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February 4, 2008

John J. Cross III
Associate Tax Legislative Counsel
Office of Tax Policy
Department of the Treasury
1500 Pennsylvania Avenue, N.W.
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Washington, D.C. 20220

Dear John:

The National Association of Bond Lawyers ("NABL") respectfully submits the enclosed draft guidance document that addresses certain tax issues that may be implicated by conversion of the interest rate mode of certain state and local bonds from an auction rate mode to another interest rate mode provided for under the existing terms of the bonds.

The current economic environment has brought about the downgrade or the threat of downgrade of certain municipal bond insurers, which has resulted in a substantial increase in rates on auction rate bonds. Accordingly, many issuers are electing to convert their auction rate bonds into another interest rate mode pursuant to the terms of the bonds.

Questions have been raised regarding the treatment under Notice 88-130 of multi-modal bonds in an auction rate mode. The enclosed draft guidance document attempts to resolve any doubts in an otherwise volatile economic environment.

The enclosed draft guidance applies to a specific, narrow issue that is affecting many issuers of tax-exempt bonds. However, a number of other difficult issues have arisen as a result of the current economic environment that relate more generally to Section 1.1001-3 of the Treasury Regulations. NABL urges prompt consideration for timely guidance on other issues, including the following:

- Providing relief for multi-modal bonds converted from a short-term mode to a long-term mode, where any changes to the terms of the bonds (other than, perhaps, the resetting of the interest rate pursuant to the existing terms of the bonds following such conversion) would not be considered significant under Section 1.1001-3.

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- Providing relief for changes in credit enhancement on tax-exempt bonds that would be considered non-recourse under Section 1.1001-3.

NABL appreciates the consideration of this submission and would welcome the opportunity to discuss these comments with you.

NABL exists to promote the integrity of the municipal market by advancing the understanding of and compliance with the law affecting public finance. A professional association incorporated in 1979, NABL has approximately 3,000 members and is headquartered in Chicago.

If you have any questions, please contact me at 205/226-3482 or though email at fclark@balch.com or Scott R. Lilienthal at 202/637-5849 or through email at srlilienthal@hhlaw.com or Elizabeth Wagner, Director of Governmental Affairs, at 202/682-1498 or through email at ewagner@nabl.org.

Thank you again.

Sincerely,

Foster Clark

Enclosure

cc: Eric Solomon
Donald L. Korb
Michael J. Desmond
Stephen Larson
Rebecca L. Harrigal
Clifford J. Gannett
Scott Lilienthal

[REV. PROC.][NOTICE] 2008 – ___

SECTION 1. PURPOSE

This [revenue procedure][notice] describes the conditions under which the Internal Revenue Service will not contend that a conversion of the interest rate mode of a "multi-modal" state or local bond from an auction rate mode to another interest rate mode pursuant to the existing terms of the bond results in the retirement and reissuance of the bond for purposes of sections 103 and 141 through 150 of the Internal Revenue Code of 1986, as amended.

The purpose of this [revenue procedure][notice] is to provide certainty in the current economic environment with respect to certain tax issues that may be implicated by conversion of the interest rate mode of certain multi-modal state and local bonds from an auction rate mode to another interest rate mode provided for under the existing terms of the bonds, as described below. No inference should be drawn about whether similar consequences would result if a transaction falls outside the limited scope of this [revenue procedure][notice]. Furthermore, no inference should be drawn that this [revenue procedure][notice] is necessary to prevent transactions within its scope from being treated as a reissuance or from otherwise affecting the tax-exempt status of state and local bonds.

SECTION 2. BACKGROUND – NOTICE 88-130 AND QUALIFIED TENDER BONDS

.01 Notice 88-130, 1988-2 C.B. 543, provides guidance to issuers of state and local bonds concerning regulations to be issued under section 150 of the Internal Revenue Code providing rules for determining when such bonds will be considered retired and, in some cases, reissued solely for purposes of sections 103 and 141 through 150. Specifically, Notice 88-130 provides guidance concerning the circumstances under which "qualified tender bonds," as defined in the Notice, will be considered retired and reissued for purposes of section 103 and 141 through 150. Terms not otherwise defined in this [revenue procedure][notice] shall have the meanings provided in Notice 88-130.

.02 Section 1.1001-3 of the Income Tax Regulations, finalized in 1996, provides general rules for determining whether a modification to a debt instrument will be treated as an exchange of the original debt instrument for a new, modified debt instrument for federal income tax purposes. Section 1.1001-3(a)(2) provides that section 1.1001-3 does not apply for purposes of determining whether tax-exempt bonds that are qualified tender bonds are reissued for purposes of sections 103 and 141 through 150.

.03 A qualified tender bond generally consists of a bond the terms of which provide that the holder of the bond may or must in all events tender the bond for purchase or redemption at par (plus any accrued interest) on one or more tender dates before the final stated maturity date. In addition, the interest on a qualified tender bond must accrue (a) in the case of interest accruing to the first tender date, at a rate set on or after the sale date of the bond at the lowest rate that would enable the bond to be marketed at par (plus any accrued interest) on the date of issue, and (b) in the case of interest accruing for each period between tender dates (including the final period to maturity), at a rate that is reset for each period at the lowest rate that would enable the bond to be remarketed at par (plus any accrued interest) at the beginning of each period. Notice 88-130 also imposes certain maturity limitations on qualified tender bonds.

.04 Bonds intended by an issuer to constitute qualified tender bonds are most often issued with multiple interest rate "modes." Typically, the documents under which such multi-modal bonds are issued provide the issuer with the option to change the period between tender dates (including the final period to maturity). Such a change is referred to in Notice 88-130 as a "qualified tender change." Notice 88-130 further provides that any purchase of a qualified tender bond pursuant to a tender right is a "qualified tender purchase" if the purchase occurs pursuant to the terms of the bond, the terms of the bond require that best efforts be used to remarket the bond, and the bond is remarketed no later than 30 days after the date of such purchase.

.05 Notice 88-130 generally provides that a qualified tender bond will be treated as retired only if: (a) in a transaction or series of transactions there is any "change" (as defined below) to the terms of the bond (other than a "qualified corrective change" as defined in the Notice) in connection with a qualified tender change which qualified tender change increases the period between tender dates from a period not exceeding one year to a period exceeding one year or vice versa; (b) there is a change in the period between tender dates that is not a qualified tender change; (c) there is a change to the terms of the bond (other than a qualified corrective change) which would cause a disposition of the bond under section 1001 without regard to the existence or exercise of the tender right; (d) the bond is purchased or otherwise acquired by or on behalf of the issuer or a true obligor which is a governmental unit or an agency or instrumentality thereof; or (e) the bond is otherwise retired or redeemed. Notice 88-130 further provides that, for these purposes, a bond will be treated as purchased or otherwise acquired by or on behalf of a person if the bond is purchased or otherwise acquired (other than pursuant to the terms of a third party guarantee) by that person (or by any other person in consideration for any payment provided directly or indirectly by such first person) in a manner that liquidates the bondholder's investment.

.06 Notice 88-130 provides that for this purpose the term “change” means, with respect to the terms of a bond, any discretionary alteration in the legal rights or remedies of the holder that occurs after the date of issue. An alteration to the terms of the bond is discretionary unless all elements of the alteration are entirely outside of the control of the issuer, any true obligor, any holder of the bond, any related person (as defined in section 147(a)(2)), anyone acting on behalf of any such person or persons, or any combination of the foregoing. Accordingly, an alteration in the period between the tender dates applicable to the bond (for example, a conversion from a daily tender and interest rate mode to a weekly tender and interest rate mode or a conversion from a weekly tender and interest rate mode to an interest rate fixed to final stated maturity with no tender right) that occurs at the option of the issuer is a change, but the resetting of the interest rate on a bond to a tender rate from another tender rate pursuant to the terms of the bond is not a change. An alteration in the terms of a bond which occurs automatically as a result of a discretionary alteration (for example, an automatic alteration in the security for a bond occurring when the interest rate is converted at the option of the issuer from a variable interest rate to an interest rate fixed to the maturity of the bond) is not a change.

SECTION 3. BACKGROUND – AUCTION RATE BONDS

.01 In the years since the issuance of Notice 88-130, the state and local bond market has seen significant growth in the issuance of auction rate bonds. Auction rate bonds are long-term, variable-rate bonds tied to short-term interest rates. Auction rate bonds generally have a long-term nominal maturity, and interest rates are reset at predetermined intervals, usually seven, 28, or 35 days or monthly, using a modified Dutch auction process. The bonds generally trade at par and are callable at par on any interest payment date at the option of the issuer. Interest is paid for a current period based on the interest rate determined in the prior auction period. Auction rate bonds are frequently issued as multi-modal bonds with a conversion feature that allows for conversion of such bonds from the auction rate mode to long-term fixed or variable rate modes. The holder of an auction rate bond typically has no right or obligation to tender the bond while it is in the auction rate mode, except for a mandatory tender upon a conversion of the bond at the option of the issuer from the auction rate mode to another interest mode. Auction rate bonds are commonly backed by municipal bond insurance.

.02 The current economic environment has brought about the downgrade or the threat of downgrade of certain municipal bond insurers, which has resulted in a substantial increase in rates on auction rate bonds. Accordingly, many issuers are opting to convert their multi-modal bonds that are in auction rate mode into another interest rate mode pursuant to the terms of the bonds. Such a conversion may require new credit enhancement for the bonds, such as a standby bond purchase agreement, if the bonds are converted to a variable rate mode.

.03 Questions have been raised regarding the treatment under Notice 88-130 of multi-modal bonds in an auction rate mode. Specifically, questions have been raised regarding the treatment of multi-modal bonds in an auction rate mode as qualified tender bonds for purposes of Notice 88-130, and whether multi-modal bonds in an auction rate mode should be treated as having a period between tender dates that does not exceed one year when they have been in auction rate mode for more than one year. Because of the questions and because of the market requirement of an unqualified opinion, issuers and their counsel may be compelled to treat a conversion of a multi-modal bond from an auction rate mode to another interest mode, albeit in accordance with the provisions of the bond, as a retirement and reissuance of the bond for purposes of section 103 and 141 through 150, potentially resulting in adverse consequences including acceleration of rebate payment obligations, change in law risk, possible treatment as an acquisition financing if the financed facilities have been or will be sold within six months before or after the conversion, and arbitrage yield recomputation issues, including issues relating to "integration" of an interest rate swap under the qualified hedge rules and calculation of the cost of qualified guarantees.

SECTION 4. SCOPE

This [revenue procedure][notice] applies to any state or local bond bearing interest at an auction rate that would be a qualified tender bond within the meaning of Notice 88-130 if for purposes of the Notice (i) the auction rate were considered to qualify as a tender rate, and (ii) during the auction rate mode the bond were considered to be subject to a tender right.

SECTION 5. APPLICATION

In the case of a bond to which this [revenue procedure][notice] applies, the Internal Revenue Service will not contend that a conversion of the interest rate mode of the bond from an auction rate mode to another interest rate mode pursuant to the existing terms of the bond results in the retirement and reissuance of the bond for purposes of sections 103 and 141 through 150 unless: (a) in a transaction or series of transactions there is any change to the terms of the bond (other than a qualified corrective change) in connection with the conversion, and the period between tender dates following the conversion exceeds one year; (b) there is a change to the terms of the bond (other than a qualified corrective change) which would cause a disposition of the bond under section 1001 without regard to the mandatory tender upon the conversion of the bond; (c) the bond is purchased or otherwise acquired by or on behalf of the issuer or a true obligor which is a governmental unit or an agency or instrumentality thereof; or (d) the bond is otherwise retired or redeemed.

SECTION 6. EFFECTIVE DATE

This [revenue procedure][notice] is effective for conversions occurring after __________ ___, 2008. This [revenue procedure][notice] may be applied to conversions occurring on or before __________ ___, 2008.

SECTION 7. DRAFTING INFORMATION

The principal author of this [revenue procedure][notice] is ______________ of the Office of Associate Chief Counsel (Financial Institutions and Products). For further information, contact _____________ on (202) 622-______ (not a toll-free call).