

Re: Detailed Technical Comments on
Chairman's Tax-Exempt Bond
Proposal

The following are technical comments on the Chairman's Proposal relating to tax-exempt bonds:

1. Management Contracts (p. 186). The safe harbor should not permit the manager to be compensated exclusively on an incentive fee basis. This is especially important since there are many cases when a percentage of gross revenue (or profits) may be essentially the equivalent of a percentage of net profits.

2. Private Loan Bonds (p. 198). The exception for tax assessment bonds should be repealed because a bond to be repaid with tax assessments does not involve an indirect loan. A bond should never be considered nongovernmental merely because it is to be repaid by a nongovernmental person. When bond proceeds are used to finance property, a loan should not be deemed to arise unless the bond-financed property is at least "used" by a nongovernmental person.

3. General Taxing Powers (p. 188). The exceptions that apply to governmental units with general taxing powers should be revised to apply to general purpose governmental units. Many cities, counties, and towns have very limited taxing powers (e.g., the power to impose an ad valorem real property tax), which are no broader than the taxing powers possessed by single purpose districts. The exceptions should focus on whether a governmental unit performs many functions rather than on the breadth of its taxing powers.

4. In Progress Transition Rule (p. 189). The in progress transition rule should not require that the project be completed or that significant expenditures be incurred after 3/1/86. That requirement unnecessarily penalizes taxpayers who issue bonds later (rather than early). The transition rule should expressly be made inapplicable to refunding obligations and should require an inducement resolution (or other comparable preliminary approval) before 3/1/86. The 3/1/86 date should be 9/26/85 as in the House Bill; there is no reason to grandfather projects under a reliance theory where a binding contract or significant expenditures occurred after 9/26/85.

5. Treasury LMI Report (p. 190). The requirement of an annual Treasury Department report on compliance with the low or moderate income requirement should be deleted. The GAO recently completed a detailed report on residential rental project compliance and other matters.

6. Student Loan Bonds (p. 194). Present law requires that the issuer merely reasonably expect to use a major portion

of the proceeds to make or finance student loans. The issuer should be required to use all the proceeds for such purpose (as in the case of qualified mortgage bonds) or at least 95% (as in the case of other nongovernmental bonds). There is no need for any leeway here because there are no "bad" costs that need to be financed (shortfalls in revenues prior to making the loans are neutral costs) and a reasonable expectations standard is entirely inappropriate.

7. Mortgage Revenue Bonds (p. 195). The present law requirement of annual Treasury reports should be deleted. The so-called "policy statements" were intended for the purpose of determining whether additional targeting was desirable and whether the sunset should be extended or repealed. Assumptions of mortgages should be prohibited (the seller rather than the new borrower is the only one who benefits from the ability to assume).

8. Qualified Veterans' Mortgage Bonds (p. 196). Substantially all (90%) should be changed to 100% (or at least 95%). No leeway is necessary or appropriate here.

9. Qualified Redevelopment Bonds. Owner-occupied and multifamily housing that is actually rehabilitated with bond proceeds should be subject to the requirements applicable to mortgage revenue and multifamily housing bonds. Otherwise, bond proceeds might be used for luxury single and multifamily homes.

10. Maturity Limit (p. 200). Mortgage revenue bonds should be limited to 32 years and student loan bonds should be limited to 17 years.

11. Change in Use (p. 200). The "are to be" test should be clarified, a good faith rule should be added to avoid retroactive taxability, and the penalties should apply only while the noncompliance remains uncorrected. See Attachment A.

12. Volume Cap Transition Rule (p. 204). All bonds issued after the effective date should be subject to the volume cap. As in the case of the 1984 Act, issuers should be required to give in progress projects priority.

13. Arbitrage Restrictions (p. 205). The clarification of the reasonable expectations test should be effective for actions taken after the date of Senate Finance Committee action. See Attachment B. The validity of the 1978 sinking fund regulations should be expressly upheld. See Attachment C. The arbitrage rebate requirement should be revised. See Attachment D. The IDB 150% limitation should be repealed (or at least not extended to governmental bonds). See Attachment E.

14. Advance Refundings (p. 208). The flip-flop rule should not be implemented through the arbitrage rebate rules. Flip-flop benefits and other monetary benefits (apart from

interest rate savings) available solely by refunding should be eliminated at the outset (e.g., by prohibiting them or taking them into account in computing the escrow yield). An excess proceeds rule should be added. See Attachment F.

15. Information Reporting. Issuers of governmental bonds should be permitted to file a single, consolidated report for all issues with a face amount of \$100,000 or less. The Secretary should be permitted to extend the time to file unless the failure to timely file is willful (present law requires that good cause be established for the delay) and to impose a small monetary penalty as a condition of granting relief.

16. Federal Use and Security Interest Test. The federal government should not be a significant beneficiary of tax-exempt financing, because the revenue loss from the tax-exemption far exceeds the benefit. Under present law, there is no limit on federal involvement with exempt facilities financed by IDBs (except to the extent, if any, that such involvement may arise to a federal guarantee). An exempt facility IDB should not be tax-exempt if the federal government uses more than 10-25% of the exempt facility and is the source of more than 10-25% of the payment of debt service on the bonds.

17. Short-Term Obligations. Present law discourages issuers from issuing short-term obligations to take advantage of lower interest rates, because the requirements for tax-exemption must be re-applied every time the issuer rolls the short-term obligations over. This creates uncertainty and unnecessary administrative burdens. The Secretary should be authorized to treat obligations issued pursuant to a "program" (i.e., for a specified purpose, etc.) as a single issue (issued on the date of issue of the first obligation issued under the "program") for purposes of the requirements of section 103.