expect to issue more than \$10 million of such bonds in that calendar year
- BQ Bonds could not be sold in a pooled or composite issue with an aggregate face amount in excess of the \$10 million limit

New BQ rules under Stimulus Act

- BQ limit is increased from \$10 million to \$30 million for each of 2009 and 2010
- Each 501(c)(3) entity is now treated as an issuer with its own limit
- Issues may be pooled – for example, a single issue of \$50 million might be done benefiting two borrowers for \$25 million each

Key Points and Predictions on BQ Provisions

- Each 501(c)(3) entity having its own BQ limit is VERY IMPORTANT and likely to promote significant volume
- Municipal issuer (e.g. EDA/IDA) should evidence in bond documents that 501(c)(3) entity is using its own BQ limit
- Outstanding Non-BQ Bonds (including some taxable issues and loans) may be able to be refunded and become BQ bonds if within the issuer's \$30 million limit

Build America Bonds ("BABs") – Tax Credit Option

- For issuers able to issue otherwise tax-exempt governmental bonds (not private activity bonds), the issuer, during 2009 and 2010, may elect to issue such bonds as taxable interest bonds and permit bondholders to receive a tax credit equal to 35% of the total interest coupon paid on each interest payment date
 - Capital projects and working capital included
- Rules similar to tax credit bonds under IRC § 54A apply except that credit is determined based upon amount of interest paid

BABs – Tax Credit Option (continued)

- No national ceiling on the amount of Tax Credit BABs
- Cannot have more than a *de minimis* amount of premium over the stated principal amount of the obligation

BABs – Direct Pay Option

- For *capital project* BABs issued during 2009 or 2010 (as opposed to financing working capital), issuers may, in lieu of the tax credit to bondholders, elect to receive a direct payment from the Federal government
- The amount of the payment is 35% of the amount of interest payable on the interest payment date
- Bondholder still receives taxable interest

BABs – Direct Pay Option (continued)

- NO limitation on the amount of Direct Pay BABs that may be issued
- 100% of available project proceeds (net of any amounts placed in a reasonably required reserve fund) must be used for capital expenditures; 2% costs of issuance limitation
- Unless a state's laws are changed after 02/17/09, the taxable interest or credit for any Direct Pay BAB is to be treated as federally tax-exempt for purposes of such state's income tax laws

IRS Notice 2009-2026 (April 3, 2009)

- Made “Direct Pay” BABs tangible and user-friendly
- Instructions on how to claim subsidy payments

Examples of BABs

- Initially large governmental and State-university systems issued BABs
- More recently medium-sized localities with high credit ratings are taking advantage of BABs
- In October 2009, The Bond Buyer reported that approximately \$35 billion in BABs had been issued

Practical Issues

- Redemption Provisions – Do publicly-offered BABs need to be structured similar to “corporate bonds”?
- Short-Term and Medium-Term Maturities – Do BABs make economic sense?
- Disclosure Issues
- Opinions
- Multi-Purpose Issues

Recovery Zone Economic Development Bonds (“RZEDs”)

- RZEDs are a subset of “Direct Pay” BABs
- The amount of the refundable credit is 45% of the amount of interest payable on the interest payment date
- Must qualify as a BAB, plus meet the following:
 - 100% of available project proceeds (net of any amounts placed in a reasonably required reserve fund) must be used for qualified economic development purposes
- The issuer must irrevocably elect the refundable credit option

RZEDs (continued)

- Qualified purposes are described as “expenditures for purposes of promoting development or other economic activity in a recovery zone” and include capital expenditures paid or incurred with respect to property in the zone, expenditures for public infrastructure and construction of public facilities and expenditures for job training and educational programs
- A recovery zone is an area (i) designated by the issuer with significant poverty, unemployment, rate of home foreclosures or general distress, or as economically distressed by reason of the closure or realignment of a military installation pursuant to the Defense Base Closure and Realignment Act of 1990, or (ii) with an effective designation as an empowerment zone (under IRC § 1391 (b)(2)) or renewal community (under IRC § 1400E (a)(1))

RZEDs (continued)

- National allocation of \$10 billion apportioned among the states with each state receiving an amount of allocation determined according to a ratio of that state's 2008 employment losses to such losses for all states
- Virginia's total allocation is \$104,396,000
- Guidance provided by IRS Notice 2009-50
 - Apportioned the allocation within each state among counties and large municipalities according to a ratio of their employment losses versus the state's losses

- Governor's Executive Order Number 94 (9/3/09)
- Established process for localities to declare use of RZED allocation or waive allocation or have allocation "deemed waived"
- November 2, 2009 – first filing deadline
- December 15, 2009 – second filing deadline
- No later than March 15, 2010 – required issuance date
- Allocations actually waived or "deemed" waived will be available for re-allocation by the Commonwealth to other eligible projects

- Questions?
- For more information, contact:
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