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Integrity in Our Municipal Markets

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America Was #BuiltByBonds

118th Congress Policy Platform

Above all else...

Congress and the administration should reject efforts to eliminate or reduce the tax exemption on municipal bond interest. Holders do not pay federal income taxes on interest paid on qualified municipal bonds, which reduces the interest costs for state and local borrowers. **Any effort to reduce or eliminate the tax exemption would result in increased borrowing costs**, forcing state and local governments to either cut back infrastructure investment or raise taxes.

Four Ways to Support Municipal Finance

Municipal bonds have a proven track record as an effective tool for state and local governments to finance critical infrastructure, but there are several ways in which federal policymakers can further expand and strengthen these tools:

1 Modernize financing options available to our smallest communities.

Banks generally cannot deduct the borrowing costs of holding tax-exempt securities but may deduct up to 80 percent of the carrying costs of securities from "qualified small issuers" that issue less than $10 million in a calendar year per section 265 of the Internal Revenue Code (IRC). This exemption allows smaller communities to access tax-exempt rates more easily through bank placements and reduces their financing costs. These small issuers typically save between an estimated 25 – 40 basis points per transaction.[1] The current $10 million threshold was set in 1986 and is no longer enough to finance most projects even in smaller communities. By raising the threshold, indexing it to inflation, and applying it to the borrower instead of the issuer, Congress and the administration can help small communities, as well as nonprofits, reduce borrowing costs for critical infrastructure projects.

2 Expand financing options for innovative and critical projects.

Many capital projects with a private use provide essential public benefit, such as airports, seaports, waste disposal facilities, housing, 501(c)(3) institutions, and many more. A private activity bond (PAB) is a bond issued to finance a facility that includes some private use, through ownership, management agreements, a lease, or another economic interest in the facility. The Internal Revenue Code (IRC) provides specific categories of PABs that may qualify to be issued on a tax-exempt basis due to the public benefit they offer. In certain instances, the volume of qualified PABs a state is allowed to issue each year is capped. States frequently reach their volume cap well before the end of the year—limiting access to financing opportunities for innovative and critical infrastructure projects and public-private partnerships. By expanding certain categories of PABs and raising state volume caps, Congress and the administration can leverage greater investment in national infrastructure projects.

3 Allow our communities to once again refinance at lower rates.

For decades, state and local governments were able to refinance outstanding debt by issuing a tax-exempt advance refunding bond to pay off another previously issued bond. Typically, the new refunding would allow the issuer to achieve a lower interest rate and generate savings to the issuer and taxpayer. Between 2007 and 2017, issuers used advance refundings to save more than $18 billion.[2] While issuers can still use current refunding bonds within 90 days of the call date, reallowing issuers to issue tax-exempt advance refunding bonds beyond that window would permit state and local governments to take advantage of favorable interest rate environments, save tax dollars, and reinvest savings in additional infrastructure.

4 Equip our communities with a new financing tool.

During the Great Recession, Congress temporarily authorized a direct pay bond program known as Build America Bonds, or BABs. Interest paid on these direct-pay bonds is taxable to the bondholder, so the interest rate is higher than a tax-exempt rate. The federal government, however, pays an amount equal to a percentage of the interest payable on the bonds directly to the issuer of the bonds, effectively reducing the financing cost of the project funded by these bonds. The subsidy reduces the cost of financing infrastructure for state and local governments, while the taxable rates broaden the purchaser base by attracting new investors who would not otherwise be interested in tax-exempt bonds. By creating a new iteration of direct-pay bonds, Congress and the administration can add an additional, efficient, and tested financing tool for state and local governments.

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[1] The Government Finance Officers Association (GFOA). "Bank Qualified Debt." Web access: https://www.gfoa.org/bank-qualified-debt

[2] GFOA. "Advance Refunding Myth Buster." Web access: https://www.gfoa.org/advance-refunding-issuance

About NABL

The National Association of Bond Lawyers (NABL) is a specialty bar association of approximately 2,500 lawyers who represent municipal market participants, including: state and local government issuers, nonprofit and other conduit borrowers, underwriters, investors, and trustees.

Resources

- **Need the basics?** Our Bond Basics series provides the public with plain-English explanations of hundreds of concepts relating to municipal bonds. **www.nabl.org/basics**
- **Looking for deeper dives?** Our resource hub features more than 350 documents, including reports, comment letters, and issue briefs on topics relating to bond law. **www.nabl.org/resources**
- **Support the Municipal Market?** Our advocacy center tracks federal policy issues of importance to the municipal market as well as provides deeper explanations of policy initiatives to support financing tools for our communities. **www.nabl.org/advocacy**

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Here to Help We collectively serve as a brain trust on all things related to public finance and municipal bond law. Our members throughout the country and professional staff based in Washington, D.C. are committed to promoting sensible public finance policy.

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