Private Activity Bond Tests

Real World Challenges

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OCTOBER 18–20, 2023

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Agenda

- Allocation and Accounting Rules
- Change in Use
- Tax Increment Financings
- Electric Vehicle Charging Stations

The Panel will be hypo-based with the black letter and/or guiding principles layered throughout the discussion of the hypotheticals

Allocation and Accounting Rules Hypothetical

MetroCity owns 50 acres of undeveloped land on the edge of its downtown district. The land is dedicated parkland, which can be used only for recreational and cultural purposes. The adjacent area includes the campus of a university that is a 501(c)(3) organization, a bustling shopping and entertainment district and several new office towers.

MetroCity formed a membership corporation under the State's local development corporation law to develop the land ("CiviCorp"). CiviCorp has 7 members, consisting of the Mayor of MetroCity and 6 additional members appointed by the Mayor of MetroCity, 2 of whom are nominated by the MetroCity Council, 2 of whom are nominated by the president of the University and 2 of whom are nominated by an association of business owers in the shopping and entertainment district.

Allocation and Accounting Rules Hypothetical

On January 1, 2013, MetroCity issued a 4-year taxable note in the amount of $50 million, which was used to finance the core and shell of a new 30,000 square foot performing arts center and the fit-out of a 15,000 square foot concert hall, which was placed in service in January 2014. The note was secured in part with a $5 million equity-funded reserve fund.

In February 2014 CiviCorp contributed $50 million of capital campaign cash (the "2014 Equity") and MetroCity issued $10 million of tax-exempt bonds (the "2014 Bonds") to fit out a 10,000 square foot opera house in the performing arts center. Construction of the opera house began March 2014 and the opera house was placed in service in March 2017.

Allocation and Accounting Rules Hypothetical

On January 1, 2017, MetroCity issued 500 million of its tax-exempt general obligation bonds (the "2017 Bonds"), of which (i) $50 million was used to refinance the taxable note, $48 million was used to fund a parking lot between the performing arts center and the shopping and entertainment district, $1 million was used to complete the opera house, $1 million was used to pay costs of a pedestrian bridge connecting the peforming arts center, parking facility and the shopping and entertainment district, and $400 million was used to reconstruct streets and roads in MetroCity.

$5 million of reserve fund moneys released upon the defeasance of the taxable note, and $44 million of capital campaign moneys was used by CivicCorp to pay the remaining costs of the pedestrian bridge.

The parking garage and pedestrian bridge were placed in service on January 1, 2018.

Allocation & Accounting Rules Hypothetical Timeline

Jan 2013	• Taxable Note Issue Date
Jan 2014	• Placed in service date of core and shell and concert hall
Mar 2014-17	• Equity used to fit-out opera house
Mar 2017	• Opera house placed in service
Jan 2017	• Issue date of GO Bonds to refinance note, fund parking lot and pedestrian bridge and complete opera house
Mar 2017	• Opera house placed in service
Jan 2018	• Parking garage and pedestrian bridge placed in service

Allocation & Accounting Rules Analysis

- **May CiviCorp be treated as a state or local governmental unit?**
  - Would the response be the same if CiviCorp was established by a special legislation
  - Would the answer be affected if the annual budget of CiviCorp were subject to approval by the MetroCity Council or if the Mayor of MetroCity could remove members of the CiviCorp board without cause
- **Are the concert hall and the opera house part of the same project?**
- **Are the parking garage and pedestrian bridge part of the same project as the performing arts center?**
- **May the 2014 Equity contribution by CiviCorp be treated as qualified equity?**
- **May the $5 million release from the taxable reserve fund be treated a qualified equity?**
  - Would such treatment be different if the taxable reserve was funded with taxable proceeds?

Allocation and Accounting Rules Hypothetical and Analysis

Assume that on January 1, 2026 enters into an arrangement with CiviCorp in which CiviCorp manages the performing arts center for a term of 10 years, MetroCity reimburses CiviCorp for all expenses of operating the performing arts center, and MetroCity receives all receipts. Assume that at the same time, MetroCity agrees to apply all net receipts from the performing arts center to finance infrastructure improvements within the area surrounding the performing arts center, university and shopping and entertainment district.

- Is the arrangement a management contract?
- If not, what factors would cause the arrangement to be a management contract?

Change in Use Hypothetical and Analysis

Assume on January 1, 2026 that MetroCity leases the performing arts center and the parking garage to CiviCorp for a 10-year term for annual rental of $5 million of per year

- On what date would a deliberate action occur?
- What type of remedial actions are available to CiviCorp?
  - How would the answer differ if prior to the lease effective date CiviCorp obtains a 501(c)(3) determination letter from the IRS?
- How would the analysis be affected if the annual rental is equal to MetroCity's cost of providing security for the premises, and CiviCorp is obligated in the lease to allow MetroCity's schools to use the performing arts center free of charge for at least 10 events each year?

Change in Use Hypothetical and Analysis

- **Assume instead that CiviCorp leases the performing arts center for a 99-year term and makes an upfront payment to MetroCity of $150 million.**
  - How much of the purchase price must be treated as disposition proceeds?

- **Assume instead that the leased premises also includes the parking lot and the upfront payment to MetroCity is in excess of the outstanding allocable bonds?**
  - How much of such upfront payment must be treated as disposition proceeds?
  - How may disposition proceeds in excess of the nonqualified bonds be treated as spent?

Tax Increment Financing Hypothetical

City P, pursuant to state legislation, creates a tax increment financing district within its boundaries (the "TIF District").

The TIF District will consist of a single parcel of land owned by Corporation T. Corporation T plans to build a $400 million 20,000 seat basketball arena on the parcel.

The arena will be financed by a $300 million equity contribution by Corporation T and by a grant of $100 million from City P. City P will fund the grant with the proceeds of City P's issuance of TIF revenue bonds that are solely repayable from the incremental real property taxes generated from the parcel.

Corporation T intends to lease the basketball arena to Professional Team K, an affiliated entity of Corporation T, for its home basketball games and to State University U, at a below market rate, for its men's and women's home basketball games.

Tax Increment Financing Analysis

- Are the TIF revenues generally applicable taxes?
  - Generally applicable taxes
    - Enforced contribution for governmental or public purposes
    - Uniform Tax Rate
    - Benefit assessments not generally applicable taxes
  - Impermissible agreements
    - Personal liability
    - Minimum market value subject to tax
    - Agreement not to challenge tax

Tax Incremental Financing Analysis

How would the analysis be affected if the District includes other parcels that generate incremental property taxes pledged to the repayment of the TIF revenue bonds?

What would be the impact of an agreement permitted by State law between City P and Corporation T where Corporation T's property tax rate is calculated by applying the mill rate to 60% of the market value of the arena and the property, rather than the rate of 70% of market value applicable to other taxpayers?

In addition to the incremental property taxes, the TIF revenue bonds are secured by a ticket tax collected by City P for all events at any private facility that has a seating capacity of at least 1,000 people. What if the basketball arena is currently the only private facility with a seating capacity of at least 1,000 people. Is the ticket tax a generally applicable tax?

Tax Increment Financing-Payments in Lieu of Taxes ("PILOT")

PILOT Payments

- Commensurate and not greater than generally applicable tax
  - Fixed percentage or fixed adjustment
  - Must take into account annual assessed value of property determined in the same manner as generally applicable tax
  - Cannot be a fixed dollar amount
- Designated for use for a public purpose

Instead of paying property taxes on the parcel, Corporation T agrees to make annual PILOT payments to City P equal to the mill rate times 75% of the market value of the arena and property. Other taxpayers within City P, pay property taxes semi-annually.

Is the PILOT payment a generally applicable tax?

What if the PILOT payments are equal to mill rate times 60% of the market value of the arena and property but are paid quarterly?

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Tax Increment Financing Bonds Backed by Special Assessments

Essential Government Function

- Utilities or systems available for use by the general public
- Customarily performed by governmental units with general taxing powers
- Eligible to make deferred payments on an equal basis

Enforced Contributions for a specific purpose

- State law of general application
- Applicable equally to natural persons and entities engaged in a trade or business

Tax Increment Financing -Analysis

Would City's P's bonds be private activity bonds if the grant from City P is used only for infrastructure and parking for the arena and City P's bonds were also backed by a benefit assessment imposed on all property owners within the TIF District that is collected only if the incremental property taxes are not sufficient to pay debt service on the revenue bonds?

Would it make a difference if the arena is located downtown and the parking is available to the general public and not limited to arena events?

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Electronic Vehicle Charging Stations Hypothetical and Analysis

City issued $20 million of bonds in 2015 to finance a new 200-space parking garage. The parking garage is used by the general public and operated by the City. In July 2023, City enters into a 10 year contract with ElectriCo, which will install 25 charging stations in the parking lot. ElectriCo will pay City a commission equal to 20% of its collections from members of the general public.

Does the incidental use exception apply?

Would the answer be affected if in 2023 City issues $5 million of tax-exempt bonds to construct a trench under the parking lot to accommodate additional power needs for the garage and water lines for adjacent properties?

Electronic Vehicle Charging Stations Hypothetical and Analysis

Assume instead that City uses 100 spaces in the garage for City vehicles and 100 spaces for public parking. City contract with ElectriCo provides for ElectriCo to use 15 chargers exclusively for City vehicles for a fee equal to $100,000 per year and ElectriCo may use 10 chargers for service to the general public at fees generally applicable uniformly applied fees approved by the City.

- Would ElectriCo be treated as a private user?
- Would the answer be different if ElectriCo retains 90% of charges to private users and remits the remaining 10% to City?

Questions?

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