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Editor's Notes

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

In this Edition

A very warm welcome to Andrew R. Kintzinger of Hunton Andrews Kurth as our new columnist on federal securities matters. Drew is a familiar face and voice on securities law matters relating to municipal finance. He served on the NABL Board of Directors 1990-1996 and as NABL President in 1994, as well as participating on numerous projects and panels over the years. He is a Founding Fellow and current Director of the American College of Bond Counsel and also an Adjunct Professor of Law at Georgetown University Law Center, teaching Public Finance: Tax and Securities Aspects. In his inaugural column, in addition to summarizing the recent flurry of SEC enforcement activity, Drew delves into the current issues regarding the SEC's administrative proceeding process in the run up to constitutional challenges to that process being argued before the U.S. Supreme Court. It is an interesting piece that puts the results of some historical enforcement actions into perspective. Welcome Drew!

Tony Martini's column in this edition includes a heartfelt remembrance of the late Perry Israel who passed away unexpectedly in August 2022. In addition to being a remarkable human being personally, he made countless valuable contributions to the municipal market generally and to NABL, in particular. Tony also reviews the Inflation Reduction Act of 2022 and the resulting flurry of activity around tax matters disclosure.

Depending on the Facts and Circumstances

One aspect of the SEC approach to municipal issuers that continues to be of concern to me is the repeated mantra that "depending on the facts and circumstances," information that "becomes public" and "reasonably expected to reach the market" is covered by the antifraud provisions. What do those phrases actually mean in the municipal securities context?

Private companies (even those that are public reporting companies) have ostensible control over the flow of information to the public. Municipal entities, on the other hand, are invariably subject to state "sunshine laws" governing government meetings and public records. Florida, for example, has one of the most strict public records laws in the country. Every scrap of paper, document, report, complaint, email/text message, meeting agendas (minutes and back-up), etc., absent a statutory exception, is required to be open for public inspection. This includes draft documents sent to municipal entity representatives in a bond working group, and, in many cases, draft documents submitted for board approval in a meeting agenda package. No reason need be given for a public records request in Florida. Arguably, one doesn't even have to identify herself in order to obtain public records in Florida. Additionally, many governmental entities in Florida routinely post meeting agendas in advance of public meetings. This typically includes the documents to be approved (e.g. draft bond documents, including draft disclosure documents and, potentially, draft feasibility reports). Municipal issuer's websites are freely accessible to the general public and serve as a source of information for a variety of audiences, including, in particular, residents, visitors and businesses.

In the municipal world, the vast majority of information about governmental issuers does not "become" public. Once a record is received or generated by the municipal entity it is presumed to be public, unless an exception applies. And the exceptions in Florida are fairly narrow.

In Paul Maco's final column in *The Bond Lawyer*[1], specific reference to Part IV of the Staff Legal Bulletin No. 21 [2] was made that provides examples of statements covered by the antifraud provisions, including paragraph C, Public Reports Delivered to other Governmental or Institutional Bodies, which states:

> Though the Commission has not specifically identified other types of reports which, once public, would be subject to the antifraud provisions, the staff believes that additional types of reports could be covered by the antifraud provisions *depending on the facts and circumstances.* [emphasis added] In the staff's view, additional types of reports that could, depending on the facts and circumstances, be included in this category may include (but may not be limited to) reports submitted by a municipality to a state agency, reports made by a state or local official to a legislative body (such as a state legislature or city council), *and other reports made part of a public record and available to the public* [emphasis added].

Relying on vague references to "depending on the facts and circumstances" when referencing public information in the municipal context, while consistent with the SEC's historical approach, is not helpful guidance to municipal issuers trying to manage potential securities liability. In the Harrisburg proceeding[3], one could have come away with the idea that it was only because the city had not been current with EMMA filings that investors had no alternative but to seek out information from other sources.[4] That was a somewhat understandable, if not logical, position at the time; however, this is clearly not the SEC's view.

The Staff Bulletin includes advice for municipal issuers to look to the SEC's guidance to corporate entities to see how they could manage their flow of information. The Staff Report also mentions the 1994 Interpretive Release[5] as a foundation for some of its analysis. A lot has changed in the nearly three decades since the release was published, particularly with respect to technological advances and public access to information via the internet and social media. Now would be a great time to update the 1994 Interpretive Release to address these technological changes and provide additional useful guidance and clarity regarding the responsibilities of both municipal issuers and investors in light of these changes.

[1] *The Bond Lawyer®*, The Journal of the National Association of Bond Lawyers; Volume 46, Number 2; available (to NABL Members) at https://www.nabl.org/Newsroom/e-Publications/The-Bond-Lawyer-Members-Only/the-bond-lawyer-spring-2022.

[2] Application of Antifraud Provisions to Public Statements of Issuers and Obligated Persons of Municipal Securities in the Secondary Market: Staff Legal Bulletin No. 21 (OMS), available at: https://www.sec.gov/municipal/application-antifraud-provisions-staff-legal-bulletin-21.

[3] In the Matter of the City of Harrisburg, Pennsylvania, Securities Exchange Act Release No. 69515, A.P. File No. 3-15316 (May 6, 2013).

[4] Id.

[5] Release No. 33-7049; 34-33741; Statement of the Commission Regarding Disclosure Obligations of Municipal Securities Issuers and Others; available at: https://www.sec.gov/rules/interp/1994/33-7049.pdf.

More helpful and practical guidance specific to the municipal market would be greatly appreciated along the following lines:

1. Issue guidance that disclaimers/terms of use on a municipal issuer's website or in documents can be effective to establish the circumstances under which information is provided (although it will not provide insulation from intentional fraud). If a municipal issuer has a multi-purpose website (e.g. information for residents, visitors, and businesses, as well as investors), it should be acceptable to cordon off information that is intended for investors, including information that has been vetted by appropriate staff and, where needed, legal counsel. A clear statement to investors that they should NOT rely on information elsewhere on the municipal issuer website with respect to an investment decision should be a sufficient fact and circumstance to protect municipal issuers from inadvertent consumption by an investor of inconsistent information. Investors should be held accountable to reasonably assess the reliability of the information they may obtain indirectly about a municipal issuer and the SEC should confirm this would be a "fact" or "circumstance" that is taken into account.

2. In the municipal context, the "total mix of information" should not include <u>all</u> public information of the municipal issuer (because that information is infinite), but rather the information a reasonable investor has access to in its capacity as an investor and not merely as an inquisitive member of the general public. Perhaps something like the total *weighted* mix of information would be appropriate, with information that is clearly intended for investors (EMMA or investor section of a website) is given significantly more weight in the analysis and information that is clearly not intended for investors is given no weight.

3. Absent actual fraud, the intent of the municipal issuer should be a material, if not defining, factor in determining whether information can be reasonably expected to reach the market. Additionally, express terms of use and cautionary language on a website or elsewhere should also be dispositive of the intent of the municipal issuer and the reliability of the information for investor purposes.

The SEC is undoubtedly (and understandably) resistant to disparate treatment of private entities and municipal entities but, *under the facts and circumstances*, the SEC should consider it.

Closing Thoughts

In addition to losing Perry Israel in August, my mother passed away August 12, 2022, three days after her 103rd birthday. Virginia Marie Madison MacLennan was a force in the universe, or at least my universe, and the universe of most people she met. She was a woman born into one era but part of the foundation of a new era. When she was born, the Spanish Flu Pandemic was still ongoing and women did not have the constitutional right to vote. She was born and raised in San Francisco by her maternal grandmother and maiden aunt after the untimely passing of her mother. She was the descendant of pioneer families in California (Lawler, Rogers and Dunn) and Washington (Madison). She was smart, creative, determined, and adventurous. She was the mother of three daughters in whom she instilled the power and confidence for each of us, in our own way, to be a fierce independent woman. In her heyday, you would likely not see her in public without at least lipstick, and likely high heels; although there was that period when she discovered Birkenstocks (a blip on the timeline). Truth be told, she was the strongest woman I have ever known. She faced and overcame many challenges in her life with grace and quiet strength and taught me to do the same (with varying success). Be adventurous in your life and inspiring and kind to others as she was in her life.

Federal Securities Law

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After a flurry of SEC enforcement actions filed in June in federal courts (Sterlington, Louisiana; City of Rochester; Anthony Michael Holland), discussed in the Spring 2022 edition of this publication, the summer months were relatively quiet from the Enforcement Division's Public Finance Abuse Unit. However, while recent enforcement cases have focused on issuer financial disclosures, September brought renewed vigor from SEC Enforcement regarding municipal underwriter practices. In addition, a Fall preview offers much to watch from SEC Enforcement, from the courts, from the SEC's Office of Municipal Securities, and from the MSRB.

Enforcement—Municipal Underwriters and the Limited Offering Exemption

On September 13, 2022, the SEC announced three administrative settlements and filed one litigation action against underwriters for allegedly failing to satisfy the criteria in the limited offering exemption in Rule 15c2-12.

The limited offering exemption contained in Rule 15c2-12 for offerings placed with a small number of sophisticated investors with investment intent (as distinguished from distribution intent) has sometimes been a challenge for practitioners to "perfect" with their issuer, underwriter, remarketing agent and purchaser clients. The exemption requires an underwriter in a limited offering (minimum denominations of $100,000 and sold to no more than 35 persons) to have a reasonable belief that each purchaser (1) has such knowledge and experience in financial and business matters that it is capable of evaluating the merits and risks of the investment and (2) is not purchasing the securities for more than one account or with a view to distributing the securities.

In separate administrative settlements with TD Securities (USA) LLC, BNY Mellon Capital Markets LLC and Jefferies LLC, the SEC maintained that each underwriter "sold securities to broker-dealers and certain investment advisors without a reasonable belief that the broker-dealers and investment advisors were purchasing the securities for investment . . . [and] [m]oreover . . . lacked policies and procedures designed to ensure that purchasers satisfied the exemption's requirements." Each administrative order states that:

> As a result, [the underwriter] violated Exchange Act Rule 15c2-12 as well as MSRB Rule G-27, which requires municipal underwriters to adopt, maintain and enforce written supervisory procedures reasonably designed to ensure compliance with Rule 15c2-12 . . . and also violated Section 15B(c)(1) of the Exchange Act for failing to comply with the MSRB rule.

These are essentially companion, near identical, orders in wording—perhaps a "model" for future settlement orders to come, as discussed below.

The SEC premised these enforcement actions on the 1989 Adopting Release for final Rule 15c2-12, as amended by the 1994 continuing disclosure provisions of the Rule and its expressed concern about the parameters of the limited offering exemption:

> The Commission was concerned that any securities offered pursuant to a limited offering exemption could immediately be resold to public investors without the benefit

> of the Rule's requirements, including the undertaking by issuers to provide investors with continuing disclosure about their investments. For these reasons, the Commission required that the securities be issued in relatively large denominations, $100,000 or more, and that the underwriter have a reasonably belief that the securities are being acquired by the purchasers for investment. The Rule also requires underwriters to determine if each investor is purchasing the securities for one account in order to preserve the integrity of the limitation on sales to no more than thirty-five persons. Moreover, the persons that purchase the securities must possess the necessary knowledge and experience to evaluate the merits and risks of the investment. The Rule does not identify purchasers presumed to meet these criteria. Instead, the Rule requires that underwriters make a subjective determination that investors meet the purchaser qualifications.

Each administrative order maintains that, across multiple limited offerings by each underwriter, the underwriter "did not inquire, or otherwise determine, if broker-dealers and investment advisors were purchasing the securities for more than one account or for distribution . . . [and] also failed to ascertain for whom the broker-dealers and investment advisers were purchasing the securities." Consequently, the underwriter "therefore was unable to form a reasonable belief that the broker-dealers and investment advisors were purchasing the securities for investors who possessed the necessary knowledge and experience to evaluate the investments. As a result, [the] limited offerings did not qualify for the exemption".

The SEC additionally maintained that each underwriter failed to adopt policies and procedures reasonably designed to ensure compliance with the limited offering exemption, as required by MSRB Rule G-27 and, as a result of not complying with and MSRB Rule, also violated Section 15B(c)(1) of the Exchange Act which requires underwriters to comply with MSRB Rules.

These administrative orders (a) included a no admit/no deny provision by the underwriters as to the findings, and (b) specifically took into account remedial actions taken by each underwriter. The SEC ordered disgorgement of each underwriter's earnings realized in the limited offerings; ordered a cease and desist from future violations of Rule 15c2-12, MSRB Rule G-27 and Exchange Act provisions; formally censured each underwriter; and imposed civil money penalties on each underwriter (amounts ranging from $100,000 to $300,000 depending on volume of alleged violative limited offerings).

On the same date, SEC Enforcement commenced a litigation proceeding, SEC vs. Oppenheimer & Co., Inc., alleging similar violations against an underwriter for failure to meet the legal requirements of the limited offering exemption. Why a litigation proceeding rather than an administrative proceeding? One can only glean from the SEC's allegations that (a) the volume of limited offerings during the relevant time period (2017 to present) was significantly higher; (b) according to the SEC's complaint, the underwriter "made deceptive statements to municipal securities issuers by representing that it would and did comply with the limited offering exemption ("[the underwriter] was negligent in making these statements because its regular practice was to not obtain the information necessary to know whether its sales of municipal securities would or did meet the Limited Offering Exemption requirements"); and (c) according to the SEC, the underwriter continues in its limited offerings practices, failing to implement policies and procedures to comply with the limited offering exemption. However, to every Complaint, there is an Answer, and this is likely a contested matter in which the actual facts, and application of legal principles, remain in dispute.

In its Litigation Release announcing the charges against the four underwriters in the above three administrative and one litigation proceeding, SEC Enforcement concluded:

> ***As a result of its findings in these investigations, the SEC staff has begun investigations of other firms' reliance on the limited offering exemption. Firms that believe their practices do not comply with the securities laws are encouraged to contact the SEC at LimitedOfferingExemption@sec.gov.***

Reminiscent of the MCDC Initiative, SEC Enforcement is sending a clear message: the administrative orders described above are "model settlements" for underwriters that are addressing compliance with the limited offering exemption with policies and procedures, and beware the potential litigation action for those that cannot demonstrate remedial steps. These are important enforcement developments to be monitored.

Enforcement—Underwriter and Municipal Advisor Registration

In the same September week, on September 14, 2022, the SEC announced a settled administrative order with broker-dealer Loop Capital Markets, LLC. In this order, that SEC alleged that the broker-dealer provided advice to a municipal entity regarding the investment of municipal securities proceeds while not registered as a municipal advisor. The SEC maintained that the broker-dealer violated the Exchange Act in failing to register as a municipal advisor, and violated MSRB Rule G-27 for failure to maintain an appropriate supervisory system. The broker-dealer did not admit or deny the findings, and the SEC noted that the broker-dealer implemented remedial actions promptly. Remedies included censure, cease and desist, disgorgement of earnings from the investment activity and a $100,000 civil penalty. This action is noted as the first time the SEC has brought civil claims against a broker-dealer for allegedly violating the municipal advisor registration rule. As promised, the Public Finance Abuse Unit continues to focus on potential advisory activities by municipal market participants and the fine-tuned analysis of the need to register as a municipal advisor.

Enforcement—Case Watch

SEC investigations of municipal market participants can often span months to multiyear, intense, and costly document production and fact development through testimony. Often in this process, issuers, underwriters or other respondents decide to settle allegations in an administrative order negotiated with SEC Enforcement staff. However, there are instances when the respondent or target decides that settlement is not a viable option. Instead of initiating an action in federal court, SEC Staff can commence a litigated administrative proceeding before an administrative law judge ("ALJ") to resolve case disagreements. The ALJ effectively acts as judge and jury. Appeal of ALJ rulings are made to the five SEC Commissioners which may give the matter *de novo* review. Only after decision by the Commissioners does a respondent have the ability to seek Federal court review to the US Court of Appeals—DC Circuit. And, on appellate review of an SEC decision, the standard of review—whether there is substantial evidence to support the SEC's decision—is viewed on the "deference spectrum" as favorable to affirming the Commission's decision. Respondents who are challenging nuanced matters of fact and law, particularly in the municipal securities space, express legitimate concern that SEC Staff has many advantages in navigating a litigated administrative proceeding. The respondent misses the safeguards of a federal court proceeding, including the right to jury trial.

In 2018, the US Supreme Court, in ***Lucia v. SEC***, held the SEC's Staff appointments of ALJs unconstitutional. Many securities litigators, in the lead-up to that decision, observed that SEC Staff was increasingly reluctant to use the litigated administrative proceeding due to the risk of constitutional challenges. Consequently, including in the municipal securities enforcement area, we have seen settlement orders or, as highlighted in *The Bond Lawyer* Spring Edition, more aggressive enforcement actions initiated in Federal Court.

Indeed, challenges to the SEC's use of the litigated administrative proceeding continue. In May of this year, the US Supreme Court granted certiorari in ***SEC v. Cochran*** to decide if a defendant in an administrative proceeding can go directly to Federal district court to challenge the SEC's adjudication as unconstitutional, or whether the defendant must proceed through a full administrative hearing with the ALJ, appeal the ALJ's decision to the full Commission and only then appeal the Commission's final decision to the US Court of Appeals. There is a circuit split on this issue. The US Supreme Court will consider this case in its upcoming October term.

Also in May of this year, the 5th Circuit Court of Appeals in ***Jarkesy v. SEC***, held, among other issues, that the SEC's "in-house adjudication" of alleged securities law violations by an SEC ALJ violated a defendant's Seventh Amendment right to a jury trial. On July 1, 2022, the SEC filed a petition with the 5th Circuit Court of Appeals for a rehearing *en banc*. The SEC could also consider seeking US Supreme Court review of this issue, depending on the outcome in the 5th circuit. Our colleagues in the corporate and securities litigation practices have written extensively on both cases. These case law developments on the use of ALJ administrative proceedings have special meaning for municipal bond market participants who find themselves respondents in SEC investigations and Enforcement actions.

Two "teaching cases" on the antifraud provisions and materiality in municipal bond offerings offer special insights on the real impact litigated administrative proceedings may have on final outcomes. ***Dolphin and Bradbury, Inc. and Robert J. Bradbury v. SEC*** is a material omissions case regarding risk and projections disclosures about the duration of office lease rentals necessary to pay debt service on bonds. The key focus in this proceeding was the conduct of the underwriter. The ALJ found that the underwriter violated various antifraud provisions, and on appeal to the Commissioners, the Commission affirmed the ALJ. The underwriter, Bradbury, appealed the Commission finding that he acted with scienter to the US Circuit Court of Appeals for the DC Circuit. The case is perhaps best known for its colorful statement of scienter and materiality for Rule 10b-5 purposes:

> Bradbury in effect asks us to apply the scienter standard in a way that would protect someone who warns his hiking companion to walk slowly because there might be a ditch ahead when he knows with near certainty that the Grand Canyon is one foot away.

The Court of Appeals, in its decision, noted that "[t]he Commission's finding that Bradbury acted with scienter is conclusive if, under our 'very deferential' substantial evidence standard . . ., 'a reasonable mind might accept [the] evidentiary record as adequate to support [the Commission's] conclusion' . . . ." But in upholding the Commission's finding that Bradbury acted with scienter, note the Court's statement that "[w]ere we writing on a blank slate, this would be a very close case, because the scienter threshold is high. But we need not decide how to sketch the contours of extreme recklessness on a blank slate, because Congress has directed us to uphold the Commission's factual findings if supported by substantial evidence."

Another litigated administrative proceeding that proceeded to appellate court review is known well to many municipal securities practitioners, ***Weiss v. SEC***. This case involved alleged securities law violations arising from bond counsel's unqualified opinion issued in connection with a school district' bond offering. The original action was brought before an ALJ who decided that bond lawyer Weiss did *not* violate Section 17(a) of the Securities Act, Section 10(b) of the Securities Exchange Act or Rule 10b-5. The Initial Decision of the ALJ dismissed all charges against Weiss. SEC Enforcement appealed to the Commission, who found that Weiss was "at least negligent" and had violated Sections 17(a)(2) and (3) of the Securities Act, which do not require proof of intent. Weiss appealed to the DC Circuit Court of Appeals, which upheld the Commission on the deferential "substantial evidence" review standard referenced in *Bradbury*.

So the current case challenges to ALJ administrative proceedings resonate directly with underwriters, bond counsel and other municipal market participants, including issuers and municipal advisors. Nonetheless, the Enforcement Division's Public Finance Abuse Unit has recently demonstrated depth and nimbleness in navigating between administrative settlements and initiating Enforcement cases in Federal court, apparently not missing the ALJ litigated administrative hearing in recent fraud actions. Under Chairman Gensler and current Enforcement priorities, expect tough cases to play out in Federal court, not through the ALJ option.

What's Ahead from OMS? The Materiality "Northstar"

In 2020, the SEC's Office of Municipal Securities offered interpretive guidance to issuers and counsel on antifraud provisions, materiality and forward looking disclosures in a February 7, 2020 Staff Legal Bulletin on Municipal Bond Continuing Disclosure and in a May 4, 2020 Statement to Municipal Issuers on Covid Disclosures. It appears that the theme in these guidance pieces continues post-pandemic.

New Director of the SEC's Office of Municipal Securities, Dave Sanchez, commenced his speaking outreach at municipal industry conferences in late spring and early summer, and in reported comments continued to emphasize the materiality analysis theme. Particularly in the context of the SEC's climate risk disclosure rule proposal for registered, reporting companies, and acknowledging the currency of ESG disclosure topics for municipal issuers, his reported comments at the GFOA Annual Conference in May suggested a "stick to the principles" approach, reminding that traditional disclosure rules have not changed but are being applied to different topics, such as climate risk disclosure, general climate or "green" disclosures, and revisiting earlier Covid projections disclosures in new primary offerings. Consistency with the 2020 guidance pieces appears to be the theme, and the Director reportedly acknowledged that municipal market participants have expressed an "appetite" to see future disclosure guidance on new topics along the lines of the 2020 statements. Stay tuned for Workshop and other Fall municipal conferences where we can expect to hear more on these disclosure themes.

MSRB—Wading Into ESG Waters

The topic of "ESG disclosure" seems to be on every working group due diligence checklist for municipal primary offerings this summer. This is in part due to the SEC's much commented upon climate proposal for public, registered companies. It is also because issuers are starting to get unsolicited ESG scores from rating agencies, which is leading issuers to start thinking about what types of disclosures they make.

In December of last year, the MSRB issued a broad Request for Information regarding ESG practices in the municipal securities market. This led to much discussion among municipal market participants through the Spring and early summer conference season, and over 50 market participants, including NABL, submitted comment letters.

In early August, the MSRB published its much awaited "Summary of Responses" report on its ESG information request. This report is a balanced response back from the MSRB, particularly given initial concerns of the issuer and bond and disclosure counsel communities. First, as is now customary in pieces from the MSRB that appear to be suggesting either content or format for issuer disclosures, the report acknowledges that while its broader Dodd-Frank mission includes "to . . . protect municipal issuers," the Tower Amendment prevails: under Exchange Act Section 15B(d)(2), the MSRB is barred from requiring issuer filings, both pre- and postsale. Second, the report summary emphasizes the distinction between ESG related risk disclosure, with a recognition of the importance of materiality analysis, and the separate topic of labeling and marketing bonds with ESG designations—"Green Bonds." The report highlights that (a) ESG disclosure practices are still evolving, (b) market-based solutions are occurring and (c) regulation on this topic is premature, specifically including NABL's comment that "[R]egulation or standardization is premature, may be cost-prohibitive for small issuers, and could hamper the market's ability to address emerging ESG concerns." Third, the report says that enhancements may be made to EMMA that could improve market transparency of ESG—leaving us interested to see the improvements in EMMA. The Fall conference season may bring us more comment from the SEC's Office of Municipal Securities on applying materiality principles to ESG risk disclosures and to ESG labeling practices in primary offerings.

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September 2022

The Tax Microphone

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Remembering Perry E. Israel

All of you taking time to read this column will already know that our small community of bond tax practitioners suffered a devastating loss with the untimely passing of our esteemed friend and colleague, Perry Israel, in August. Innumerable small tributes to and reminiscences about Perry have been shared over the past several weeks, and I am sure there will be many more to come, not least at NABL's Workshop conference in October. But I want to take a moment to remember Perry in this column, not only because Perry had such an profound impact on so many in NABL's membership and on the good work that NABL does but, more importantly, because he was an outstanding friend and colleague to so many of us.

I've had the exceptional good fortune to know Perry from my very first days in private practice. I met Perry and first came to know him when I was a summer associate in the San Francisco office of Orrick, Herrington & Sutcliffe in 1990; when I joined Orrick as a newly-minted attorney in the Fall of 1992, shortly after completing a judicial clerkship, I fell into Orrick's tax practice and in particular into that firm's grouping of 103 specialists. At that time Perry had only been a partner in the firm for a short period of time, as I recall. Naturally, it fell to Perry to be one of a small group of mentors to me as I developed my skills as a bond tax lawyer. How lucky I was. I couldn't possibly have wished for a smarter, a more patient, a better listening, a more trusting and confidence-inspiring guide than Perry. And he was funny and easy-going, always ready with a broad smile. He had a unique way of putting people at their ease and, though he was virtually always the smartest and most insightful person in the room, he also had a knack for not talking down to anyone else and for listening to others with the utmost attention and care, even when what they had to say wouldn't have been worth much of his time.

Perry was extremely orderly and systematic in his approach to the law, which made him the amazingly effective teacher (or rabbi, as we used to say at Orrick all those years ago, of Perry and other seasoned vets in their 103 practice—the rest of us were scribes). I suppose this is why he also was perfectly suited to the herculean task of organizing all of the federal tax law materials in the bond financing field into coherency in the very first edition of NABL's most substantial and enduring reference tool, *Federal Taxation of Municipal Bonds*. I can still remember his office in that first year or so after I arrived at Orrick, piled high (but neatly) with print-outs and photocopies of vast amounts of primary source materials for inclusion in FTMB. I can't imagine how much effort Perry put into whipping that very first edition of the treatise into shape, but I would venture to guess that if Perry hadn't been its first Editor-in-Chief, *Federal Taxation of Municipal Bonds* wouldn't be the invaluable resource it is today, for so many of NABL's members. For this alone, NABL really owes Perry something like his own Nobel Prize.

Sticking with FTMB for a moment, though, and just to show that Perry was perfectly human, I'll share an anecdote from those days that perhaps a few other NABL members can recall. It goes like this:

After all of those months (years?) of marshalling all of those primary sources for FTMB, after writing (or overseeing the writing of) all of those squibs on private letter rulings and general counsel memoranda, after creating (or overseeing the creation) of tables of contents and table of authorities and after figuring out exactly how many loose leaf volumes it would take to cram all of this stuff into, it was time for the publishers to produce full-volume proofs of the entire set, complete with printed three-ring binders and the like. A small dry-run of the treatise to put on the shelf, to thumb through and to look over before giving the green light for a full production run.

Well, that was done and Perry (and presumably a number of trusty NABL hands) had a chance to test-drive the proofs, and when that was done, the go-ahead was duly given, and FTMB went into its first full production run. And only after boxes and boxes of those treatise volumes had been readied for delivery to practitioners and law libraries around the country, only then was it discovered that every single binder of every single volume in the set had been imprinted as follows: FEDERAL TAXATION OF "**MUNCIPAL"** BONDS. Yes. "Muncipal" Bonds. I don't remember Perry's remarks about this snafu exactly; he hardly owed an explanation to a junior tax associate like me. But I can remember his bemused look as we stood there in his office in real time talking about the screw-up, that slight nod of the head that he'd do, that inscrutable smile of his signifying something like, "For crying' out loud, after all this, how'd we miss THAT?" In spite of it all, though, Perry maintained his characteristic great good humor, and FTMB carries on today, an outstanding legacy of his hard work and leadership in service of NABL.

(Post script: The fix was relatively simple—small rectangular pieces, with a sticky adhesive backing were produced, bearing the correctly-spelled legend "FEDERAL TAXATION OF MUNICIPAL BONDS", and affixed to the spine of each and every one of those loose leaf binders that were part of the first run).

Having said all of this about Perry, I will say that it took some time for it to dawn on me that Perry was actually held in universally high regard throughout the bond lawyer community (and more broadly in the bond community as a whole). In the late 1990s, I left Orrick and California to join the firm of Palmer and Dodge in Boston. Turned out that we shared a good deal of 103 DNA because Perry, before me, had done the same thing, but in reverse. He'd started out as a young tax attorney in Palmer and Dodge's bond practice in Boston in the early 1980s, had learned the 103 ropes there from Neil Arkuss and had subsequently decamped for California and Orrick. As I learned when I arrived in Boston some years later, Perry had not been forgotten by his former colleagues at Palmer and Dodge, or by his counterparts in the bond community in New England. Suffice it to say that they had a lot to say about Perry, all of it good.

After my arrival at Palmer and Dodge, as I got started on a path of engaging with and contributing to NABL's Tax Committee projects and seminars with the encouragement and support of Neil Arkuss, I began to see that Perry had an outsize presence and influence in and on NABL and its work and was held in the highest regard by anyone who knew anything about NABL's tax law projects and priorities. Much of that had to do with Perry's mastery of the 103 practice, and his ability to impart the law to others. Neil Arkuss himself recently recounted to me the story of how Perry, when he was just starting in private practice, was asked to take on the formidable task of being on the front line of handling tax compliance work for the Massachusetts Housing Finance Authority's tax-exempt single family bond financing program. You'll recall that in the early 1980s, all of the sui generis federal tax regulations governing this category of bonds were quite new; and if that body of law seems nearly incomprehensible and impenetrable today, 40 years later, you can imagine how absolutely awful and terrifying it must have seemed back then, even to a seasoned veteran like Neil Arkuss. Anyway, as Neil tells the story, Perry, knowing what a tangled mess the single family bond rules were, sat there in his office, agreeing to take on this impossible task with that broad smile on his face. And Neil says that Perry handled the job with aplomb. The consummate 103 lawyer.

One last story, this one from another NABL worthy, Hobby Presley. This one underscores Perry's warmth and graciousness. Hobby remembers that he and Perry were once "dueling experts" on opposite sides of a sanction case brought by the IRS and Justice Department, and they were being deposed by the lawyers on the case on the same day. The litigators on each side of course tried in their turn to discredit the opposing party's expert. Hobby relates that Perry graciously acknowledged the former's expertise and integrity but noted that he disagreed with some of Hobby's legal conclusions. (Hobby also says that his responses about Perry were to the same effect.) After the depositions were over the litigators on both sides said they were surprised to see opposing experts respond favorably like that about each other, and they wondered if there was something Hobby and Perry needed to tell them about their relationship. Hobby reports that he and Perry laughed and responded that they were nothing more than professional acquaintances and that their mutual regard was simply part of the "NABL spirit", of which both were proud.

NABL spirit, indeed. I could go on, of course. Perry was devoted to his wife and family. He was unbelievably well-read and cultured. But I'll end on NABL spirit. Perry personified the very best of it. His influence will reverberate through the NABL membership for generations. As Hobby Presley put it to me, Perry is a person we all should aspire to emulate. I couldn't agree more.

Perry E. Israel
In loving memory

Enactment of a New Corporate Alternative Minimum Tax and other Highlights from (and Missed Opportunities in) the Inflation Reduction Act of 2022

It won't be news to bond tax practitioners that the Inflation Reduction Act (or "IRA") was enacted into law on August 16, 2022. Unfortunately, the IRA was bereft of provisions directly bearing on the tax-exempt bond markets, such as a restoration of tax-exempt advance refunding bonds (i.e., a repeal of the tax-exempt advance refunding bond repealer that was part of the Tax Cuts and Jobs Act of 2017), an extension of "qualified small issuer" treatment to issuers issuing up to $30 million of bonds in a calendar year for purposes of the "bank qualification" provisions of Section 265(b) of the Internal Revenue Code and the restoration of taxable direct-pay subsidy bonds (with modifications and improvements to the "build America bonds" model of years ago), each of which NABL has been advocating for with policymakers. NABL's leadership will have to continue advocating for the inclusion of these useful provisions in future legislative initiatives.

The IRA does, however, impose a new corporate alternative minimum tax for the taxable years of "applicable corporations" beginning after 2022, which creates a considerable secondary legislative effect for purposes of bond counsel practice.

Here's how the new corporate AMT provision works, in a brief nutshell. Under the IRA, an "applicable corporation" is a corporation (other than an S corporation, regulated investment company, or real estate investment trust) that together with the other members of its controlled group meets the adjusted financial statement income (AFSI) test. This AFSI test generally will be satisfied if the corporate taxpayer has average annual AFSI for the three years ending prior to the current tax year that is in excess of $1 billion. In brief, the new corporate alternative minimum tax will apply if and to the extent 15% of AFSI exceeds an applicable corporation's regular federal corporate income tax.

A corporate taxpayer's AFSI for a particular taxable year is its net income or loss on its "applicable financial statement" (AFS); this appears to be a "book income" concept because an AFS generally is defined to mean a financial statement prepared in accordance with GAAP principles that is required to be filed with the Securities and Exchange Commission (or a counterpart foreign securities regulator) or, if no financial statement is required to be filed with the SEC, an audited financial statement used by the corporate taxpayer for non-tax purposes.

There are lots of intricacies to the new corporate AMT that are beyond the scope of this column, including special rules for foreign corporations and any number of adjustments to AFSI relating to depreciation, intercorporate dividends within a consolidated group, and so on. The main point for purposes of the NABL membership, however, is that AFSI clearly includes interest income on all tax-exempt bonds, whenever issued.

Over the last month or so, this particular provision of the IRA precipitated a flurry of activity and discussions about modifying the tax disclosure for pending offerings of tax-exempt bonds (and even "stickering" of existing disclosure for publicly-offered bonds that had been closed some time prior to the enactment of the IRA but continued to be in an "underwriting period" under federal securities law). Bond opinions for many current transactions also have been modified to address this new AMT provision. At this point, most of the flurry appears to have subsided and the market seems to be internalizing its assessment of the potential impact of the new corporate AMT on tax-exempt bond pricing. Though in general the new tax will tend to create a drag on demand on the part of affected corporate taxpayers for tax-exempt bonds and other investments that are incorporated into the calculation of the new tax liability, it is not clear to me at this point how substantial the effect of the provision has been, or will be, on pricing for tax-exempt bonds. This may well be because the new tax, by all accounts, has been designed to create a new, additional tax liability for a very limited number of "applicable corporations". We shall see about that.

Apart from the new corporate AMT provisions, some NABL members will be interested in the provisions of the IRA that reduce the investment tax credit for energy property (Code Section 48), the clean electricity investment tax credit (Code Section 48E), the renewable energy production tax credit (Code Section 45), the clean electricity production credit (Code Section 45Y), the tax credit for carbon oxide sequestration (Code Section 45Q) and the clean hydrogen production tax credit (Code Section 45V) by the lesser of (i) 15% and (ii) the percentage of capital expenditures of the project or facility giving rise to the tax credit that is financed with the proceeds of tax-exempt bonds. At least with respect to the tax credit for carbon capture and sequestration under Code Section 45Q, this feature of the IRA appears to be bond-friendly, insofar as federal tax law prior to enactment of the IRA provided for a maximum reduction of these tax credits at a level of 50% rather than at a 15% level. Moreover, the IRA appears to allow state and local governments to receive direct payments from the United States in lieu of the Section 45Q credit.

Private Letter Ruling 202229002 (July 22, 2022)

Finally, let's turn to a recently-released private letter ruling addressing management contract compensation. Here is a summary of the PLR from the Public Finance blog at taxassociate.wordpress.com:

> "Hotel management contract. The manager is paid a percentage of gross revenues. The manager is also reimbursed for employee costs. The employees are employees of the manager operating the hotel. The PLR states: 'However, because the compensation to Service Provider includes the reimbursement of employee costs of Service Provider, the terms of the Agreement do not meet section 5.02(2) of Rev. Proc. 2017-13.' Section 5.02(2) [of Revenue Procedure 2017-13] states: '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 (other than any reimbursements of direct and actual expenses paid by the service provider to unrelated third parties) for any fiscal period.'"

For what it's worth, I think the 103 law updates and brief commentaries on this blog are excellent; they're well-written, and they're informative and timely. I am not sure who produces this content as there is no authorial attribution on the website itself, but thanks to the person or persons producing the blog for putting this kind of content out there in the public forum. We all benefit from it.

Anyway, back to the PLR. I did a bit of a double-take when I first read it, though on reflection it seems to me that this is because, as is often the case, the ruling is a bit thin on factual exposition. The reason it caught my attention is that seems to imply that a management contract that contemplates reimbursements of a manager's employee costs, such as salaries, incentive compensation and bonuses, in combination with a gross revenue sharing formula for compensating the company providing management services, can potentially cause a management contract to be characterized as one in which compensation is based on sharing of both revenues and expenses (which in turn trends toward a sharing of net profits, which under the principles of Treasury Regulations Section 1.141-3 and Revenue Procedure 2017-13 will cause the management contract to be treated as one that gives rise to private business use of the bond-financed facility under management).

That characterization might be fair enough if the employees whose salary expense (including incentive compensation and bonuses) were being reimbursed under the terms of the contract were “related parties” to the manager. But it seems like a stretch to reach that conclusion, or to be concerned about reaching that conclusion, if the employees in question are of the rank-and-file variety, with no ownership stake in or significant “dominion and control” over the manager. The ruling does refer in passing to incentive compensation and bonuses to “senior management employees” of the manager, which may have been enough to cause the IRS to be concerned. But, based on the facts presented in the ruling, which has no discussion of whether the employees in question could or should be considered “related parties” to the manager for purposes of Section 5.02(2) of Revenue Procedure 2017-13, it seems difficult to understand why this contract should be categorically treated as outside the safe harbor principles of Revenue Procedure 2017-13, at least to me; in most cases, my intuition is that employees can be treated as “unrelated third parties” to the companies for which they work.

In any event, PLR 202229002 reaches appears to reach the right result, because it concludes, based on all of the facts and circumstances, that no part of the compensation to the manager under the contract is based on a sharing of the net profits of the hotel operation. So perhaps the most we can say is that this ruling is something of a creature of the facts presented, not all of which are crystal clear in the ruling itself, that the “senior” status of some of the employees whose compensation is being reimbursed was enough to make the Service want to take a closer look at the arrangement rather than declare it purely safe harbor in nature. That would be fair enough, of course.

Another reflection I’ve had about this ruling is that it can serve as a reminder that we 103 practitioners need to be prepared to think holistically about compensation arrangements in contracts relating to the operation or management of facilities financed with tax-exempt bonds. Prior to the release of Revenue Procedure 2017-13, of its predecessor, Revenue Procedure 97-13, it could be said in many cases that safe harbor compensation arrangements were somewhat easier to discern: per capita, per-unit of service, gross revenues, periodic fixed fees and so on. Of course, those pre-2017 safe harbor parameters were more constrained, particularly in terms of contract duration, but there was an articulated catalog of permitted categories for compensation to fit into. Under Revenue Procedure 2017-13, by contrast, we’re told essentially that anything goes as long as it’s not based on a sharing of net profits. There clearly is consistency between the two sets of guidance, of course, but these days there is perhaps more stress on evaluating the economic substance of compensation provisions to determine whether a management contract gives rise to private business use.

As a final note, apart from the pass-through arrangement with respect to employee compensation, I will remark that the IRS in this ruling seems not to intimate any fundamental concerns with a management contract that is based on a gross revenue sharing formula for compensation. Some practitioners have noted that Revenue Procedure 2017-13 is not entirely clear on its face on that score, but the ruling seems to support the view that gross revenue compensation provisions in a management contract will not, by themselves, give rise a “bad use” of a bond-financed facility. I think this is the correct view of the law of private business use under Section 103 of the Code.

Antonio D. Martini
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