The Bond Lawyer

THE JOURNAL OF THE NATIONAL ASSOCIATION OF BOND LAWYERS // VOLUME 46 NUMBER 4 // FALL 2022

Contents

Because opinions with respect to the interpretation of state and federal laws relating to municipal obligations frequently differ, the National Association of Bond Lawyers ("NABL") has given the authors who contribute to *The Bond Lawyer*® and the editor the opportunity to express their individual legal interpretations, opinions, and positions. These interpretations, opinions, and positions, whether explicit or implicit, are not intended to reflect any position of NABL or of the law firms, branches of government, or organizations with which the authors and the editor are associated, unless they have been specifically adopted by such organizations. For educational purposes, the authors and editor may employ hyperbole or offer suggested interpretations for the purpose of stimulating discussion. While NABL subjects each of the articles which are contained herein to a review process, neither the authors, reviewers, and editor nor NABL take responsibility for the completeness or accuracy of the materials contained herein. Readers are encouraged to conduct independent research into the completeness and accuracy of the materials contained herein, including the original sources of authority. *The Bond Lawyer*® is not intended to provide legal advice or counsel as to any particular situation. Errors or omissions should be forwarded via e-mail to lwyman@nabl.org.

The Bond Lawyer®: The Journal of The National Association of Bond Lawyers is published four times a year, for distribution to members and affiliate members of the Association. Membership information may be obtained by writing to Linda H. Wyman, COO, National Association of Bond Lawyers, 601 Thirteenth Street, NW, Suite 800 South, Washington, DC 20005-3875; calling (202) 503-3300; emailing nabl@nabl.org; or at www.nabl.org.

Editor's Notes

Alexandra M. (Sandy) MacLennan, Squire Patton Boggs (US) LLP, Tampa, Florida

Welcome to the Fall 2022 Edition of *The Bond Lawyer*.

In this Edition

Tony Martini's column in this edition, provides a summary of the proposed SLGS regulations and takes a trip down memory lane with his thoughts on declarations of official intent. His thoughts on what lies ahead in 2023 a little nostalgic.

Drew Kintzinger reports on SEC enforcement activities in the last several weeks, including updates on enforcement matters relating to Rochester and Montebello School District, as well as the fiscal year-end SEC report on enforcement activities. Excerpts from the SEC Chair's recent remarks are a reminder for us of the SEC's views on "gatekeepers" in the securities markets.

What is "Indebtedness?" -- Accounting Treatment of Leases

In the past year or so, I have been spending a lot of time (too much) talking to clients about accounting changes in the treatment of leases and how that change in treatment flows through financial covenants in bond documents. There have been other accounting changes over the past several decades that have sent ripples through our market (e.g. pension and OPEB, in particular), but the change in the treatment of leases may have the most significant effect yet. Under the current (and relatively new) accounting treatment from both the Governmental Accounting Standards Board (GASB) and the Financial Accounting Standards Board (FASB), essentially all leases are required to be shown on the balance sheet as a liability with a corresponding "right of use"[1] asset. Particularly with respect to the GASB version, this change has the potential to result in compliance difficulties with respect to financial covenants, including debt service coverage ratio and capitalization requirements.

Under prior GASB and FASB treatment, leases were generally either operating leases or capital leases, which was straightforward enough. Operating leases were generally "off balance sheet" and not treated as indebtedness and capital leases were generally "on balance sheet" and treated as indebtedness. The rules that defined the two types of leases, while not without interesting nuances, were mostly predictable. Many (most) bond resolutions and indentures determine the inclusion of leases in the definition of "indebtedness" based upon whether a lease was a "capital lease" or "required to be capitalized" under generally accepted accounting principles. Then, the accounting changes were proposed, discussed, and eventually adopted with varying adoption and compliance dates.

The discussion regarding the accounting treatment of leases had been going on for years with both primary U.S. accounting standard setting organizations (the GASB for governments and the FASB for

[1] Referred to as "ROUs" but not to be confused with "ROUS" which are the famed "rodents of unusual size" seen in *The Princess Bride*.

non-governments[2]) re-examining their respective positions (which were, for the most part at that time, simpatico). Both GASB and FASB prior treatments were the "dual-approach" models, as described above. Some leases were in the nature of financing mechanisms (e.g. capital leases) and others were not. The GASB, however, decided that a single approach was the better model for comparability purposes. According to the GASB, all leases have a financing component and so all should be treated in the same manner for accounting purposes (except for some complicated and nuanced structures that the GASB decided to exclude, for now). From the GASB Statement No. 87 on Leases:

> In a lease transaction, a lessee receives the legal right to use an underlying asset (the asset that is subject to the lease, such as a vehicle or building) at the commencement of the lease term. In exchange, the lessee promises to make payments over time for the right to use that underlying asset. Therefore, the lessee has financed the acquisition of that legal right.[3]

The GASB acknowledged some comments received regarding the exposure draft of the lease statement asserted the elimination of the dual approach could result in some governments being out of compliance with financial covenants or statutory debt limits, but the GASB did not find that concern compelling and eliminated the distinction between operating and capital leases altogether. The FASB treatment, on the other hand, retained the distinction but changed the nomenclature (capital leases now being referred to as "finance leases"). While all leases are reported on the balance sheet under both GASB and FASB rules, the FASB retained the concept that payments under operating leases are expensed[4], while payments under finance leases are amortized with a portion of the lease payment attributed to principal and a portion to interest.

Taking these concepts back to the typical definition of "indebtedness" in bond documents, all leases are likely to be considered "indebtedness" because all leases are now on the balance sheet. However, depending on the definition of "debt service," under the FASB rule, it is likely only payments under finance leases would be included as only finance leases have a calculated amortization and interest component. Under the GASB rule, however, through the magic of accounting wizardry (and the concept of incremental borrowing cost), all leases will have amortization and interest components.

For some governments, particularly those who operate in corners of the financial markets shared with the private sector (e.g. publicly owned healthcare and higher educational entities, among others), the disparity between GASB and FASB lease treatments likely will lead to different accounting treatment for the same lease structure. Coverage ratios and capitalization requirements are part of the credit profile of the borrower and including traditional operating leases (e.g. what used to an operating lease under the prior GASB treatment) in financial calculations for governmental entities may skew the metrics and result in a diminished amount of comparability of financial statements across these markets.

The point I am trying to make, while likely misstating a lot about accounting rules, is that it may be time to revisit how our standard bond documents rely on GAAP and how the pertinent provisions might be affected by changes in GAAP over the life of the bond document (which, for master indentures could be 30 years or more). I have seen some proposed amendments to bond indentures purporting to "freeze"

---

[2] There is also the International Accounting Standards Board (IASB).
[3] See GASB Statement No. 87 on Leases, Appendix B.
[4] This is an over-simplified statement and probably not technically correct but used for illustration purposes.

GAAP to insulate against future accounting changes by providing the borrower the ability to opt in or out of new accounting rules, or providing that a failure to achieve specific financial targets as a result of accounting changes is not breach of the applicable covenant. Ideally, future bond documents would include specific provisions addressing the inclusion of leases in the definition of "indebtedness" that auditors could follow without requesting/requiring a legal interpretation. Borrowing a phrase from the Securities and Exchange Commission adopting release for the last amendments to Rule 15c2-12, perhaps leases should only be included in financial covenants if they are "debt, debt-like, or debt-related." But wait, that might require a legal interpretation.

Closing Thoughts

Our Tampa office moved earlier this year to an "open concept" floor plan. This required significant downsizing of all my "stuff," which necessitated sorting through decades of deal mementos and tchotchkes (or chotskies, if you prefer), some more memorable than others. There were lots of acrylic cubes with replica official statements inside, creative tributes with a water faucet or a lightbulb affixed (utility deals, obviously), a set of glasses with water pitcher (from one of only two deals I worked on that defaulted, knock on wood), a windbreaker jacket (with a Lehman Brothers logo), duffel bags of various sizes and with a variety of logos, a baseball bat (a Louisville Slugger), and a bamboo cane (yes, you read that correctly), to name just a few. But, for those who were in practice during the Bear Stearns heydays and remember, there are the stuffed plush bears, lots of bears. Some small, some large, and most dressed in vests with the deal description on the back. One is in a raincoat and hat. With no space in the new office to display these treasured reminders of the deals of yesteryears, they have all migrated to my house where most sit safely packed in boxes for the self-imposed required waiting period before they find a new permanent home in my local landfill, except for the baseball bat (which will be usefully positioned by my front door). And the bears….

Interested in hearing from others with ideas for the respectful disposition of tchotchkes. I am wondering if Weird Al Yankovich would buy any of these on eBay™.

And now, please enjoy the Fall 2022 edition of *The Bond Lawyer*. Best wishes to all for a happy holiday season and a prosperous New Year.

Federal Securities Law

Andrew R. Kintzinger
Hunton Andrews Kurth
Washington,DC

Since we convened at The Workshop in Chicago in October—an event well attended by SEC personnel as speakers and attendees—Commission enforcement activities affecting municipal securities continue to percolate.

Case Watch Follow-Ons

In ***SEC v. City of Rochester, New York, Rosalind Brooks-Harris, Capital Markets Advisors LLC, Richard Ganci, and Richard Tortora*** (previously summarized in the Spring 2022 issue of **The Bond Lawyer**), on November 14, 2022, the City and its Finance Director (Brooks-Harris) filed an answer to the SEC's complaint, providing a good example of countering Commission disclosure charges. The City and its Finance Director offered eleven affirmative defenses, seeking dismissal of charges because "the City and Brooks-Harris did not make any false statements or omissions and cannot be held responsible for false statements or omissions made by the [School] District or others." Defenses include that the alleged misstatements or omissions were not material; that there was no duty to disclose the information alleged to have been omitted; that the City and Finance Director did not act, or fail to act, with the required level of scienter; and that the City and Finance Director acted in good faith reliance on professionals. The answer provides a "real life" illustration of liability concepts we wrestle with at Fundamentals, the Institute and the Workshop: misstatements, omissions, duty to disclose, scienter, and reliance on professionals. In sum, a costly dispute of "facts and circumstances." The financial advisor and its principals offered its response previously.

In September 2019, the SEC issued a settlement order **In the Matter of *Montebello Unified School District and Anthony James Martinez*** and simultaneously filed a complaint in federal district court against the District's former Chief Business Officer in ***Securities and Exchange Commission v. Ruben James Rojas***. Both the settlement order and complaint allege violations of the federal antifraud provisions in the 2016 offer and sale of the District's bonds by failing to disclose fraud and internal controls concerns raised by the District's outside auditor, all as summarized in the Fall 2019 issue of **The Bond Lawyer**. On November 21, 2022, the SEC announced that Mr. Rojas had agreed to admit his conduct violated Section 17(a)(3) of the Securities Act and agreed to pay a $50,000 penalty to resolve the SEC Enforcement case. On November 18, the federal court entered an amended final judgement permanently enjoining Mr. Rojas from participating in municipal securities offerings. This final resolution of this enforcement proceeding illustrates the Commission's use of litigation, rather than administrative settlement, to pursue individual liability.

SEC Enforcement Results for FY 2022

On November 16, 2022, the SEC released its report on enforcement actions in fiscal year 2022. Emphasizing general themes of "robust enforcement," "penalties, undertakings and admissions" and "individual accountability", the Commission reported a 9% increase in enforcement actions over the prior year. The report mentions "leveraging the entire enforcement toolkit," including "use of data analytics." Touching on themes of interest to the municipal market, the SEC emphasizes that it continues to place "a high priority on pursuing issuers or their employees who make materially inaccurate disclosures, as well as auditors and their professionals who violate applicable laws and rules in connection with such disclosures." The SEC report highlights its enforcement "focus on gatekeepers" with specific mention of lawyers. And touching on current themes in the corporate market of analogous interest to the municipal market, the report includes mention of enforcement actions brought in the cybersecurity compliance area and in the ESG area.

The report devotes a distinct section to **Public Finance Abuse**, reprinted in full, below:

> *The SEC brought several important enforcement actions in the municipal bond sector in fiscal year 2022, including:*
>
> - *The SEC's first-ever charges in the municipal bond space against underwriters for allegedly failing to obtain required disclosures from investors when selling new issue municipal bonds.*
> - *The SEC's first action against a broker-dealer for violating a municipal advisor registration rule.*
> - *Charges against four investment advisers for violating the SEC's pay-to-play rule for investment advisers by continuing to receive investment advisory fees from government entities following campaign contributions made by associates to elected officials or candidates for elected office.*
> - *A case charging a Louisiana town, its mayor, and its unregistered muni advisor and its owner, alleging that they misled investors in the sale of $5.8 million in municipal bonds across two offerings in 2017 and 2018.*

In an Addendum to the report, the Division of Enforcement reports 20 enforcement actions from the Public Finance Abuse Unit in Fiscal Year 2022, involving 26 named parties. While this represents only 3% of total Enforcement Division actions for the fiscal year, it is almost double the number of enforcement actions and party counts brought by the Public Finance Abuse Unit in Fiscal Year 2021 (12 actions, 15 parties). In addition to the numbers, what stands out is the breadth of the Public Finance Abuse Unit's actions during Fiscal 2022: financial disclosure and issuer, issuer employee and outside auditor liability reported in the Crosby Independent School District enforcement case (not highlighted in the report excerpt above but summarized in the Winter 2022 issue of **The Bond Lawyer**), broker dealer conduct, municipal advisor roles and responsibilities and other municipal issuer and advisor conduct.

Enforcement Focus on Lawyers as Gatekeepers

On November 2, 2022, SEC Chair Gary Gensler gave remarks before PLI's 54th Annual Institute on Securities Regulation. Citing words of President Franklin Delano Roosevelt when the President signed the first of the federal securities laws ("This law and its effective administration are steps in a program to restore some old-fashioned standards of rectitude."), the title of Chair Gensler's speech was "This Law and Its Effective Administration." He went on to say that "effective administration" of SEC enforcement occurs through, among other themes, a focus on those in "positions of trust"—gatekeepers—including securities lawyers. The portion of the Chair's comments on lawyers as gatekeepers is reprinted below, worthy in its mention of the four public finance enforcement actions reported in the Summer, 2022 Issue of ***The Bond Lawyer*** regarding the limited offering exemption in Rule 15c2-12. Also noteworthy are his final words regarding lawyers advising clients that may be contemplating "a course of action that takes them up to the line":

Positions of Trust

Finally, to all the securities lawyers I am speaking to, you play an essential role to the clients that you counsel.

You also have a role as gatekeepers in upholding the law.
For instance, today's event takes place in the State of New York, where the state courts describe the role of attorney as a position of duty, trust, and authority, conferred by governmental authority for a public purpose.
We want you to succeed in meeting these standards of rectitude.
When lawyers—or other gatekeepers, like auditors and underwriters—breach their positions of trust and violate the securities laws, we will not hesitate to take action.

During the recent fiscal year, for example, we charged an attorney for his role in an unregistered, fraudulent securities offering, and we suspended him from practicing before the SEC as an attorney.

We also are litigating an action against an attorney for his alleged role in a would-be pump-and-dump scheme. In addition to other remedies, we seek an injunction to prohibit him from providing legal services regarding securities offers or sales.

In June, we charged Ernst & Young (EY) for cheating by its audit professionals on its ethics exams.

These are professionals whose job, amongst other important responsibilities, is to catch cheating by clients. Yet, these same professionals cheated on their ethics exams. Further, EY attorneys who were aware of the conduct failed to bring these problems to our attention despite direct requests.

What an egregious failure of the public trust. In charging EY, we imposed remedial actions and a $100 million penalty, the largest of its kind against auditors.

If issuers or registrants in our markets are relying upon them, it doesn't matter where the gatekeeper is located. This fall, we charged Deloitte-China, an audit firm who essentially asked companies to complete critical parts of their own audits, a plain violation of professional requirements. Deloitte-China abdicated their responsibility as a gatekeeper. Among other things, we imposed a $20 million penalty.

We also filed actions against four underwriters—Oppenheimer & Co., BNY Mellon, TD Securities, and Jefferies LLC—charging them with failing to meet disclosure requirements when offering municipal bonds. This, too, was the first action of its kind.

As I said last year, if your client is considering a course of action that takes them up to the line, keep them back from the line.

These are themes that repeat themselves every practice day for bond lawyers, underwriter's counsels and disclosure counsels as they exercise professional judgements on the "facts and circumstances" of material disclosure and on the many compliance issues posed by SEC Rule 15c2-12. The full text of Chair Gensler's remarks to PLI, with notes, can be found at https://www.sec.gov/news/speech/gensler-remarks-practising-law-institute-110222.

Happy Holidays to December readers and Best Wishes for the New Year to our January readers!

The Tax Microphone

Antonio D. Martini
Hinckley Allen
Boston, Massachusetts

Looking Back

We're fast approaching the end of 2022, the year in which we've seen the worm turn, or begin to turn, after years and years, even decades, of historically low interest rates. Of course, there's no way to tell if rates will stay high for an extended period of time, or whether we'll see them begin to drop as we turn the page and move on to 2023, but one could be forgiven for imagining that we could be entering a new market phase, in which the cost of funds will be notably higher for many issuers of municipal securities than it has been for some time. If that's so, then perhaps the phase we're currently in could be characterized as "transitional." And it seems to me that the municipal market has had certain earmarks of transition, and volatility, such as reduced volumes of new issuance and a sense in some quarters at least that borrowers are sitting out the market for a while, to see whether rates start to look like they will climb back down. In the meantime, here's hoping that NABL's membership finds ways to troubleshoot and problem-solve for its client base. I've been doing this work long enough to know that when market paradigms shift, and things begin to look out of balance (think 2008-2009), it can be a full employment act for solution-oriented practitioners like us.

One thing that looks like it isn't changing, alas, is that there continues to be a dearth of new, helpful and evolutionary guidance from policy- and rule-makers in the municipal market. Guidance is urgently needed on the bond and tax credit provisions of the Inflation Reduction Act that affect state and local governmental entities, for example. NABL's leadership has also been asking Treasury and the IRS to modify and finalize proposed regulations addressing whether and if tax-exempt and other tax-benefited debt instruments are treated as reissued for federal tax law purposes, and for supplemental guidance to simplify and expand the reach of the bond remedial action rules. Treasury told us in early November that it is working on some of these issues. Let's hope we see some tangible forward progress in 2023.

In the meantime, let's look at a couple of topics with some currency.

Proposed Revisions to the SLGS Regulations

On September 30, 2022, the Bureau of the Fiscal Service within the Treasury Department published a Notice of Proposed Rulemaking (Docket ID No. FISCAL-2022-0002, 87 Fed. Reg. 59353) to amend the regulations that govern the Bureau's State and Local Government Series (SLGS) offering of securities. You can find a print of the Bureau's September 2022 NPRM at https://www.federalregister.gov/documents/2022/09/30/2022-21173/us-treasury-securities-state-and-local-government-series.

As readers of this column will know, SLGS are a type of non-marketable United States Treasury security that can be purchased by or on behalf of state and local governmental entities, generally to facilitate compliance with the arbitrage yield restrictions and rebate requirements that arise in connection with their tax-exempt bond borrowings. The SLGS regulations, which have been in place for years, have been amended from time to time, most recently in 2012 and back in 2004-2005. And, going as far back as 2004-2005 (see the preamble to the 2005 final SLGS rulemaking at 70 Fed. Ref. 37904), an articulated concern of SLGS rulemakers has been to ensure that the "flexibilities" afforded to bond issuers, in terms of the timing of subscriptions for the purchase of SLGS securities and the amounts specified in those subscriptions, do not create what are viewed by the regulators as "impermissible cost-free options" in the hands of bond issuers. An example of this, prohibited under the current SLGS rules, would be the unconstrained making and cancellation of SLGS subscriptions, prior to SLGS purchase, as available interest rates on SLGS move in and out of favor relative to the subscribing bond issuer, in particular relative to the yields available at the same time to the issuer on comparable open-market Treasury securities. The September 2022 NPRM appears to be focused largely on implementing additional guardrails to trammel the opportunity for bond issuers to use the SLGS program to engage in optionality gamesmanship.

Without going into great detail, the September 2022 NPRM identifies and seeks to address three categories of cost-free option-capturing behavior: (1) purchasing a long-term SLGS security and redeeming the security before maturity to capture redemption premium; (2) establishing or changing the maturity and associated interest rate on SLGS securities already subscribed for to take advantage of interest rate movements, either to capture redemption premiums or to minimize losses; and (3) establishing or changing the SLGS subscription amount in order to maximize redemption premiums or minimize potential losses. The Bureau of the Fiscal Service suggests in the September 2022 NPRM that it has detected SLGS transactional behavior on SLGSafe, the internet site on which SLGS acquisitions and dispositions are transacted, that warrants additional rulemaking.

The Bureau of the Fiscal Service proposes a raft of changes to the SLGS rules to counteract these identified behaviors. I won't enumerate them here; you can review the proposal in the Federal Register. Instead, I will only highlight a very few of these proposed changes. Among other things, the September 2022 NPRM would reduce the lead time for the submission of a SLGS subscription from a maximum of 60 days, as permitted under the current SLGS regulations, to 45 days; it would also require that identifying information about the bond issue to which the SLGS subscription relates conform to the issue description conventions used on the Electronic Municipal Marketplace Access (EMMA) platform of the Municipal Securities Rulemaking Board, to the extent information about the bond issue is reported on EMMA. The September 2022 NPRM would also impose new bond/SLGS duration and eligibility certification requirements and may in some cases oblige bond issuers to definitively "lock in" SLGS principal amounts sooner than currently required, potentially creating access for issuers who have not fully worked out their financing plans (other than knowing they'll need to purchase SLGS come hell or high water).

The good news is that NABL's Tax Law Committee, under Brian Teaff's leadership, has prepared comments and recommendations on the September 2022 NPRM, which were submitted to the Bureau of the Fiscal Service on November 29. You'll find a copy of the NABL submission on the NABL website here. Stay tuned for further developments on the SLGS regulatory front; if and when the new rules are finalized, I would anticipate a detailed summary of the particulars will be catalogued in this column.

A Brief Note on Declarations of Official Intent

This next segment isn't about a legal development in any formal sense. It's not about a new statutory enactment or new regulatory guidance or any interpretive release. Instead, it's a brief commentary in response to anyone out there in the world who may be wondering to himself or herself right now, out loud or under their breath, whether under Treasury Regulations Section 1.150-2, an expression of "official intent" must include the words "to reimburse" or perhaps some other equivalent phrasing to convey the idea of reimbursement by name.

A declaration of "official intent", of course, generally serves as a linchpin to the use of the proceeds of a tax-exempt bond issue to reimburse oneself for otherwise financeable out-of-pocket expenditures that were made prior to bond issuance. But it is clear beyond peradventure that under Treasury Regulations Section 1.150-2, an official intent <u>need not</u> include any talismanic or formalistic phrasing or incantations, such as "to reimburse" or otherwise, to serve as the basis for a reimbursement allocation of bond proceeds.

Here's the full text of Treasury Regulations Section 1.150-2(e), which specifies what an "official intent" is for purposes of the tax-exempt bond reimbursement rules:

> *(e)* ***Official intent rules****. An official intent satisfies this paragraph (e) if:*
>
> > *(1)* ***Form of official intent****. The official intent is made in any reasonable form, including issuer resolution, action by an appropriate representative of the issuer (e.g., a person authorized or designated to declare official intent on behalf of the issuer), or specific legislative authorization for the issuance of obligations for a particular project.*
> >
> > *(2)* ***Project description in official intent*** *-*
> >
> > > *(i)* ***In general****. The official intent generally describes the project for which the original expenditure is paid and states the maximum principal amount of obligations expected to be issued for the project. A project includes any property, project, or program (e.g., highway capital improvement program, hospital equipment acquisition, or school building renovation).*
> > >
> > > *(ii)* ***Fund accounting****. A project description is sufficient if it identifies, by name and functional purpose, the fund or account from which the original expenditure is paid (e.g., parks and recreation fund - recreational facility capital improvement program).*
> > >
> > > *(iii)* ***Reasonable deviations in project description****. Deviations between a project described in an official intent and the actual project financed with reimbursement bonds do not invalidate the official intent to the extent that the actual project is reasonably related in function to the described project. For example, hospital equipment is a reasonable deviation from hospital building improvements. In contrast, a city office building rehabilitation is not a reasonable deviation from highway improvements.*

> *(3)* ***Reasonableness of official intent****. On the date of the declaration, the issuer must have a reasonable expectation (as defined in § 1.148-1(b)) that it will reimburse the original expenditure with proceeds of an obligation. Official intents declared as a matter of course or in amounts substantially in excess of the amounts expected to be necessary for the project (e.g., blanket declarations) are not reasonable. Similarly, a pattern of failure to reimburse actual original expenditures covered by official intents (other than in extraordinary circumstances) is evidence of unreasonableness. An official intent declared pursuant to a specific legislative authorization is rebuttably presumed to satisfy this paragraph (e)(3).*

Let's boil this down, for the removal of doubt. Under these rules, as written, an "official intent" flies for reimbursement purposes if (1) it's in any reasonable form, (2) it fairly describes the project with respect to which expenditures will be made (and with respect to which reimbursement allocations from bond proceeds will eventually be sought), (3) it specifies the maximum par amount of bonds expected to be issued for the project and (4) at the time it's adopted, the issuer has a reasonable expectation that it will reimburse the aforementioned expenditures from the proceeds of a borrowing. That is all there is to an official action. Nowhere in Treasury Regulations Section 1.150-2(e) does it say that the words "to reimburse" must appear in an official action, nor is this even remotely implied. In fact, the closest approach to the notion in this regulatory text is in Treasury Regulations Section 1.150-2(e)(3), where it provides that at the time of adoption of an official intent, the issuer must have in mind <u>an expectation</u> that it will reimburse an out-of-pocket project expenditure in the fullness of time from bond proceeds. But an expectation generally is descriptive of an idea, a mental state—and nowhere, but nowhere, is it required in the reimbursement regulations that this idea or expectation must be written down anywhere, let alone using the words "to reimburse."

This actually makes a lot of sense, when you pause to think about it. We bond practitioners know that declarations of "official intent" come in all shapes and sizes, and that our issuer clients have countless internal processes, all different and fairly idiosyncratic, for adopting and memorializing these declarations. Often, we thread them together from disparate contemporaneous expressions that are made "on the record" by issuer staff, and these declarations are often made many months or even years before a bond issue coalesces. The key is to look for the ingredients of an official action holistically—a project description, and intention to borrow, a statement of a not-to-exceed amount for the borrowing.

The drafters of these reimbursement regulations back in 1993 (the late Eliot Stern?) were wise to craft a substantive rule defining "official actions" that afforded issuers a good deal of flexibility. Perhaps they were reacting to the generally more rigid and formalistic requirements of the 1970s-vintage "official action" requirements of Treasury Regulations Section 1.103-8(a)(5), which were essentially subsumed in the Section 1.150-2 reimbursement rules when they came along in the early 1990s. I also recall that the immediate predecessor to the current provision, in a now-withdrawn Treasury Regulations Section 1.103-18, which was in place from March 1992 until June 1993, also left a lot to be desired in terms of flexibility. In fact, old Treasury Regulations Section 1.103-18 may be the cincher in this discussion. That regulation required among other things that an "official intent" specifically state that it is a declaration of official intent under Treasury Regulations Section 1.103-18. This isn't exactly the same as a requirement that the magic words "to reimburse" be used in a declaration of official intent, but it was pretty wooden, and the requirement clearly created a trap for unsuspecting issuers. And, clearly, it was jettisoned with the promulgation of the current reimbursement rules in 1993 for that very reason.

Last point and then I'll stop. When the drafters of Treasury Regulations Section 1.150-2(e) thought it important to mandate a specific, formal element that must appear in an official intent (i.e., the maximum principal amount of obligations expected to be issued for the project), they knew how to say so. But they obviously stopped short of requiring any official intent to use the words "to reimburse." End of story.

Looking Forward

And so we look forward, through the end of 2022 and into 2023. As I write this column, Congress has about a week to act to provide funding for the federal government for fiscal year 2023 and to avoid a shutdown. Moreover, before the end of the current session of Congress, on or about January 2, 2023, legislation must be passed to waive the application of the provisions of the Pay as You Go Act of 2010 to the legislative expenditures that have been enacted over the last two sessions of Congress (including in the "hard infrastructure" spending package signed into law last year as the American Rescue Plan of 2021). Otherwise, it appears that the PAYGO rules will significantly constrain increases in federal spending or reduce other federal expenditures (or both), including by sequestration of federal outlays like direct-pay subsidies on tax-benefited instruments such as build America bonds (BABs) and other qualified tax credit bonds. Reports have suggested that, absent a PAYGO waiver in the current Congress, BABs subsidies could be automatically zeroed out, quite literally, in 2023 and beyond—see, for example, the GFOA-led June 21, 2022 coalition letter to policymakers here: https://www.gfoa.org/materials/gfoa-leads-coalition-letter-on-sequestration-and-direct-subsidy-bonds).

Further out, we can foresee that the stepped-up IRS funding provisions of the Inflation Reduction Act of 2022 will eventuate in increased staffing and resources for its Tax Exempt Bonds group (IRS-TEB). It will take time for those resources to be put in place, and for new staff to be trained and to get up and running, but all of this may imply more audit activity on the part of the IRS on the near- to middle-term horizon. Time will tell.

Finally, if the worm is really turning, as I suggested it may be at the top of this column, and if borrowing rates really are on a sustained uptick, it may be a good time for all of us at the end of 2022 to brush off our copies of the late Rick Ballard's chestnut, *The ABCs of Arbitrage*. Perhaps our issuer clients will be seeing their first meaningful opportunity in many years to earn a rate of return on project fund investments that is greater than virtually nothing. And perhaps they will benefit from the assistance of NABL members and manage to retain some of those earnings with some old-fashioned arbitrage rebate planning and housekeeping, the way issuers used to all those years ago.

My best wishes to you for a happy and prosperous New Year.