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June 19, 2015

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Branch Chief, Branch 5
Office of Chief Counsel
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, DC 20024

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

Re: Supplemental Commentary on TEFRA Public Approval Requirement

Dear Messrs. Polfer and Cross:

The National Association of Bond Lawyers ("NABL") respectfully submits the attached supplemental commentary with respect to (i) the temporary regulations governing the "TEFRA" public approval requirement under Section 147(f) of the Internal Revenue Code of 1986 contained in Section 5f.103-2 of the income tax regulations, and (ii) the proposed regulations governing the TEFRA public approval requirement published on September 9, 2008, and corrected on October 8, 2008. These comments were prepared by an ad hoc committee composed of the individuals listed in Attachment C to the comments and approved by the Board of Directors of NABL.

NABL exists to promote the integrity of the municipal market by advancing the understanding of and compliance with the law affecting public finance. We respectfully provide the attached supplemental commentary in furtherance of that mission.

If NABL can provide further assistance, please do not hesitate to contact Bill Daly in our Washington, D.C., office at (202) 503-3303.

Sincerely,

Antonio D. Martini
President

Attachments

SUPPLEMENTAL COMMENTARY CONCERNING "TEFRA" PUBLIC APPROVAL REQUIREMENT

The National Association of Bond Lawyers ("NABL") respectfully submits the following comments with respect to (i) the temporary regulations governing the "TEFRA" public approval requirement under Section 147(f) of the Internal Revenue Code of 1986, as amended (the "Code"),[1] contained in Section 5f.103-2 of the income tax regulations (the "Temporary Regulations"), and (ii) the proposed regulations governing the TEFRA public approval requirement published on September 9, 2008, and corrected on October 8, 2008 (the "Proposed Regulations").

This submission supplements NABL's previously submitted comments to the Department of the Treasury ("Treasury") and the Internal Revenue Service (the "IRS") (i) dated January 24, 2007 (the "2007 NABL TEFRA Comments"), and (ii) dated October 15, 2008 (the "2008 NABL TEFRA Comments" and, together with the 2007 NABL TEFRA Comments, the "2007/2008 NABL TEFRA Comments"). The 2008 NABL TEFRA Comments were submitted primarily in response to publication of the Proposed Regulations. The 2007 NABL TEFRA Comments are attached to this submission as Attachment A, and the 2008 NABL TEFRA Comments are attached as Attachment B.

The TEFRA public approval requirement is arguably one of the more burdensome requirements for tax exemption. NABL believes that ways in which the requirement may be made less burdensome to issuers and conduit borrowers, while still achieving the underlying objectives of the requirement, should continually be reassessed, with deference given to how state and local governments carry out their day-to-day operations and with recognition of technological advances as tools for implementation. The comments made herein are premised on this notion.

NABL reaffirms the 2007/2008 NABL TEFRA Comments and applauds the advances made by Treasury and the IRS in the Proposed Regulations. Post-issuance remedial action procedures, electronic notice publication and the ability to cancel a public hearing, among other changes, mark significant progress in Treasury's efforts to modernize the TEFRA requirements and reduce the burdens imposed by these requirements. In this submission NABL does not intend to reiterate the 2007/2008 NABL TEFRA Comments. Rather, this submission is intended to provide several discrete comments that reemphasize certain of the points made in the 2007/2008 NABL TEFRA Comments and add a few new comments for Treasury and the IRS to consider in finalizing the next set of TEFRA regulations, whether proposed, temporary or final (the "New TEFRA Regulations").

Working Capital

The 2008 NABL TEFRA Comments touched on the treatment of working capital for TEFRA public approval purposes by recommending that the redirection of proceeds from

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[1]Unless otherwise indicated, all section references herein are to the Code.

approved facilities to working capital for an activity conducted in whole or in part at the approved facilities be treated as an insubstantial deviation under Prop. Treas. Reg. § 1.147(f)-1(b)(6). Those comments point out, for example, that the use of unspent proceeds from a construction or acquisition fund or, with bondholder permission, from a reserve fund to pay working capital costs may be essential to avoidance of default in many distress situations.

We suggest that the very nature of working capital expenses, most commonly an entity's ordinary and necessary operating expenses, may not always lend itself to the precise association of a working capital expenditure with a particular facility. In addition, issuers and borrowers typically will not think to include the use of proceeds of their bond issues for working capital in the first instance since that is not the original intention of the bond issue. Given that (i) there are protections and limitations built into the Code and the Treasury Regulations governing the use of proceeds for working capital purposes,[2] and (ii) working capital expenditures by their nature do not "give rise" to facilities, which were the original basis for giving notice to the public, and have long been recognized as such, NABL recommends that the New TEFRA Regulations provide that an issuer need not include a reference to working capital expenditures in its TEFRA notice. The New TEFRA Regulations should also provide that the issuer or, as applicable, the conduit borrower may later redirect proceeds of its bond issue to working capital expenditures without regard to a determination of location.[3]

We note that the Proposed Regulations, in Prop. Treas. Reg. § 1.147(f)-1(c)(1), provide with respect to qualified 501(c)(3) bonds that "the term facility means a facility, as defined in the first sentence of this paragraph (c)(1), and also includes working capital expenditures to be financed with proceeds of the issue." This section also defines a facility as including one or more capital projects, without a specific reference to working capital.[4] We recommend that the New TEFRA Regulations permit, more broadly, the use of proceeds for working capital, in addition to the financed capital facilities, without a requirement that working capital items as such be explicitly referenced in the notice of public hearing.[5]

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[2]For all bond issues, see Treas. Reg. § 1.148-6(d), which provides certain limitations on the use of proceeds for working capital expenditures generally. For exempt facility bonds, Section 142 of the Code contains a 95% test for providing the specific type of project, which must be capital in nature. *See also* Treas. Reg. § 1.148-10, which effectively limits the timing and sizing of bond issues.

[3]In such case, the reference to working capital in the parenthetical in Prop. Treas. Reg. § 1.147(f)-1(b)(2)(i) would not be needed.

[4]The term "capital projects" is defined in the arbitrage regulations' definitions to include "related" working capital expenditures to which the de minimis rules under Treas. Reg. § 1.148-6(d)(3)(ii)(A) apply. Using such a limitation in the TEFRA public approval context may be unduly limiting and not in furtherance of the policies underlying the TEFRA public approval requirement.

[5]With respect to Section 147(b)'s limitation of the average maturity of a private activity bond issue (including a qualified 501(3)(3) bond issue) issue to 120% of the average reasonably expected economic life of the bond-financed property, Treas. Reg. § 1.147(b)-1 provides specifically that "Section 147(b) does not apply to proceeds of a private activity bond issue used to finance working capital expenditures." Given the policies underlying the TEFRA public approval requirement, a similar approach should be considered here.

Multiple Facilities and Integrated Operations

In the 2007 NABL TEFRA Comments, NABL provided a comprehensive discussion relating to the definition of "facility" and the concept of "integrated operations." As the 2007 NABL TEFRA Comments indicate, "[d]eciding what constitutes an 'integrated operation' is most difficult for borrowers that are complex organizations with multiple campuses and/or physical locations . . . such as health care delivery systems, airports, utility systems, universities and other similar organizations."

As indicated above, the Proposed Regulations, in Prop. Treas. Reg. § 1.147(f)-1(c)(1), provide a definition of the term "facility." This section, however, unlike the Temporary Regulations,[6] is silent on the concept of an integrated operation. The 2008 NABL TEFRA Comments specifically recommended that final regulations include the concept of integrated facility as set forth in Treas. Reg. § 5f.103-2(f)(4), to the effect that separate tracts of land may be treated as a single facility if they are used in an "integrated operation."

The 2007 NABL TEFRA Comments recognize that there are essentially two major areas to which the concept has application: (i) the address or addresses of the financed property that are included in the TEFRA notice, and (ii) the statement of dollar amounts. The 2007 NABL TEFRA Comments provide a comprehensive discussion of each. Please refer to the 2007 NABL TEFRA Comments for a discussion of addresses needed to be set forth in the TEFRA notice. We continue to endorse those comments.

In addition, the 2008 NABL TEFRA Comments recommend the addition of a statement that, in the case of a multipurpose issue, the notice and approval do not need to allocate the amount of the issue between the various facilities or purposes of the issue. Those comments go on to say that "the statutory requirement of approval of the issue is satisfied by a notice and approval of the estimated amount of the issue as a whole and does not require a breakdown or itemization of different portions of the issue, other than in the case of post-issuance pooled finance approvals . . . ."

With respect to the requirement to state a maximum amount of obligations to be issued for a facility in the context of multiple facilities, we call your attention to a statement in a footnote in the 2007 NABL TEFRA Comments that "many tax practitioners provide an amount of obligations to be issued for every non-contiguous building that might be financed," and that this over-inclusive approach does not provide the public adequate notice regarding what is being financed." In our experience, probably more often, practitioners will manage to reach the conclusion that an organization of commonly controlled multiple facilities constitutes an integrated operation, so as to be able to eliminate having to state a separate dollar amount for each facility.

NABL recommends that the New TEFRA Regulations provide that, to the extent the bond-financed improvements to be made at various locations are and/or will be owned or

[6]Treas. Reg. § 5f.103-2(f)(4).

operated by the same entity or by separate legal entities that are related persons,[7] under common management or control[8] or are part of a controlled group,[9] such locations, improvements or properties be considered part of an integrated operation for purposes of defining the bond-financed facility and the amount of the obligations to be issued for such facility.

Movable or Intangible Property

Neither the Temporary Regulations nor the Proposed Regulations explain how the TEFRA public approval requirements are to be applied to financed property that is movable or intangible. NABL recommends that final regulations acknowledge these types of property and guide issuers and borrowers in applying the appropriate approval procedures.

Vehicles are an example of movable property and include, for instance, mobile library or medical vans or rescue helicopters that provide services to rural communities. This type of financed property may be moved on non-specific routes and often without predetermined schedules throughout several jurisdictions, possibly including other states, and does not necessarily have predetermined locations at which services are provided. Federal, state or local law may set forth where the property must be licensed, titled, registered or insured, or an issuer or borrower may have a central location at which the property is serviced or to which the property returns after assignments. NABL believes that the "location" of this type of property for purposes of the approval under Section 147(f) should be any location with a strong nexus to the financed property, such as the location at which the property is located for the longest period. The determination should be based on all facts and circumstances and take into account special characteristics of the property. This is important for intangible financed property, which may have a nexus with more than one jurisdiction. Radio frequency licenses, for instance, may be registered under federal law in one jurisdiction (or otherwise assigned to one jurisdiction) but the radio signal may be transmitted using facilities in other jurisdictions. A facts and circumstances analysis should permit the issuer or borrower to treat the jurisdiction of registration, the jurisdiction of assignment or the jurisdiction having transmission facilities as the location of the property for purposes of Section 147(f). A safe harbor for movable or intangible financed property should permit an issuer or borrower to conclude that the applicable location is the location (a) in which the property must be licensed, titled, registered or insured, (b) to which the property returns after assignments, (c) to which the property is assigned under applicable law or (d) from which the output associated with the property (e.g., a radio signal) is transmitted.

Issuers and borrowers should be given sufficient flexibility and discretion in deciding the strength of a property's nexus under the facts and circumstances analysis. The "substantial connection" standard that is set forth in other contexts relating to state or local bonds (e.g., in Rev. Rul. 77 281 or Rev. Rul. 85-112) may be helpful to illustrate the nexus recommendation, but that requirement can be unnecessarily restrictive. A substantial connection within those

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[7] *See* Section 144(a)(3).

[8] *See* Section 145(b)(3).

[9] *See* Treas. Reg. § 1.150-1(e).

contexts was or is required to prove either that movable property would be located within the boundaries of the issuer (which was a condition to qualifying bonds as part of an exempt small issue under Section 103(b)(6) of the Internal Revenue Code of 1954) or to determine whether capital expenditures for the property are to be included in determining compliance with the $10 million limit for exempt small issue private activity bonds. These considerations are not relevant where the purpose of determining nexus is to give reasonable public notice to the population that is most likely to be affected by the bond project.[10]

The New TEFRA Regulations should also provide that once the issuer or borrower determines the applicable location of movable or intangible property and uses the property in a manner supporting the association with the applicable location for a substantial period of time,[11] a post-issuance change in the use of the property that would have supported a different location will not be treated as a substantial deviation in the use of such bond-financed property.[12]

Post-Issuance Public Approval for Substantial Deviations

NABL applauds Treasury and the IRS for incorporating into the Proposed Regulations the notion of post-issuance public approval[13] to "cure" a deviation that rises to the level of a substantial deviation. This approval, referred to herein as "supplemental approval," must be accompanied by the satisfaction of two conditions. The first of the two conditions[14] requires that the issuer, as of the issue date of the bonds, had reasonably expected that there would be no substantial deviation between the information required to be conveyed in the notice of public hearing and public approval and actual information (which we assume to mean actual facts). NABL takes no issue with this condition as it is similar in concept to the reasonable expectation requirement in the remedial action regulations.[15]

The second of the two conditions[16] is two-pronged: Either (i) the cost of the facility was less than expected so that the issuer or conduit borrower ended up with more proceeds than were

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[10]NABL is not suggesting that the proposed nexus determination described for purposes of Section 147(f) change the manner in which compliance with the $10 million limit is determined for small issue bonds.

[11]See, e.g., Treas. Reg. § 1.141-2(d)(2)(ii)(A). Although the term "substantial" is susceptible to differing meanings in differing contexts, practitioners have often used 10% of the term of the bond issue as a reasonable interpretation of "substantial" in the context of applying Treas. Reg. § 1.141-2(d)(2)(ii).

[12]Alternatively, if such change in the use of such property were considered a substantial deviation, the supplemental public approval permitted in Prop. Treas. Reg. § 1.147(f)-1(b)(6)(iii) should not be restricted to situations in which the original use is no longer feasible or viable. See a more general discussion of supplemental public approvals below.

[13]Prop. Treas. Reg. § 1.147(f)-1(b)(6)(iii)(C).

[14]Prop. Treas. Reg. § 1.147(f)-1(b)(6)(iii)(A).

[15]Treas. Reg. § 1.141-12(a)(1).

[16]Prop. Treas. Reg. § 1.147(f)-1(b)(6)(iii)(B).

needed for the facility, or (ii) the issuer or borrower must be able to establish that the use of proceeds for the facility is "no longer feasible or viable." NABL views this condition as unnecessarily limiting. Aside from opening up new interpretive questions regarding feasibility and viability, there seems to be little in the way of policy justification to limit issuers and borrowers in reallocating proceeds to new locations and facilities as long as supplemental approval is obtained prior to the reallocation. Indeed, there may be many legitimate reasons for the reallocation of proceeds between one facility and another based on the issuer's or borrower's own economic and business-driven determinations. The 2008 NABL TEFRA Comments provided several examples of situations where this condition would be too limiting and suggested that the condition "be liberalized to give issuers and borrowers more flexibility." Since the time of the 2008 NABL TEFRA Comments, NABL has updated its thinking on this point and now recommends that Treasury eliminate this condition altogether.

Cancellation of Public Hearing

Prop. Treas. Reg. § 1.147-1(c)(2) sets forth the definition and scope of, and operating rules, for the public hearing. That subparagraph provides in part that if a governmental unit "provides reasonable public notice for a public hearing and receives no timely requests to participate in the hearing, then the governmental unit may cancel the hearing and, for purposes of this section, the public hearing requirement will be treated as met."

The 2008 NABL TEFRA Comments requested clarification of whether the notice of public hearing must indicate that the hearing may be cancelled without notice if no timely requests to participate are received, and of how to address the non-receipt of cancellation notice by the issuer (e.g., a failed email). In addition to our continuing interest in these two requested items, NABL requests clarification regarding the manner in which the issuer or, in cases where the issuer is issuing on behalf of a governmental unit, the governmental unit, communicates notice of cancellation to the public. NABL recommends that the New TEFRA Regulations provide that either the governmental unit or the issuer issuing on behalf of a governmental unit may provide notice of cancellation by posting such notice on its website in the same manner in which it posts other public notices in accordance with state and local law and procedures.

Effective Date

The Proposed Regulations provide that they would apply to bonds sold on or after the date of publication of final regulations in the Federal Register. We understand that it is likely that the New TEFRA Regulations will be published in proposed form at least in part. Because many provisions of the Proposed Regulations are intended to reduce the burden on issuers and borrowers and are ameliorative, it is important that the New TEFRA Regulations provide for the ability of issuers and borrowers to apply the regulations prior to their adoption in final form. In this regard, it would be helpful if the New TEFRA Regulations could be optionally applied not only to bond issues issued after the date of publication of the New TEFRA Regulations, but also to supplemental approvals with respect to bond issues outstanding prior to such date.

Attachment A

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January 24, 2007

John J. Cross III
Associate Legislative Counsel
Office of Tax Policy
Department of the Treasury
1500 Pennsylvania Avenue, N.W., 4212 B MT
Washington, D.C. 20220

RE: Guidance Recommendations for Update and Clarification Regarding Public Approval Requirements for Private Activity Bonds under Internal Revenue Code Section 147

Dear John:

Enclosed are guidance recommendations by the National Association of Bond Lawyers (NABL) for an update and clarification regarding public approval requirements for private activity bonds under Internal Revenue Code Section 147. A list of the NABL TEFRA Study Group who participated in the preparation of the recommendations is also enclosed as Exhibit II.

NABL has continued interest in clarifying and facilitating compliance with the tax law and regulations and believes that this area is particularly in need of such clarification. NABL also continues to offer assistance in developing alternatives that would achieve clarity, certainty and administrability for its members.

If you have questions, please contact me at 949/725-4237 or through email at clew@sycr.com or Elizabeth Wagner, Director of Governmental Affairs, at 202/682-1498 or through email at ewagner@nabl.org.

Thank you for the opportunity to submit NABL's recommendations. We look forward to working with you.

Sincerely,

Carol L. Lew

Carol L. Lew

Enclosures

cc: Eric Solomon
Michael J. Desmond
Donald L. Korb
Clifford J. Gannett
NABL TEFRA Study Group Members
Catherine E. Livingston
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Johanna L. Som de Cerff
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RECOMMENDATIONS
BY THE
NATIONAL ASSOCIATION OF BOND LAWYERS
TO THE DEPARTMENT OF THE TREASURY
OFFICE OF TAX POLICY
AND THE
INTERNAL REVENUE SERVICE

REQUESTING AN UPDATE OF GUIDANCE AND CLARIFICATION
UNDER INTERNAL REVENUE CODE SECTION 147
REGARDING PUBLIC APPROVAL REQUIREMENTS
FOR PRIVATE ACTIVITY BONDS

Introduction

The following comments are submitted on behalf of the National Association of Bond Lawyers ("NABL") TEFRA Study Group ("Study Group") for the purpose of offering specific recommendations regarding the "public approval requirements" under Section 147(f) of the Internal Revenue Code of 1986, as amended, (the "Code") and Treas. Reg. § 5f.103-2.[1]

Consistent with NABL's "Tax Simplification Recommendations to Treasury on Tax-Exempt Bonds," dated June 14, 2002 (the "2002 Report"), the Study Group continues to recommend repeal of the TEFRA public approval requirement for private activity bonds under Section 147(f) of the Code. (*See* attached excerpt, Exhibit I.) The Study Group agrees with the 2002 Report that a "sunshine" policy generally promotes good government, but that "this requirement has outlived its original purpose in 1982 of helping to control private activity bond volume."

Absent repeal, the Study Group also concurs with the 2002 Report's assertion that simplification of the public approval requirement could be accomplished through public administrative guidance, "given that many of the excessive details reside in old regulations in this area." Specifically, the Study Group has addressed below the application of these old rules to bond issues involving complex projects, such as projects for multi-property borrowers, and projects that change either during the issuance process or after bond issuance is completed, such as under-budget projects. In addition, the Study Group has identified areas needing clarification, such as what constitutes an "insubstantial deviation" from the published notice for an otherwise qualifying project

[1] Section 147(f) the Code was enacted by the Tax Equity & Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, 96 Stat. 324 ("TEFRA"). Treas. Reg. § 5f.103-2 was promulgated under Section 103(k) of the Internal Revenue Code of 1954, as amended (the "1954 Code").

Except as noted, all references to the Code are to the Internal Revenue Code of 1986, as amended.

due to change in business conditions. Simplification in the TEFRA rules should prove helpful to issuers and practitioners, as well as afford assistance to the Internal Revenue Service (the "IRS") in tax administration.

I. TEFRA Notice – Definitions of "Facility" and "Integrated Operation"

Section 147(f) of the Code provides that, in order to qualify for tax exemption, a private activity bond issue must satisfy the necessary public approval requirements. Public approval can be obtained by voter referendum or, more commonly, a public hearing following "reasonable public notice."

Treas. Reg. § 5f.103-2(f)(2) (promulgated under Section 103(k) of the 1954 Code, the predecessor to Section 147(f) of the Code), specifies that the public notice must contain:

(1) A general, functional description of the type and use of the financed *facility*;

(2) The maximum amount of obligations to be issued *with respect to the facility*;

(3) The initial owner, operator or manager of the *facility*; and

(4) The prospective location of the *facility* by its street address or, if none, by a general description designed to inform readers of its specific location (emphasis added).

Each of these public notice requirements refers to the "facility." Treas. Reg. § 5f.103-2(f)(4) currently defines "facility" as a tract or adjoining tracts of land, improvements thereon, and personal property used in connection therewith. It further provides that separate tracts of land may be treated as one facility only if they are used in an integrated operation. Therefore, if separate facilities are being financed with one issue of obligations, Treas. Reg. § 5f.103-2 requires that the public notice contain the maximum amount of the obligations, the initial owner, operator or manager and the location, for each facility that is not part of an integrated operation. Because "integrated operation" is not defined, determination of when the public notice requirements must be separately stated for a particular facility proves difficult.

Deciding what constitutes an "integrated operation" is most difficult for borrowers that are complex organizations with multiple campuses and/or physical locations (for purposes of this paper, an "Organizational System"), such as health care delivery systems, airports, utility systems, universities and other similar organizations. These Organizational Systems are often located on several non-adjoining tracts of land, at times within several jurisdictions, but function as an integrated operation. Their operations often are conducted, sometimes for various state law and/or regulatory purposes, through use of subsidiaries, affiliates and related parties having different

names, but under common ownership, management or control.[2] These Organizational Systems generally represent themselves to the public, and, in fact, are often viewed by the public, as integrated operations. Frequently, they are publicly known by one name, usually the name of the main operating entity or the Organizational System. Notwithstanding this public perception, bond counsel are often uncertain how to comply with Treas. Reg. § 5f.103-2 in the context of an Organizational System, so may err on the side of concluding that an entity is not an "integrated operation." Accordingly, if there is any doubt that the borrower is an "integrated operation" for purposes of Treas. Reg. § 5f.103-2, the parties are forced to describe the "facility" by multiple street addresses or locations in a cumbersome way.[3]

Additionally, tax-exempt financings for multi-property Organizational Systems often involve large-scale or numerous capital improvements that are to be financed with multiple funding sources. Organizations that benefit from these financings (*i.e.*, the borrowers) are often dependent on sources of funding (*e.g.,* donations, loans and grants from public and private parties) that (i) are not under their direct control, and (ii) are unpredictable as to timing and amounts. Moreover, the extent and nature of the contemplated capital projects can change, depending on these other funding sources. This situation results in greater uncertainty for the Organizational Systems and bond counsel regarding which facilities may ultimately be financed with the proceeds of the obligations and which facilities may need to be included in any notice published under Treas. Reg. § 5f.103-2.

Due to the absence of public administrative guidance concerning what constitutes an integrated operation and the practical considerations relating to funding sources described above, current practice is often to over-state the number of "facilities" in the notice by providing a long list of separate street addresses, the amount of obligations[4] and the name of the controlling affiliate and/or subsidiary to be used to finance each "facility" within the Organizational System. Under Treas. Reg. § 5f.103-2, when this information is identified in the public notice, the borrower is generally considered to be locked into

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[2] Allowing a simpler and broader definition of "facility" for identification purposes in the context of Organizational Systems does not alter the requirement to continue to inform the public of the initial owner, operator or manager of the facility, which is discussed later in this paper.

[3] For example, the location of a medical or university campus or similar large facility may sometimes be described in public notices with reference to adjacent roads (e.g., the campus bounded on the north by X Street, on the west by Y Street, on the south by Z Street and on the east by A Avenue). The problem arises when all properties are not on adjoining tracts of land, but are situated in the same general vicinity. Current guidance is unclear whether the entire campus of a university, though interspersed with book stores or other properties not owned and operated by the university, is part of a single "facility," so long as the outside boundaries are provided; or if a "facility," by means of application of the integrated operation rule, includes dormitories or medical office facilities that are located one block away from the main buildings. Bond counsel typically would err on the side of treating the dormitory or medical office facility as a separate "facility," resulting in separate inclusion in the public hearing notice. The problems multiply as there are more non-adjoining dormitories, offices or other properties.

[4] Especially in response to the recent examinations by the IRS of 'telephone book' TEFRA violations, many tax practitioners provide an amount of obligations to be issued for every non-contiguous building that might be financed. Arguably, this over-inclusive approach does not provide the public adequate notice regarding what is being financed.

the allocation of proceeds to separate "facilities." This approach limits the borrower's flexibility to direct the bond proceeds where needed as the other sources of funds change or are identified. Essentially, a borrower can end up with bond proceeds "siloed" into separate facilities as a result of the public hearing approval process even if, from the borrower's perspective, the various facilities comprise a single, integrated operation. While identification of the "facility" and the amount of bond proceeds applicable to the "facility" is designed to inform the public of the type and extent of a project, the public approval rules should not be a technical trap that removes all flexibility in a complex borrower's operations, if its project and plan of finance otherwise comply with applicable tax laws.

The Study Group recommends that public administrative guidance define an integrated operation to include the facilities of an Organizational System. For Organizational Systems with central headquarters or a center of main operations, ancillary or supporting campuses of the Organizational System can be identified in the public notice without street addresses. These types of Organizational Systems are generally universities with properties, such as dormitories, that may not be located on the main campus or immediately adjacent to it, but are still in the same general vicinity, or hospitals with laboratories, outpatient care and other supporting properties that are close to but not contiguous with the main hospital campus. If these ancillary campuses and the central headquarters are located in different jurisdictions, the host approval requirement in Section 147(f)(2)(A) of the Code (described below) would ensure public notification of these ancillary properties. This clarification would result in a more efficient and potentially more informative application of the public approval rules and remain true to the policy purposes of the public approval requirement by informing the public of the beneficiaries of, and types of facilities being provided with, tax-exempt financing.

To ensure adequate public notice, the Study Group recognizes that when an Organizational System does not have a main site of operations and/or has ancillary facilities of significant size or operational importance, these facilities and their locations should be individually identified. For example, a university system with multiple but significant campuses or a health care delivery system composed of several large, physically separate hospital properties should be separately identified.

II. Post-Approval Changes – "Insubstantial Deviation"

Treas. Reg. § 5f.103-2(f)(2), which specifies the requirements for public notice, also provides that "insubstantial deviation" in any of the required information will not render a public approval invalid. Alternatively, any change in information or mistake in the original notice that is not an insubstantial deviation, will (i) require a new public approval process, if discovered prior to the bond issuance, or (ii) possibly preclude the issuer from proceeding with the revised project, if discovered after bond issuance. Each of these scenarios can be costly and cause delays.

The Study Group recommends that public administrative guidance delineate what constitutes an insubstantial deviation to assist issuers in complying with the public approval rules, while simultaneously reducing costs and delays caused by obtaining

multiple public approvals through an overabundance of caution. The Study Group further recommends that the delineation be in the form of safe harbors or additional examples, such as fact patterns in Private Letter Rulings ("PLRs") issued in these contexts, for each of the public notice content requirements.

A. Description of Facility

The Study Group believes that the description of the facility may be the component of the public notice for which it is most difficult to formulate a safe harbor for interpreting insubstantial deviation. Based on the examples given in Treas. Reg. § 5f.103-2(f)(4), the size specification (such as square footage or number of stories) of a project is not expressly required. But once given, it is uncertain whether, and to what extent, a specification can be changed without affecting the validity of the public notice. For example, in PLR 200703017, a new contiguous property was added to the original facility, and the combined property exceeded the square footage described in the public notice. This change in the facility description was determined by the IRS to be an insubstantial deviation for purposes of the public notification requirements. Because PLRs are redacted, however, the ruling shed no light on what the IRS regards as insubstantial for changes in facility description specifications. To comply with current law, a borrower has more incentive to keep a project description vague, since a more detailed description may limit the type of change a borrower can later make to the project. As noted above, the result is often that the project description is generalized or over-stated. This result is contrary to the stated goal of providing notice to the public.

For more uniform facility descriptions, the Study Group recommends a safe harbor that allows the public notice to state only the category (as listed in Sections 141(e) and 142(a) of the Code) of exempt facility that is being financed with the bonds. No further description of the facility would be required, even though all other elements of the public notice and approval process would still apply. Under this rule, there would be no insubstantial deviation analysis needed. The Study Group believes that the statutory categories are already sufficiently descriptive to adequately inform the public of the nature of the facility. Other elements required in the public notice would complete the process of providing public notification of the nature and scope of the project being financed.

B. Maximum Amount of Obligations

In contrast to the facility description requirement, the Study Group believes the requirement that the public notice list the maximum amount of obligations to be issued for a facility may be the most suitable requirement for which to create an insubstantial deviation safe harbor. Therefore, the Study Group recommends a safe harbor for an insubstantial deviation (*e.g.*, varying the amount of 10% could be automatically considered an insubstantial deviation). Based on a recent PLR, a new use for 20% of the amount of bond proceeds was considered an insubstantial deviation.[5] To avoid

[5] *See* PLR 200049022.

confusion, this safe harbor should reference that the deviation applies to each "facility" described in the public notice, as previously discussed.

C. Initial Owner, Operator or Manager

The Study Group believes that an insubstantial deviation in the name of the initial owner, operator or manager should not be limited solely to typographical errors. As previously stated, many private activity bonds are issued for the benefit of Organizational Systems, which have affiliates, subsidiaries and other related parties, where the actual owner, operator or manager ultimately may be any one of many entities under the system. Additionally, pending negotiations for the operation or management of a facility, these borrowers may intend to enter into agreements with unrelated parties or even other related parties with different names closer in time to completion of the facility (which can be long after the issuance of the bonds). Also possible, single-purpose entities could be formed for the sole purpose of owning the facility, where the name of the entity may not be known (even though the real party in interest is known) at the time of public approval. Under Treas. Reg. § 5f.103-2(f)(2), any change of the entity (including a change of name) identified in the public notice casts doubt on whether the change is an insubstantial deviation, although the new entity and the published entity may be part of the same Organizational System.[6]

The Study Group believes that appropriate safe harbors here should include (i) treating the substitution of the party identified in the public notice with any "related party" (as defined under any applicable Treasury Regulation[7]) or, in the case of nonprofit organizations, any member of the same "controlled group" (as defined in Treas. Reg. § 1.150-1(e)) as an insubstantial deviation; (ii) allowing a listing of the potential controlling owners, operators or managers within the same Organizational System; and (iii) allowing the true party in interest (*e.g.*, the 501(c)(3) organization who is the sole owner of a disregarded single-member limited liability company, as opposed to the limited liability company itself) to be listed, instead of the ultimately named borrower-entity. All of the above provisions will publicly identify the party in interest or the main entity with whom the public is more familiar. The Study Group questions what public purpose is served when a single-purpose entity or a small affiliate with an Organizational System is identified as the initial owner, operator or manager rather than the true party in interest.

D. Location of Facility

The Study Group also believes that an insubstantial deviation in the location or street address of a facility should not be limited solely to a typographical error. Instead, the Study Group recommends a safe harbor that, subject to other conditions, treats an

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[6] This situation is distinguished from the circumstance where the initial owner, operator or manager is not known, in which case, pursuant to Treas. Reg. § 5f.103-2(f)(2), the public notice is considered inadequate. In the interest of public information, the Study Group is not advocating altering this rule.

[7] Currently, 'related parties' are defined in Treas. Regs §§ 1.141-1(d), 1.150-1(b), and 'affiliated persons' are defined in Prop. Reg. § 1.150-1(d)(2)(ii). The Study Group recommends the inclusion of all of these provisions for TEFRA purposes.

incorrect facility location as an insubstantial deviation to the actual location as long as the two are within close proximity of each other. (In addition to the change in the facility description cited above, in PLR 200703017, the new contiguous property that was added to the original facility also had a different street address than that published in the notice, and the IRS treated the difference as an insubstantial deviation. Also, in PLR 8831046, an incorrect address that was one city block from the correct address was considered an insubstantial deviation.) The Study Group recognizes that a close proximity differs between urban and rural areas. For example, half a mile in a densely populated urban area is not comparable to the same distance in an undeveloped area. Therefore, different safe harbors should apply to urban or rural areas. Following the private letter ruling, a city block safe harbor would provide helpful guidance in an urban area, while a safe harbor of a mile would be reasonable in an undeveloped or otherwise rural area. Further conditions could be imposed that the category of exempt facility cannot be different, and all issuer and host approval requirements (as described below) cannot be affected by use of this safe harbor (in the event that the actual facility lies in another jurisdiction).

Public administrative guidance should also focus on what constitutes "same geographical area," a concept introduced by the IRS in PLRs that have provided welcome flexibility for post-issuance changes in the facility. The rulings illustrate how the IRS has interpreted insubstantial deviation in the context of a change in the location of the facility.

For example, in PLR 200050026, the IRS considered the use of a small amount of unexpended proceeds on a parcel of land that was not identified in the public approval as an insubstantial deviation. The IRS noted in that PLR that the new parcel was in the same geographical area as the parcels that were originally identified, and that the borrower and purpose remained the same.

In PLR 200049022, the original hospital borrower was acquired by a hospital system. In connection with the acquisition, the hospital system ceased the operations of the borrower and sought a ruling to permit use of 20% of the borrower's bond proceeds for another hospital that was also part of the system. The IRS determined the new use to be an insubstantial deviation even though one-fifth of the proceeds were to be used by a different hospital and at a new facility, neither of which was listed in the public approval. The ruling stated that both hospitals were located in the same geographical area. This PLR provides a good illustration of the application of the insubstantial deviation exception to accommodate practical circumstances. Project plans and borrower entities sometimes change. These changes are usually not related to the bond issuance and not driven to achieve arbitrage. If the IRS had not agreed to the use of proceeds by the new hospital, the hospital system would have had to issue additional bonds to finance the alternate project, obtain a new public approval and seek some lawful way to account for the unspent proceeds.

The Study Group believes that the incorporation of the PLR examples into public administrative guidance would reduce unnecessary redemptions of prior bonds, issuances of new bonds and the attendant costs, delays and inefficiencies of these actions. However, the Study Group recommends that because these rulings do not provide any

specific factors or guidelines, public administrative guidance should expand on when facilities would be considered to be in the "same geographical area."

III. Hearing and Approval Process

A. Issuer and Host Approval

Currently, Section 147(f)(2)(A) of the Code requires that qualified private activity bonds must have both (i) issuer approval from the issuer or the governmental unit on whose behalf the issuer is issuing *and* (ii) host approval from all governmental units in which the financed facilities are to be located. "Governmental unit" can be as broadly defined as a State, and narrowly defined as a political subdivision. Treas. Reg. § 5f.103-2(d) states that "the location of a hearing will be presumed convenient for residents of the unit if it is located in the governmental unit's capital or seat of government." For a State issuer, this rule is often interpreted to require a hearing in the State capital, where it may have no geographical bearing on the locations of the financed projects. For example, in the context of an incinerator financing with solid waste disposal bonds, the immediate community is most likely to be concerned about the project and bond issuance; however, the wording of Treas. Reg. § 5f.103-2(d) often precludes holding the hearing in the community near the project site, resulting in a hearing in a more distant State capital. While the underlying goal of requiring these approvals is to inform nearby residents and businesses of the project, the current rules governing them often awkwardly serve, if at all, that underlying goal of public notification. Accordingly, the Study Group recommends that public administrative guidance provide explicitly that, while governments may continue to use their capital or seat of government for these hearings, a hearing held in a public location in the more immediate community (*e.g.*, school or another local governmental building in the part of the jurisdiction more proximate to the proposed facility) may also be presumed convenient.

For an Organizational System, such as a hospital system with properties throughout the State that is not using a State-level issuer, obtaining host public approval in every jurisdiction where bond proceeds may be spent, regardless of whether proceeds will actually be spent there, may be burdensome and expensive. Likewise, a borrower that does not expect to, and in actuality does not, spend a substantial amount of proceeds on a facility may face burdensome approval requirements relative to the proceeds spent. Therefore, the Study Group recommends that issuer approval and "limited" host approval be the only requirements in these instances. "Limited" host approval should include the State capital or jurisdictions where a substantial amount of bond proceeds is expected to be, and will be, spent on a project. "Substantial" should be defined as at least 10% of the maximum amount of the bond issue.

B. Communication of Public Notice

Under Treas. Reg. § 5f.103-2(g)(3), a "reasonable public notice" means that it (i) be communicated no fewer than 14 days prior to the hearing for purposes of the issuer and host approvals of the facility; (ii) be published in at least one newspaper of general

circulation available to residents of the applicable locality or announced by radio or television broadcast to those residents for purposes of the host approval of the facility, and, (iii) be given in the same manner and locations as required by the approving governmental unit for any other purposes for which applicable State or local law specifies a notice or public hearing requirement for purposes of the issuer public approval of the facility.

The Study Group recommends that, if applicable State or local law exists, then it be made a safe harbor regardless of whether the public approval is an issuer or a host approval. Thus, publication requirements for all public approvals would be presumed met if they complied with *either* applicable State or local law *or* the current 14-day newspaper safe harbor. Deference should be given to a local entity's regular process of hearing and approval, with the presumption that local officials are in the best position to ensure that residents receive proper notice and the opportunity to be heard.

Further, given the tremendous technological advances made over the last two decades and the high costs associated with both newspaper publication and radio/television broadcasting, the Study Group recommends that some form of electronic publication, which is relatively cost-free, should be adopted. This change would be consistent with other recent federal law changes, such as the allowance of electronic submission of tax filings and the mandate for use of SLGSafe (*i.e.*, requiring the electronic submission of subscriptions for the purchase of United States Treasury Securities - State and Local Government Series). Since the last consideration of the public approval requirements, State and local jurisdictions have changed and expanded their methods for publication of similar notices, and any public administrative guidance issued pursuant to Section 147(f) of the Code should reflect these advances. In fact, local newspapers are decreasing in number and effective reach, while radio channels have multiplied and expanded in areas, so that choosing just one can be difficult. Even a large circulation newspaper, such as one that serves a county or even several counties, may not provide proper notice to residents within a particular city.

For a State or local government that regularly provides information to its residents via a web site, the Study Group recommends that reasonable public notice requires publication under the existing methods (*i.e.*, newspaper), but with a general notice that bonds are to be issued and that specific information is available on the government's web site. If desired, this provision could be applicable only for issuers which customarily provide public notices via their web sites. To illustrate, a notice published on the governmental entity's official web site in a location where similar notices are published, plus a short newspaper publication referring the public to the applicable web address for details and a telephone number for those without Internet access, would be sufficient.

Note that this recommendation can be distinguished from PLR 8411077 (where the IRS found inadequate a notice which provided only that information regarding the project was available upon request), because the communication landscape has changed dramatically since the 1984 release date of that PLR.

The Study Group believes that public administrative guidance encompassing these recommended changes would put public notices for purposes of Section 147(f) of the Code on the same level as other public notices issued by a particular governmental unit, which could serve the goal of most efficiently and effectively informing the public.

C. Supplemental or Corrective Notice

The Study Group recommends that public administrative guidance provide a means for correcting or supplementing a published notice where the defect is discovered prior to the hearing date. For example, if the original notice were published 14 days prior to the hearing date and two days later a defect was discovered, rather than canceling the hearing and restarting the public approval process, the Study Group recommends that an issuer have the option to publish a correction notice. The allowance of a corrective notice could apply to the same items as covered by insubstantial deviation and be published up to three business days before the hearing date. A correction notice could also be allowed for changes to the date, time or location of the public hearing and be published no fewer than three business days prior to the ultimate hearing date.

IV. Public Approval for Pooled Financings

The Study Group recognizes that pooled financings, mainly blind pools, where the initial borrowers are not known at the time of debt issuance, have been under recent scrutiny. In those pooled financings that were subject to the TEFRA requirements, the lack of information (specifically, the identity of the borrowers) called into question the reasonableness of the governmental issuer's expectations.[8] For pooled financings subject to TEFRA requirements, the Study Group believes that, with the proper administrative tools, parties could provide more accurate information on the borrowers and the projects, in order to more effectively inform the public.

Currently, Treas. Reg. § 5f.103-2(f)(2) states that a notice of public hearing will be considered inadequate, if any of the required information is unknown on the date of the approval. In certain pooled issuance deals, unknown information is a possibility. The Code provides an exception for pooled 501(c)(3) financings to the maturity limitation of Section 147(b). Moreover, the Study Group notes that the General Explanation of the Tax Reform Act of 1986, dated May 4, 1987, by the Joint Committee on Taxation of the U.S. Congress (the "Bluebook"), contemplates, in certain instances, the possibility of financing projects that are not initially identified in a public notice.[9] The Bluebook

[8] Recent 2006 tax legislation provided further guidance and restrictions on pools regarding this concern. As set forth in Section 508 of the Tax Increase Prevention and Reconciliation Act of 2005, Public Law 109-222, May 17, 2006, changes to the Code provided more structure to pooled bond financings by, among other matters, strengthening the reasonable expectations requirement, and requiring written loan commitments and redemptions for un-loaned proceeds.

[9] In the context of Section 147(b)(4) of the Code, the Blue Book, at page 1219, states, in part, that "Congress recognized that the prior-law IDB public approval requirements required identification of specific facilities. (See, Temp. Treas. Reg. sec. 5f.103-2.) In extending this requirement to all private activity bonds, Congress intended that the applicable Treasury regulations will be amended for…qualified

specifically references pooled 501(c)(3) financings as financings where not all property to be financed need be identified before issuance of the bonds.

The Study Group recommends that published guidance be consistent with the Bluebook. Specifically, to enhance public information goals, the Study Group recommends the allowance of (i) a pre-issuance public approval of the general project types and obligations amounts, and (ii) a post-issuance, but pre-expenditure public approval of the specific projects being financed. To illustrate, the bond issue as a whole -- with a description of the type of project to be financed -- would be publicly approved, and the bonds would be issued. Then, as the various projects became known, their specific locations, owners, etc., would be publicly approved (or disapproved) prior to expenditure of the bond proceeds on the individual projects, and the bond issue would ultimately have multiple hearings and approvals.

V. Post-issuance Public Approval

As a final issue, the Study Group notes that one of the most common problems in practice is meeting the public approval requirements when a project (or other matters related to the project) changes after the bonds are issued. Especially troublesome are those changes that do not fall within the remediation rules under Treas. Reg. § 1.141-12.[10] Practitioners have considered the option of forcing a re-issuance of the issue, thereby qualifying the issue for another public approval. However, whether this method is valid remains unclear, and, regardless, it is cumbersome, expensive and inefficient.

As previously stated, plans change after bond issuance for a variety of reasons related to normal operating circumstances. The nature and scope of projects can change, and costs related to the projects often change accordingly. Savings in the costs of the project can result in unexpended proceeds for which a borrower has legitimate tax-exempt purposes but for the lack of public approval. Above, the Study Group has recommended public administrative guidance with respect to the delineation of insubstantial deviation and the definition of facility, which it believes would partially reduce this complication. However, recognizing the limitations of the statutory language, the Study Group further recommends that public administrative guidance accommodate, to the extent possible, certain post-issuance public approval where unexpected events occur, subsequent to the issuance of the bonds that results in proceeds being allocated in a

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501(c)(3) bonds that qualify for special exception to the maturity limitation for pooled financings (where the facilities need not be identified before issuance of the bonds)."

[10] For example, if a hospital sells a facility to another nonprofit organization, bond counsel can apply the provisions of Treas. Reg. § 1.141-12 to have a new public hearing and deemed reissuance of the bonds, which would permit any changes to be made to the project definition and/or redirect any unspent proceeds. In contrast, other transactions between nonprofits do not fall within the provisions of Treas. Reg. § 1.141-12, since there are no "disposition proceeds" and no "deliberate action," so these beneficial rules would not apply.

manner not in compliance with the public approval requirements of Section 147 of the Code.[11]

VI. Summary

For several years, NABL has maintained the view that legislative or regulatory simplification of the public approval requirements for private activity bonds is essential. The Study Group has made recommendations for public administrative guidance to clarify terms such as "facility" and "integrated operation" in relation to complex organizations and projects; to delineate "insubstantial deviation" in relation to post-approval project changes; to streamline notice requirements in relation to new technologies; to provide for an alternate process, combining both pre-and post-issuance approvals, in relation to certain pooled financings; and to accommodate, to the extent possible, post-issuance approval. These recommendations should provide efficiency and cost effectiveness for issuers, practitioners and the IRS, as well as adequate notice of private activity bond issuances for the public.

[11] The Study Group recognizes that a conforming change to Treas. Reg. § 1.147-2 to delete the reference to bonds requiring public approval would be necessary.

EXHIBIT I

Excerpt from NABL's "Tax Simplification Recommendations to Treasury on Tax-Exempt Bonds," dated June 14, 2002.

Specific Recommendations to Cut Back on Various Interim Restrictions Applicable to Most Tax-Exempt Private Activity Bonds.

1. Repeal or Significantly Simplify the Section 147(f) TEFRA Public Approval Requirement.

Our primary recommendation here is to repeal the TEFRA public approval requirement under Section 147(f) entirely. Although one is hard-pressed to object in theory to a good government "sunshine" policy in favor of public hearings and public approval (akin to mom, home, and apple pie), the reality is that most affected State and local governments and our members believe that this public approval requirement is costly, cumbersome, and ineffective. These required public hearings and public approvals have been virtually ignored by the general public at which they are aimed. It is fair to say that this requirement has long outlived its original purpose in 1982 of helping to control private activity bond volume. State procedures for obtaining volume cap serve the necessary role of providing a political check against any rare controversial projects. State volume cap allocation procedures have or presumably could incorporate a process to allow for public comment on potential volume cap allocations to address the "not in my back yard" or "NIMBY" issue.

In the 2001 Joint Tax Study, the Joint Tax Committee had several good recommendations, albeit limited, to simplify the public approval requirement. The Joint Tax Committee sensibly recommended alternative, less costly, forms of public notices, such as Internet notices. This idea could streamline the procedure and reduce the costs of public notices, particularly for large Statewide bond issues with many projects. The Joint Tax Committee also sensibly recommended permitting alternatives to public hearings, such as public comments in writing or by Internet. We concur with these recommendations.

Short of the preferred complete repeal of the Section 147(f) public approval requirement, we recommend simplifying the Section 147(f) public approval requirement to the fullest extent possible. We submit that much simplification of the Section 147(b) public approval requirement could be accomplished through regulations, given that many of the excessive details reside in old regulations in this area. In particular, we offer the following recommendations to simplify the public approval requirement. First, consider excluding refundings completely from this requirement because the public approval for the original new money financing duly addresses the nature of the financed project and the 120% economic life test under Section 147(b) duly addresses the burden on the tax-exempt market of the refunding. Second, consider giving more deference to State

sunshine laws on the adequacy of various aspects of the public approval process. In many instances, these laws will be more than enough. Third, consider providing more flexibility to allow delegations of approval authority to particular State or local public officials below the "highest elected representative" to reduce the challenges of tracking down busy governors and mayors to sign these public approvals. Fourth, consider expressly permitting "post-issuance" amendatory public approvals to cure changes in the described nature and location of the financed project and, for qualified 501(c)(3) bonds, to address projects unknown at the time of the original tax-exempt bond issuance. Finally, consider replacing the old "insubstantial deviations" standard for project changes without new public approvals under Treas. Reg. §5f.103-2(f)(2) with a much stronger standard that requires new public approvals only if the fundamental nature and location of the project change.

National Association *of* Bond Lawyers

EXHIBIT II

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Attachment B

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October 15, 2008

Internal Revenue Service
CC:PA:LPD:PR (REG-128841-07) Room 5203
PO Box 7604
Ben Franklin Station
Washington, DC 20044

RE: REG-128841-07: Public Approval Guidance for Tax-Exempt Bonds

Ladies and Gentlemen:

The National Association of Bond Lawyers (NABL) respectfully submits the enclosed comments on the proposed regulations on public approval guidance for tax-exempt bonds published September 9, 2008, and corrected October 8, 2008.

NABL appreciates the significant effort of the Department of the Treasury and the Internal Revenue service in the preparation of the proposed regulations.

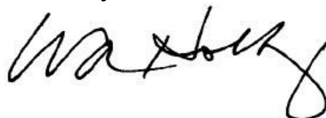
Primary drafting responsibilities for these comments were assumed by Frederic L. Ballard, Jr., Scott R. Lilienthal, and Perry E. Israel.

NABL believes that participating in the guidance process supports clarification of and facilitates compliance with the tax law and regulations. Accordingly, NABL members would welcome the opportunity to discuss these recommendations to achieve clarity, certainty and administrability in this area of the law.

If you have any questions, please contact Frederic L. Ballard, Jr., at 202-661-2210 or through email at flb@ballardspahr.com.

Thank you again for the opportunity to submit NABL's comments.

Sincerely,



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RECOMMENDATIONS BY THE
NATIONAL ASSOCIATION OF BOND LAWYERS
TO THE
DEPARTMENT OF THE TREASURY
OFFICE OF TAX POLICY
AND THE
INTERNAL REVENUE SERVICE
REGARDING
PROPOSED REGULATIONS ON PUBLIC APPROVAL GUIDANCE
FOR TAX-EXEMPT BONDS

OCTOBER 15, 2008

The National Association of Bond Lawyers ("NABL") submits the following comments on the proposed regulations concerning the public approval requirement under section 147(f) of the Internal Revenue Code (the "Code") published in the Federal Register on September 9, 2008, and corrected on October 8, 2008 (the "Proposed Regulations"). The comments were prepared by members of a NABL task force who are identified on an attachment.

General Comments

NABL thanks the Department of the Treasury (the "Treasury") and the Internal Revenue Service (the "IRS") for the flexibility and practicality of the Proposed Regulations in dealing with many specific problems that arise for bond issuers and bond counsel in complying with the public approval requirement. Given that the public approval requirements apply generally to all forms of private activity bonds issued under sections 142, 143, 144, or 145 of the Code, the Proposed Regulations are clearly of great importance to NABL's members and their clients. While NABL does have comments, NABL hopes that the comments will not obscure the basic appreciation of NABL for the various policy decisions reflected in the Proposed Regulations. NABL applauds particularly the addition of the post-issuance remedial action procedure for correction of deviations between a granted approval and subsequent events. And more broadly, NABL congratulates the Treasury and the IRS on the “principle-based” approach of the Proposed Regulations, which are a model for other future rule-making concerning tax-exempt bonds.

The Explanation of Provisions (the "Explanation") that accompanied the Proposed Regulations recognizes that several categories of bonds became subject to the public approval requirement for the first time as a result of the Tax Reform Act of 1986, such as qualified mortgage bonds ("QMBs") or qualified student loan bonds ("QSLBs"), and that the pre-1986 public approval regulations in Treas. Reg. §5f.103-2, being appropriately “facility-focused” as required by the pre-1986 application of the public approval

requirement to various forms of exempt facility bonds or small issue manufacturing bonds, provided no specific guidance for "portfolio loan" financing using QMBs or QSLBs or in certain other situations that became subject to the public approval requirement in 1986. The Explanation states that an issuer of these post-1986 bonds that made a "good faith effort" to comply with section 147(f) of the Code and Treas. Reg. §5f.103-2(f)(2) will not be subject to audit by the Service "merely because the issuer did not include all of the information required to be included in the public notice and public approval" under §5f.103-2(f)(2). This principle of giving effect to good faith efforts at compliance is of course welcome. NABL suggests that the principle is so important that it ought to be included in the text of the final regulations in a number of specific contexts as well as in the transitional rule in the manner suggested in the Explanation.[1] While a general statement of a good faith rule would be helpful, there are specific contexts in which it may be particularly relevant, as indicated by the presence of a reference to good faith in certain of the comments below.

Specific Comments

Preservation of pre-1986 regulations (Prop. Treas. Reg. §1.147(f)-1(a)). The Proposed Regulations state that to the extent not inconsistent with the Proposed Regulations, the pre-1986 regulations (Treas. Reg. §5f.103-2) continue to apply. NABL recommends that with exceptions noted at the end of these comments, the substance of the pre-1986 regulations in matters not addressed by the Proposed Regulations be brought forward into the final regulations so that bond issuers and bond counsel are not faced with the need to review two sets of regulations on the same subject and decide to what extent they are consistent with each other. Provisions in Treas. Reg. §5f.103-2 that NABL believes should be modified in addition to the changes made by the Proposed Regulations are indicated at the end of these comments.

Information required in public notice relating to the facility (Prop. Treas. Reg. §1.147(f)-1(b)(2)(i)). The Proposed Regulations (similar to the existing regulations) require a "general functional description" of the use of the facility financed with the issue, but also add new language making it easier to satisfy this standard. NABL appreciates the flexibility provided in the Proposed Regulations, including the ability to satisfy the requirement by making reference to a specific category of exempt facility bond.

Maximum stated principal amount of bonds (Prop. Treas. Reg. §1.147(f)-1(b)(6)(ii)). NABL recommends the addition of a statement that in the case of a multipurpose issue, the notice and approval do not need to allocate the amount of the issue between the various facilities or purposes of the issue. The statutory requirement of approval of the issue is satisfied by a notice and approval of the estimated amount of the issue as a whole and does not require a breakdown or itemization of different portions of the issue, other than in the case of post-issuance pooled financing approvals as discussed below.

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[1] There is precedent for the use of a "good faith" standard in the context of tax-exempt bonds. See, e.g., Temp. Reg. §6a.103A-2(c), relating to single family housing bonds.

Initial owner or principal user (Prop. Treas. Reg. §1.147(f)-1(b)(2)(iii)). The Proposed Regulations require the notice and approval to state the "expected initial owner or principal user" of the facility or the name of the "true beneficial party of interest for such legal owner or user," such as a 501(c)(3) organization that is the sole member of a limited liability company that owns the facility. "Principal user" is defined in turn by reference to the rules for aggregation of capital expenditures and prior bond issues in measuring the compliance of a "small issue" with the dollar limits of section 144(b) of the Code. Those rules provide generally that a user of 10% or more of a facility may be treated as a principal user, so that there could be up to 10 principal users (generally, tenants) in addition to the owner of a facility. In situations where there are multiple parties who could be listed, NABL recommends that language be added stating that the requirement as to names of parties may be met by naming one or more of the parties in a manner intended in good faith to carry out the purposes of section 147(f) of the Code.

Location of the facility (Prop. Treas. Reg. §1.147(f)-1(b)(2)(iv)). NABL supports the provision in the Proposed Regulations stating that issuers may identify multiple capital projects located on the same, adjacent, or proximate sites, and notes that this is consistent with what has long been the practice with respect to hospital and university campuses. NABL notes that, in addition to identification of the various boundary streets, it is often just as informative to identify a campus solely by its main address, and recommends that the final regulations include such an option as an alternative to identifying what may be numerous boundary streets. In addition, NABL also recommends that the final regulations provide additional flexibility in identifying the general location of a facility where the project is located over a widespread area, such as a privately operated water supply system or properties purchased with the proceeds of qualified redevelopment bonds.

In one or more recent audits of 501(c)(3) Bonds involving improvements at multiple locations, an issue was raised as to whether the public notice had to set forth the maximum amount of proceeds to be used with respect to each location. NABL does not believe that the maximum amount of proceeds to be used with respect to each location needs to be specified. Either the preamble to the final regulations or the text of the final regulations should state that for a bond issue financing improvements for multiple locations, it is not necessary to specify the dollar amount at each location in the public notice and public approval.

Special rules for mortgage revenue bonds and qualified student loan bonds (Prop. Treas. Reg. §1.147(f)-1(b)(3) and (4)). NABL is concerned that the Proposed Regulations appear to require that the notice and approval for QMBs or QSLBs specifically cite section 143 or section 144. NABL recommends that the language be revised to eliminate any inference to this effect. A required citation of Code sections would not further the purposes of section 147. For example, in a public notice of QMBs, NABL believes that it would be more meaningful to say that the bonds are being issued to finance residential mortgages than to say that the bonds are to be issued under section 143. Also, in the case of qualified student loan bonds, it seems unnecessary to require that the notice and approval indicate whether the issue will be for Federally guaranteed loans or unguaranteed "state supplemental" programs: both types of financing are portfolio loan

financings for student loans and NABL believes that they should not have to be further categorized in this technical manner. Further, § 1.147(f)-1(b)(3) should also apply to refinancings of obligations issued to finance single family mortgages to which section 143 of the Code or section 103Aof the Internal Revenue Code of 1954 do not apply. This could be accomplished by an amendment to the definition of "mortgage revenue bond" in § 1.147(f)-1(c)(F).

Post-issuance public approvals (Prop. Treas. Reg. §1.147(f)-1(b)(5)(ii)). NABL applauds the two-part approval process provided in the Proposed Regulation for certain qualified 501(c)(3) bonds issued to finance pools described in section 147(b)(4)(B). NABL believes the approach taken is an intelligent and effective way to deal with the problem of identifying projects in pools. Moreover, in response to the request in the preamble to the Proposed Regulations, NABL recommends that the two-step process be adopted in other situations involving pools, such as pools for multi-family rental housing projects or enterprise zone facility bonds (without regard to the implication in § 1.1394-1(p) example 6 that some of the facilities must be described in the initial approval). NABL also recommends that the final regulations make it clear that a second, post-issuance approval is not required for the initial use of the proceeds to the extent that the projects are identified in the pre-issuance public notice and approval. Finally, NABL notes that, in describing the characteristics of the post-issuance approval before each loan from a pooled issue of 501(c)(3) bonds, the Proposed Regulations require the issuer to treat the bonds that finance each loan as if they were reissued for purposes of the public approval requirement. NABL recommends that the regulations indicate specifically whether for this purpose the bonds to finance any particular loan include a share of the portion of the issue used to finance a common reserve fund or common costs of issuance.

Deviations in public approval information (Prop. Treas. Reg. §1.147(f)-1(b)(6)). NABL applauds the attempt in the Proposed Regulations to provide guidance on what constitutes an “insubstantial deviation” for purposes of the approval requirements. However, NABL suggests that the proposed standard of 5% of “net proceeds” be modified in certain respects. On a technical level, NABL believes this standard should refer to the principal amount of the issue rather than net proceeds, in order to conform with the underlying requirement for the notice and approval. And more broadly, the standard for deviations should be measured against the purpose of the approval process, which we believe is to state and approve potential uses and maximum amount of the issue, rather than to create an affirmative commitment as to particular uses or sizing. In this light, NABL recommends that the final regulations state as a general matter that it is not a substantial deviation (i) to issue fewer bonds than stated in the approval (even if the reduction is more than 5%), (ii) to delete from a multipurpose issue one or more projects identified in the approval, (iii) to redirect proceeds between the different purposes covered by a multipurpose issue (since only the total amount of the issue should be required in the approval in any event), or (iv) to redirect proceeds from approved facilities to working capital for an activity conducted in whole or in part at the approved facilities, or (v) to redirect the “insubstantial deviation” amount from approved facilities to some other facility not covered by the approval. NABL believes that these rules would provide issuers with needed flexibility without materially affecting the reasonableness of the notice and approval. In addition, NABL recommends that the final regulations clarify

that the facts and circumstances that are relevant in determining whether a deviation is substantial should include whether the issuer has made a good faith effort to carry out the purposes of section 147(f). Finally, with respect to deviations from the project as described in the notice, NABL believes that it is probably more accurate to refer to deviations between the notice and the actual *use* of the proceeds rather than to deviations between the notice and the actual *information*.

Working capital (Prop. Treas. Reg. § 1.147(f)-1(b)(6)). NABL has recommended, in the prior paragraph, that reprogramming funds from approved facilities to working capital be treated as an insubstantial deviation. The use of unspent proceeds from a construction or acquisition fund or, with bondholder permission, from a reserve fund to pay working capital costs may be essential to avoidance of default in many distress situations. The initial public hearing and approval as to the bond-financed facility is sufficient to satisfy the legislative purpose of section 147(f). The Service recognized this in Private Letter Ruling 9452021.

Substantial deviations (Prop. Treas. Reg. §1.147(f)-1(b)(6)(iii)). NABL cannot express strongly enough our support of the ability to correct unexpected problems that arise after the issue date. The ability in those cases to do a supplementary public notice and approval will allow issuers to redirect the use of those funds without incurring the additional costs of redeeming the bonds and issuing new bonds to finance the alternative projects. NABL views this as being the most important and most helpful proposal in the package. With that in mind, NABL does have relatively minor recommendations for improvement. First, NABL believes that the unexpected events or changes in circumstances that can be cured by a remedial public approval should also include changes in the initial owner or user of a facility. This recommendation would only be necessary in the case in which proceeds have not been expended on the facility so that there is in fact no initial owner or user. Once there has been an expenditure of proceeds, there is an initial owner/user who has benefited from the expenditure. At that point a change in the owner/user would not invalidate the existing approval, since the new owner/user will not be the initial owner/user. In order to create a workable and simple rule, NABL recommends that the final regulations clarify that the status of an initial owner/user as such comes into effect as soon as a specific, bright-line percentage of the proceeds have been expended: NABL recommends 5% of proceeds (net of proceeds deposited in reserve funds or spent on costs of issuance).

Second, the Proposed Regulations state that the standard for use of the remedial approval is that either the originally approved use is no longer feasible or viable, or that the cost of the facility was less than expected. NABL suggests that this standard be liberalized to give issuers and borrowers more flexibility. An issuer or borrower should be permitted to use the proceeds for projects with more pressing needs (e.g., where exigent circumstances warrant a re-prioritization of a capital improvement program or a need for an unforeseen capital improvement arises). For example, assume that a borrower plans to build a new hospital and bonds are issued but a exigent need for an unforeseen clinic arise at a different location arises). The borrower should be allowed to use the proceeds for the clinic provided a remedial public approval is obtained.

Timing requirements (Prop. Treas. Reg. § 1.147(f)-1(b)(7)). The timing requirements section is incorrectly cited as (8) rather than (7) in § 1.147(f)-1(b)(1) and § 1.147(f)-1(b)(5)(i).

Definition of facility (Prop. Treas. Reg. §1.147(f)-1(c)(1)). In general, NABL supports the newly revised definition of facility and the manner in which it includes working capital and portfolio financings, such as QMBs and QLSBs. In addition, NABL recommends that the final regulations include the concept stated § 5f.103-2(f)(4) of the existing regulations to the effect that separate tracts of land (including improvements and personal property) may be treated as a single facility if they are used in an "integrated operation").

Definition of public hearing (Prop. Treas. Reg. §1.147(f)-1(c)(2)). NABL supports the ability to cancel a public hearing if there are no timely requests to participate in the hearing. However, NABL requests clarification as to whether the notice of public hearing must indicate that the hearing may be cancelled without notice if no timely request to participate are received. NABL also requests clarification on how to address situations where timely requests to participate are not received by the issuer (e.g., a failed email or a late receipt of a regular mailing) in the context of a cancelled hearing due to no timely requests to participate Once option is to allow the public hearing requirement to be satisfied by providing notice for the cancellation of a public hearing in the same manner as the initial hearing notice was given (but with a limited time requirement (e.g., cancellation notice provided at least 48 hours prior to the hearing).

NABL appreciates the regulatory language allowing the hearing to be conducted by an appointed or employed individual or by the issuer. NABL recommends the addition of language clarifying that if the hearing is conducted by the issuer, the applicable procedural rules would be those that apply to the issuer (as distinguished, for example, from the rules that would apply to a county on behalf of which the bonds will be issued).

Definition of reasonable public notice (Prop. Treas. Reg. §1.147(f)(-1(c)(3)). NABL applauds the extension of reasonable methods of providing notice to include notice provided electronically and on websites. NABL recommends that the language of 1.147(f)-1(c)(3)(iii) be modified to clarify that, while it is necessary that "the governmental unit regularly uses that web site to inform its residents about events affecting the residents (including notice of public meetings of the governmental unit)," it is not necessary that state law allows such notice alone to be sufficient. Use of active web sites for public notice should be allowed under section 147(f) even in states which may still require paper publication. NABL believes this is an appropriate recognition of the way governments generally operate today. NABL also supports the reduction of the required notice time. However, we note that "business days" is not a concept that is uniform across different jurisdictions. NABL recommends that the notice time be reduced to 7 days (or, in the alternative, to 10 days) rather than 7 business days. Also, with respect to publication on a website, NABL notes that questions may arise as to the appropriate website on which to post the notice. For example, should the publication be on the issuer's website or on the website of the governmental entity on behalf of which

the issuer is issuing? NABL recommends clarification in the final regulations that the notice must be posted on the issuer's website. NABL would also recommend that the public posting of notices at one or more designated locations be recognized as an acceptable alternative to phone recordings. Many smaller issuers will not want to incur the expense of establishing a phone recording system when the issuer may hold very few public hearings each year.

Special rule on governmental approvals (Prop. Treas. Reg. §1.147(f)-1(d)). NABL applauds the proposed rule limiting the required governmental unit approving the issue to the issuer in the case of mortgage revenue bonds, qualified student loan bonds, and working capital financings for qualified 501(c)(3) bonds.

Effective date (Prop. Treas. Reg. §1.147(f)-1(e)). The effective date provision of the Proposed Regulations states that the final regulations will apply to bonds sold on or after the date of publication of the final regulations. NABL hopes that final regulations, modified to reflect the NABL comments, will be adopted promptly. At the same time, to protect the status of public approval proceedings prior to the date of publication of final regulations, we recommend that the final regulations be made effective for bonds issued on or after the date of publication of the final regulations pursuant to public approvals granted on or after the date falling 30 days after the date of publication. To illustrate the problem, assume that a "plan of finance" notice and approval were carried out in 2007 to cover three years of issuance of qualified mortgage bonds by a state housing finance agency. Assume also that the Proposed Regulations are adopted as final regulations in their current form in 2008. The effectiveness of the notice and approval for bonds sold subsequently to the date of the final regulations should not be affected by whether the notice and approval contain a reference to section 143, as may be required by the Proposed Regulations. NABL also recommends that the final regulations be effective on an elective basis to bonds issued prior to their publication. This would make the ability to do a post-issuance correction in the event of unexpected circumstances available to previously issued bonds.

The rule in existing Treas. Reg. § 5f.103-2(b)(1) dealing with refunding issues, which generally imposes a bond-by-bond approach in determining whether the refunding results in an extension of maturity necessitating a new TEFRA approval, was made obsolete by statutory changes enacted by the 1986Act as provided in section 147(f)(2)(D) of the Code, which instead compares the average maturity of the issue of which the refunding bond is a part to the average maturity of the bonds to be refunded. NABL recommends that the final regulations clarify that for this purpose the average maturity of a refunding issue will be considered not later than the average maturity of the bonds being refunded if the amount and date of the maturities or mandatory sinking fund installments of the refunding issue are not larger or later than those of the refunded bonds, provided that the bonds have no more than a de minimis original issue discount or premium. The recommended rule will avoid the difficulties that arise if the maturities of the refunding issue match exactly the maturities of the refunded bonds but the longer maturities of the refunding issue are sold at a premium, thus creating an extension of average maturity under a literal application of the requirement that average maturity be determined by reference to issue price in accord with section 147(b). Limiting the

recommended rule to cases where the premium is de minimis will protect against abuse of the rule in extreme cases.

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Attachment C

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