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Private Activity Bond Tests
Real World Challenges

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This panel will address more advanced issues encountered in the identification, allocation and remediation of private business use of bond-financed property. The hypotheticals are intended to identify and nuances in the private activity bond regulations that may affect whether private use arises, the availability and allocation of qualified equity and the application of the remedial action regulations. The panel is intended for bond and tax lawyers with more than five years of experience.

The following fact pattern and questions will be discussed during the session:

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 not for profit corporation law to develop the land (“CiviCorp”). CiviCorp has 7 members, consisting of the Mayor of MetroCity, 2 members appointed by the MetroCity Council, 1 member appointed by the president of the University and 3 members who are nominated by the president of the University and appointed by the Mayor of MetroCity.

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 hall, which was placed in service in January 2014. In February 2014 CiviCorp contributed \$50 million of capital campaign cash to fit out a second opera theater in the performing arts center. Construction of the second theater began March 2014 and the second theater was placed in service in January 2016. On January 1, 2017, issued \$100 million of its tax-exempt bonds to refinance the outstanding taxable note in the amount of \$50 million and applied the remaining \$50 million of proceeds to (i) install acoustical panels in the music hall, landscape the surrounding parkland (\$10 million) and construct a new 300 space parking garage (\$35

million). The final maturity date of the MetroCity Bonds is January 1, 2028. CiviCorp contributed \$5 million of its cash to pay costs of constructing the parking garage. The parking garage project included a \$10 million pedestrian bridge connecting the parking garage to the performing arts center and the shopping and entertainment district. Construction of the parking garage and pedestrian bridge commenced on January 1, 2017 and was placed in service on January 1, 2018.

All of the bond financed property was owned and operated by MetroCity through December 31, 2023. MetroCity proposes to enter into an arrangement with CiviCorp on January 1, 2024 whereby for a period of 5 years CiviCorp will manage the music hall in the performing arts center. CiviCorp will not receive a fee for its services. MetroCity and CiviCorp will agree on an annual budget for the operation of the performing arts center. All revenues from the music hall will be paid to MetroCity and MetroCity will reimburse CiviCorp for its costs of managing the performing arts center. MetroCity agreed to use any net profits from the operations of the performing arts center for capital improvements to the park complex in consultation with CiviCorp.

On January 1, 2026, MetroCity modified its arrangement with CiviCorp by leasing the performing arts center to CiviCorp for a term of 40 years. Pursuant to the lease, CiviCorp is required to pay annual rentals to MetroCity of \$5 million per year.

What amounts contributed by CiviCorp, if any, may be treated as qualified equity?

On what date or dates did a deliberate action occur?

What type of remedial actions are available to MetroCity?

If instead of leasing the facility, CiviCorp determines to purchase a 99 year leasehold of the performing arts center for \$150 million, how much of the purchase price must be treated as disposition proceeds? How would the answer change if the 2017 issue was in the amount of \$500 million with \$400 million used to finance street improvements?

How may the disposition proceeds in excess of the cost of defeasing the non qualified bonds, if any, be treated as spent?

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PRIVATE ACTIVITY BOND TESTS*

I. DEFINITIONS AND GENERAL RULES – SECTION 141 AND SECTION 1.141-1

A. Private Business Tests.

1. General. Code Section 141(a)(1)¹ defines a “private activity bond” issue as a bond issue that satisfies both of the following tests, which are set forth in Code Section 141(b) (the “private business tests”):

a. Private Business Use Test. More than 10% (or 5% if the private business use is unrelated or disproportionate to the governmental use) of the bond proceeds are to be used, directly or indirectly, in the trade or business of a person other than a state or local government unit (the “private business use test”); and

b. Private Security or Payment Test. The payment of the principal of, or the interest on, more than 10% (or 5% if the private business use is unrelated or disproportionate to the governmental use) of the proceeds of the bond issue is (under the terms of the issue or any underlying arrangement) directly or indirectly (i) secured by an interest in property used or to be used for a private business use or payments in respect of such property, or (ii) to be derived from payments (whether or not to the issuer) in respect of property, or borrowed money, used or to be used for a private business use (the “private security or payment test”).

2. \$15 Million Limitation. Even if the private business tests are not met, the bonds may be private activity bonds if the “nonqualified amount” exceeds \$15 million. The nonqualified amount is the lesser of (i) the portion of the bond proceeds to be used for private business use or (ii) the portion of the bonds that are secured by, or payments derived from, property used in private business use. If the nonqualified amount exceeds \$15 million, the bonds are private activity bonds unless the issuer allocates its annual volume cap for qualified private activity bonds to the nonqualified amount in excess of \$15 million.

3. Separate Private Loan Financing Test. In addition, Code Sections 141(a)(2) and 141(c) independently treat bonds as private activity bonds if more than the lesser of 5% or \$5,000,000 of the proceeds of the bond issue are to be used, directly or indirectly, to make or finance loans (excluding certain permitted tax assessment loans) to non-governmental persons (the “private loan financing test”). Private loans may arise even if there is no private business use, such as in the case of loans to individuals acting in a non-business capacity.

B. Private Activity Definitions. Certain definitions that are specifically applicable to the private activity bond regulations (referred to herein as the “Regulations”) are noted below. Unless otherwise noted, these definitions are set forth in Treas. Reg. §1.141-1(b).

*This outline draws significantly from the excellent outlines and updates prepared by prior chairs and panelists.

¹ Unless otherwise noted herein, all section references are to the Internal Revenue Code of 1986, as amended, and the Treasury Regulations promulgated thereunder.

1. Common Areas mean portions of a facility that are equally available to all users of a facility on the same basis for uses that are incidental to the primary use of the facility. For example, hallways and elevators generally are treated as common areas if they are used by the different lessees of a facility in connection with the primary use of that facility.

2. Discrete Portion means a portion of a facility that consists of any separate and discrete portion of a facility to which use is limited, other than common areas. A floor of a building and a portion of a building separated by walls, partitions, or other physical barriers are examples of a discrete portion.

3. Disposition means the sale, exchange or other distribution or transfer of property (other than investments) financed with the proceeds of an issue. *See* Treas. Reg. §1.141-12(c)(1).

4. Disposition Proceeds means any amounts (including property, such as an agreement to provide services) derived from a disposition of property financed with the proceeds of an issue. *See* Treas. Reg. §1.141-12(c)(1).

5. Governmental Person means a state or local governmental unit as defined in Code Section 1.103-1 or any instrumentality thereof. The federal government is not a Governmental Person.

6. Measurement Period. Except as provided in Treas. Reg. §1.141-3(g)(2), the measurement period of property financed by an issue begins on the later of the issue date of the bonds or the date on which the financed property is placed in service and ends on the earlier of the last date of the reasonably expected economic life of the property or the latest maturity date of any bond of the issue financing the property (determined without regard to any optional redemption dates). In general, the period of reasonably expected economic life of the property for this purpose is based on reasonable expectations as of the issue date. *See* Treas. Reg. §1.141-3(g)(2).

7. Proceeds means the sale proceeds of an issue (other than sale proceeds used to retire bonds of the issue that are not deposited in a reasonably required reserve fund). Proceeds also include any investment proceeds from investments that accrue during the project period (net of rebate amounts attributable to the project period). Disposition proceeds are treated as proceeds to the extent provided in Treas. Reg. §1.141-12 (remedial actions). The Commissioner may treat replaced amounts as proceeds.

8. Project Period means the period beginning on the issue date of the bonds and ending on the date that the project is placed in service. A project is placed in service on the date, which based on all the facts and circumstances, (a) the project has reached a degree of completion which would permit its operation at substantially its design level, and (b) the project is in fact in operation at such level. In the case of a multipurpose issue, the issuer may elect to treat the project period for the entire issue as ending on the expiration of the applicable temporary period or the end of the fifth bond year.

9. Renewal Option means a legally enforceable right to renew a contract. A provision that provides for automatic renewal in the absence of the exercise of a cancellation right by either party is not a renewal option, even if it is expected to be renewed.

10. Replaced Amounts means replacement proceeds other than amounts that are treated as replacement proceeds solely because they are sinking funds or pledged funds.

C. Related Parties. Except as otherwise provided, related parties are treated as one person and any reference to “person” includes any related party. *See* Treas. Reg. §1.141-1(d) and Treas. Reg. §1.150-1(b) for the general definition of related party.

1. PLR 200942037. In this ruling, a university, by reason of a special (although redacted citation) tax act definition, is a qualified educational organization equivalent to a state governmental unit for purposes of the tax-exempt bond provisions of the Code for any trade or business not constituting an unrelated trade or business. The university established a hospital corporation to run the clinical operations of the university’s medical school. The hospital corporation qualifies as an organization described in Section 501(c)(3), and the operation of the clinics does not constitute an unrelated trade or business of the corporation. The hospital corporation is controlled by the university because the university has the power both to appoint and remove, without cause, a controlling portion of the board of the corporation. Under these facts, the Internal Revenue Service (the “IRS”) determined that the university and the hospital corporation are related governmental users of a bond-financed project because both entities meet (1) the related party definition of Treas. Reg. §§1.150-1(b) and (2) the related party attribution rule of Treas. Reg. §1.141-1(d).

II. PRIVATE ACTIVITY BOND TESTS - SECTION 1.141-2

A. Overview. Treas. Reg. §1.141-1 (a) states that the purpose of the private activity bond tests set out in Code Section 141 is to limit the volume of tax-exempt bonds that finance the activities of nongovernmental persons,² without regard to whether a financing actually transfers the benefits of tax-exempt financing to a nongovernmental person. Regulations under Code Section 141 serve to identify arrangements *that have a potential to transfer the benefits of tax-exempt financing, as well as arrangements that actually transfer these benefits*. The anti-abuse rules of Treas. Reg. §1.141-14 should be considered in light of this purpose. The Regulations under Code Section 141 may not be applied in a manner that is inconsistent with these purposes.

B. Scope. Treas. Reg. §§1.141-0 through 1.141-16 apply generally for the purposes of the private activity bond limitations under Code Section 141.

C. Reasonable Expectations and Deliberate Actions.

1. General. A bond issue is an issue of private activity bonds if the issuer reasonably expects, as of the issue date, that the issue will meet either (1) the private business tests or (2) the private loan financing test. In addition, an issue is an issue of private activity bonds if the issuer takes a deliberate action after the issue date that causes the conditions of either the private business tests or the private loan financing test to be met. *See* Treas. Reg. §1.141-2(d)(1).

² The terms nongovernmental person and private business user are used herein interchangeably to refer to users whose use may result in private business use, including use by the federal government and not-for-profit entities, including 501(c)(3) entities.

2. Reasonable Expectations. In general, the issuer's reasonable expectations about events and actions affecting the use of bond proceeds must be taken into account over the entire stated term of the issue.

a. Special Rule for Contingent Mandatory Redemption. Treas. Reg. §1.141-2(d)(2)(ii) provides that an issuer may disregard an action that is reasonably expected on the issue date and that otherwise would violate the private activity bond tests if, on the issue date, (i) the issuer reasonably expects that the financed property will be used for a governmental purpose for a "substantial period" of time; (ii) the issuer is required to redeem all "nonqualified bonds" (even if the cost to redeem is in excess of the disposition proceeds by contributing its own funds) within six months of the action; (iii) the issuer has not entered into an arrangement with a nongovernmental person with respect to the action; and (iv) the mandatory redemption meets the change-in-use rules contained in Treas. Reg. §1.141-12 (taking into account the redemption described in (ii) above). This special rule allows bond redemptions to cure expected, but unpredictable, future private involvement during the term of a bond issue. The requirement that bonds be redeemed irrespective of the amount of disposition proceeds received places a certain amount of risk on the issuer.

b. Substantial Period. The absence of a definition of "substantial period" for purposes of this rule leaves some uncertainty. One possible analogy may be the definition of substantial period for a different purpose under Treas. Reg. §1.141-3(g)(7) on measurement of private business use, in which 10% of the measurement period is treated as a substantial period. Another analogy is the old five-year period used in the original change-in-use safe harbors under Revenue Procedure 93-17, 1993-1 C.B. 507.

3. Deliberate Actions. A deliberate action is an action taken by the issuer that is within its control. See Treas. Reg. §1.141-2(d)(3). An intention to violate the requirements of Code Section 141 is not necessary for any action to be deliberate. Involuntary conversions under Code Section 1033 and actions taken in response to a regulatory directive of the federal government are not deliberate actions. Certain remedial actions described in Treas. Reg. §1.141-12 can prevent a deliberate action from causing the related nonqualifying bonds to cease to be treated as tax-exempt bonds. A deliberate action occurs on the date the issuer enters into a binding contract for nongovernmental use of the financed property that is not subject to any material contingencies. The binding contract notion is important to keep in mind if an issuer signs a contract with a later effective date.

4. Special Rules. Special rules are provided for two governmental bond program situations.

a. Certain Personal Property Dispositions. Dispositions of personal property in the ordinary course of an established governmental program meeting certain requirements (*i.e.*, weighted average bond life not more than 120% of reasonably expected governmental use, the fair market value of property at time of disposition is not reasonably expected to exceed 25% of cost, the property is no longer suitable for governmental purposes on date of disposition) are not treated as deliberate actions if the issuer is required to commingle disposition amounts with substantial tax or other funds and such amounts are reasonably expected

to be expended within 6 months of commingling. Bonds properly allocated to this personal property may be treated as a separate issue under Treas. Reg. §1.150-1(c)(3).

b. Certain General Obligation Bond Programs. In addition, the determination of whether an issue of general obligation bonds of a general purpose governmental issuer that finances a large number of separate purposes (at least 25 separate purposes and not less than 4 predominant purposes) satisfies the private activity bond tests may be based solely on the issuer's reasonable expectations as of the issue date (without regard to subsequent deliberate actions) if the following requirements are satisfied: (i) the issue must be a general obligation of the issuer; (ii) the issuer must be a general purpose governmental unit; (iii) the issue must finance at least 25 separate purposes but cannot "predominantly" finance fewer than four purposes; (iv) the issuer must employ a "fund" accounting method; (v) the accounting method must make specific tracing of bond proceeds to expenditures unreasonably burdensome; (vi) the issuer must reasonably expect to spend all the net bond proceeds on capital expenditures within six months after the issue date; (vii) the issuer must adopt reasonable procedures to verify such expenditures (a program for random spot checks of actual use of 10% of the bond proceeds qualifies); (viii) the issuer must reasonably expect to spend all the net bond proceeds before spending any later similar general obligation bond proceeds; (ix) the issuer must reasonably expect to make no private loans with the bond proceeds; (x) the issuer must reasonably expect that it could make governmental capital expenditures during the ensuing six months of at least 125% of the amount financed; and (xi) the issuer must reasonably expect that the average maturity of the bond issue does not exceed 120% of the weighted average reasonably expected economic life of the financed capital improvements.

III. DEFINITION OF PRIVATE BUSINESS USE - SECTION 1.141-3

A. General Rule. Generally, the private business use test of Code Section 141(b)(1) is met if more than 10% (or, in certain cases, 5%) of the proceeds of an issue is used in a trade or business carried on by a nongovernmental person. For this purpose, the use of financed property is treated as the use of proceeds. Both indirect use and the ultimate and intermediate uses of proceeds are considered in determining whether an issue meets the private business use test.

B. General Definition of Private Business Use.

1. General. Proceeds are used for private business use if they are used in a trade or business carried on by a nongovernmental person. For this purpose, any activity carried on by a person other than a natural person is treated as a trade or business. For the purposes of the private business use test, a nongovernmental person uses bond proceeds and will generally be a private business user if it (i) owns financed property, (ii) leases/subleases financed property (unless an exception is met), (iii) manages or is a service provider with respect to the financed property under a nonqualifying management contract, (iv) purchases or agrees to purchase the output of an output facility under a nonqualifying arrangement, (v) sponsors a nonqualifying research arrangement that relates to the financed property, (vi) otherwise enjoys special legal entitlements for the beneficial use of the financed facility, or (vii) solely in the case of financed property that is not available for use by the general public, receives special economic benefit from the financed property.

2. Actual or Beneficial Use.

a. In General. In the catch-all category of other actual or beneficial use, Treas. Reg. §1.141-3(b)(7) provides that private business use may arise under two separate standards, depending on whether the financed property is available for general public use: (i) “special legal entitlements” to general public use property; and (ii) “special economic benefits” from property that is not available for general public use, based on all the facts and circumstances.

b. Special Legal Entitlements to General Public Use Property. For bond-financed property that is available for general public use, Treas. Reg. §1.141-3(b)(7)(i) provides that private business use of such property arises if a private business has special legal entitlements to beneficial use of the property. For example, an arrangement that provides priority rights to the use or capacity of a facility generally causes private business use under this standard. The special legal entitlement standard generally seems workable in that it looks to objective legal rights granted to private businesses to use bond-financed facilities.

c. Special Economic Benefits from Non-general Public Use Property. For bond-financed property that is unavailable for general public use, Treas. Reg. §1.141-3(b)(7)(h) provides that private business use of such property arises if a private business derives special economic benefits from the property, based on all the facts and circumstances, even if it has no special legal entitlements. The Regulations state that the following factors weigh towards private business use under this standard:

(i) a functional relationship or physical proximity of the bond-financed property to other private business use property;

(ii) a small number of private businesses receiving the special economic benefit; and

(iii) the cost of the property being depreciable by a private business (this depreciable interest factor would seem to give rise to private business use anyway, based on ownership).

3. Exception. A special exception under Treas. Reg. §1.141-3(d)(2) excludes nominal ownership by a nongovernmental person that is solely incidental to a financing arrangement. For example, a private business may hold title in a sale-leaseback transaction with a governmental lessee.

4. Management Contract as Lease. Treas. Reg. §1.141-3(b)(3) provides that the determination of whether an arrangement such as a management contract properly constitutes a lease is based on all of the facts and circumstances, including (i) the degree of private business control over the financed property; and (ii) whether the private business user bears risk of loss on the financed property.

5. Selected Examples from the Regulations.

a. Treas. Reg. §1.141-3(f), Example 5 - Parking Lot. Corporation C and City D enter into a plan to finance the construction of a parking lot adjacent to C’s factory.

Pursuant to the plan, C conveys the site for the parking lot to D for a nominal amount, subject to a covenant running with the land that the property be used only for a parking lot. In addition, D agrees that C will have the right to approve rates charged by D for the use of the parking lot. D issues bonds to finance construction of the parking lot on the site. The parking lot will be available for use by the general public on the basis of rates that are generally applicable and uniformly applied. The issue meets the private business use test because a nongovernmental person has special legal entitlements for beneficial use of the financed facility that are comparable to an ownership interest.

b. Treas. Reg. §1.141-3(f), Example 8 - Airport Runway.

(i) City I issues bonds and uses all of the proceeds to finance construction of a runway at a new city-owned airport. The runway will be available for take-off and landing by any operator of any aircraft desiring to use the airport, including general aviation operators who are natural persons not engaged in a trade or business. It is reasonably expected that most of the actual use of the runway will be by private air carriers (both charter airlines and commercial airlines) in connection with their use of the airport terminals leased by those carriers. These leases for the use of terminal space provide no priority rights or other preferential benefits to the air carriers for use of the runway. Moreover, under the leases, the lease payments are determined without taking into account the revenues generated by runway landing fees (that is, the lease payments are not determined on a “residual” basis). Although the lessee air carriers receive a special economic benefit from the use of the runway, this special economic benefit is not sufficient to cause the air carriers to be private business users, because the runway is available for general public use. The issue does not meet the private business use test.

(ii) The facts are the same as in paragraph (i) above, except that the runway will be available for use only by the private air carriers. The use by these private air carriers is not for general public use, because the runway is not reasonably available for use on the same basis by natural persons not engaged in a trade or business. Depending on all of the facts and circumstances, including whether there are only a small number of lessee private air carriers, the issue may meet the private business use test solely because the private air carriers receive a special economic benefit from the runway.

(iii) The facts are the same as in paragraph (i) above, except that the lease payments under the leases with the private air carriers are determined on a residual basis by taking into account the net revenues generated by runway landing fees. These leases cause the private business use test to be met with respect to the runway because they are arrangements that convey special legal entitlements to the financed facility to nongovernmental persons.

c. Treas. Reg. §1.141-3(f), Example 9 – Governmental Airport Parking. A governmentally owned airport parking facility that is generally available to both private airline employees and the general public using the airport qualifies for general public use, despite the special economic benefit to the private airlines.

d. Treas. Reg. §1.141-3(f), Example 11 - Port Road - Highway Authority. W uses all of the proceeds of its bonds to construct a 25-mile road to connect an industrial port owned by Corporation with the existing roads owned and operated by W. Other

than the port, the nearest residential or commercial development to the new road is 12 miles away. There is no reasonable expectation that development will occur in the area surrounding the new road. W and Y enter into no arrangement (either by contract or ordinances) that conveys special legal entitlements to Y for the use of the road. Use of the road will be available without restriction to all users, including natural persons who are not engaged in a trade or business. The issue does not meet the private business use test because the road is treated as used only by the general public.

6. Private Letter Rulings. Certain private letter rulings issued since release of the 1997 private activity bond regulations are summarized below in addition to the summaries under specific sections of this outline. Earlier private letter rulings are summarized in the National Association of Bond Lawyers' Federal Taxation of Municipal Bonds, Third Edition.

a. PLR 202205016 and PLR 202205017. City acquired property, which is reclaimed land consisting of sand fill on top of native soil. The District will issue bonds to be payable by incremental tax revenues generated by improvements to be financed with bond proceeds. The bond-financed projects include (i) strengthening of an existing revetment, including adding rocks to the revetment and adjacent areas and raising the level of the revetment to reduce the risk of flooding, (ii) soil stabilization improvements (iii) governmental structures, including police, fire and school facilities, and (iv) public access facilities, including roads, rights of way and sidewalks. No person or entity, other than state and local governmental units will have any special rights, privileges or other legal entitlements with respect to the bond funded improvements. A portion of the ground improvements to be funded with bond proceeds will be located on portions of the property on which private use facilities are located, however the design of the ground improvements took into account the needs of the governmental improvements, but not the needs of the private use facilities. Nevertheless the revetment strengthening and ground improvements will protect the entire area without distinction between public or private property or the type of area occupant or user. The IRS noted that when completed, the improvements would provide some benefit to all of the owners, lessees and operators of private business use facilities, and not only a small number of private business users. The IRS did not decide whether there will be a special economic benefit to such owners, lessees and operators, but held that under the facts and circumstances the benefits to such private business users would be insufficient to give rise to private business use.

b. PLR 201412011. Management contract entered into by a governmental electric company had an initial term of 12 years with potential extension to 20 years. The IRS had previously ruled favorably on the original contract and was asked to review the Amended Agreement made primarily to deal with operational difficulties encountered by the Electric Company as a result of a "Storm Event." The compensation involved a fixed fee component, an incentive fee component, and a reimbursement of certain costs, none of which exactly fit within the definitions in Revenue Procedure 97-13 ("Rev. Proc. 97-13"). The fixed component did not fit the definition of periodic fixed fee because the amount could be reduced if certain performance standards related to customer satisfaction and service interruptions were not met. The IRS concluded that the standards for reduction were not based on objective, external factors as permitted under the safe harbor, but did not give rise to private business use because the reduction was not based on net profits, and further, even after a reduction, the fee was a stated amount for a particular annual period. The incentive compensation is also different from the type described in Rev. Proc. 97-13. The Electric Company was to establish an incentive compensation pool. The incentive fee could be earned based on "favorable" performance measured against

certain detailed performance metrics but could also adjust downwards if minimum performance standards were not met. None of the performance criteria described in the ruling relate directly to revenues or profits but do include adherence to capital and operating budgets and meeting the Electric Company's "financial needs." The IRS notes that some of the performance categories provide incentives to reduce expenses, but that the incentive fee does not create private business use because it is not based on gross revenues or net profits of the Electric Company. The contract included reimbursement for transactions with affiliates. The costs passed on are described as being based on methodologies such as the fully allocated cost methodology approved by statute or regulations, which are described as not including a profit or mark-up component for the affiliate. Pass-through expenditures do not include amounts paid to senior management of the Manager. Because none of the reimbursements are based on net profits of the Electric Company, the IRS concludes that these payments do not cause private business use. The ruling addressed ancillary contracts that could arise with the manager or manager affiliate for major storm and other emergency expenditures beyond the reasonable control of the manager. Because these services were for unforeseen events and not for the day-to-day operations and must be separately approved by the Electric Company, the IRS concludes that these contracts would not be taken into account in analyzing the Amended Agreement.

c. PLR 201346002. Authority issued Bonds in part to finance construction of Facility owned by Authority and leased to State pursuant to multi-year operating Lease. State intends to enter into management contracts for performance of certain substantial services at Facility that will cause the Bonds to satisfy the private business test. Lease payments and State's rental payments on other facilities financed by parity bonds are security for the Bonds. Bondholders do not have a mortgage or other security agreement creating a security interest in Facility under State law. Authority has covenanted that generally it will not sell, lease, mortgage or otherwise dispose of Facility other than the Lease, as long as the parity bonds are outstanding. These restrictions do not apply after the Lease is terminated or if other monies are sufficient to cover the amounts of the Lease payments. Held: The Lease and related covenants will not cause the private security or payment test to be met because the Lease and indenture covenants merely provide assurance to bondholders that Authority will continue to make Facility available to State and State will continue to use Facility and make Lease payments until Lease is ended and neither bondholders nor any other parties (other than State or Authority) will be granted rights in Facility.

d. PLR 201338031. Bonds were issued to finance construction and renovation of a Hotel. Pursuant to a management contract, Manager supervises, controls, manages and operates the Hotel. The compensation to Manager is being amended to include an annual base fee and an annual incentive fee. The proposed annual base fee is the greater of (i) the amount that would be a periodic fixed fee if paid every year or (ii) a percentage of the hotel's actual gross receipts for the fiscal year. The proposed annual incentive fee amount is a percentage of actual gross receipts for the fiscal year which amount the Issuer will pay the Manager only if the Hotel's Achieved Revenue Per Available Room (RevPAR) is at least a set percentage of the Achieved RevPAR of a group of specific hotels comparable to the Hotel. Held: Under the facts and circumstances, notwithstanding the management contract will not meet the requirements of Section 5 of Rev. Proc. 97-13, the management contract will not result in private business use of the Hotel because both the base fee and the incentive fee, both independently and in combination, are not based on a share of net profits.

e. PLR 201338026. Bond proceeds are to be used to finance acquisition or renovation of facilities to be owned or leased by Hospital for purpose of providing clinical medical services. Pursuant to a management contract, Medical Group will provide physician services to Hospital at the financed clinical facilities and is paid base compensation and incentive compensation and reimbursement for certain expenses by Hospital. Every third year, the base compensation and incentive compensation will be renegotiated to ensure that they remain within fair market value. Hospital also pays a portion of the compensation of the President of the Medical Group which includes base compensation and incentive compensation. Held: Under the facts and circumstances, notwithstanding the management contract does not meet the requirements of Section 5 of Rev. Proc. 97-13, the management contract does not result in private business use of the clinical facilities because (i) neither the Hospital's payment or reimbursement of the Medical Group's miscellaneous expenses nor its payment or reimbursement of the Medical Group's compensation expenses are calculated based on net profits, (ii) the facts and circumstances of the President's incentive pay do not support a conclusion of private business use of the clinical facilities, (iii) based in part on the periodic renegotiation of base compensation and incentive compensation, the management contract provides for reasonable compensation for the services provided by the Medical Group, and (iv) the Medical Group does not have any role or relationship with Hospital that substantially limits the Hospital's ability to exercise its rights under the management contract, including its termination right.

f. PLR 201228029. Electric Company, a governmental person that owns and controls an electric transmission and distribution system, will enter into an agreement with Manager for the single-purpose subsidiary of Manager to operate the electric transmission and distribution system. The term of the agreement will not exceed 10 years, and Manager and Electric Company (and Electric Company's sole shareholder, Authority) are not related parties and do not have any overlapping board members. The compensation of Manager will consist of the following components: (1) Fixed Direct Fee, (2) Incentive Compensation Component, and (3) Reimbursement of Pass-Through Expenditures. The Fixed Direct Fee is a stated dollar amount subject to adjustment for reduced credit support and reduction for poor performance. The Incentive Compensation Component is expressed in the first year of the contract as a stated dollar amount that the Manager may earn if it attains certain favorable performance goals, including expense reduction incentives. The Reimbursement of Pass-Through Expenses includes the Manager's actual costs without mark-up or profit, but Manager's costs on transactions with affiliates, if any, may include a mark-up of the affiliates' direct expenses in accordance with Federal Energy Regulatory Commission ("FERC") sanctioned cost allocation methods. Held: Based on all facts and circumstances, the agreement with Manager does not result in private business use of the tax-exempt bond-financed electric transmission and distribution facilities within the meaning of Code Section 141(b). Although the potential adjustments to the Fixed Direct Fee cause it not to meet the definition of a "periodic fixed fee" under Rev. Proc. 97-13, such fee does not result in private business use. The Incentive Compensation Component similarly does not result in private business use because the expense reduction incentives of such fee are not based on gross revenues or net profits of the facilities. The Reimbursement of Pass-Through Expenditures component does not result in private business use because any mark-up of actual costs will occur pursuant to FERC sanctioned cost allocation methods and not a share of net profits from the facilities. Finally, the length of the agreement does not cause the contact to result in private business use because the 10-year term does not exceed the 20-year term allowable under

Rev. Proc. 97-13 for contracts that relate to public utility property and satisfy either the 95% or 80% periodic fixed fee safe harbor.

g. PLR 201216009. IRS concludes that, if an agreement between a public hospital district and a public university creates a partnership, the partnership would nonetheless not create private business use because, applying the aggregate approach to partnership, the persons using the facilities will all be governmental persons.

h. PLR 201213010. Automated people mover (APM) transporting airline employees and passengers between terminals of an airport facility is not a common area of the terminals and may be treated as a separate facility. Further, because passengers and employees may ride the APM at no cost and no preferential treatment, the APM is available to the general public, despite security requirements imposed on those entering the terminals.

i. PLR 201043001. The IRS concluded that bonds issued to pay insurance claims for losses on commercial policies and residential policies resulted in private business use, but the bonds will not be treated as private activity bonds because the bonds will be repaid with taxes of general application. In the private letter ruling, an association was established by the state legislature to provide insurance to applicants who would otherwise be unable to obtain insurance in the marketplace. To the extent that the association's funds are insufficient to pay claims, the association will issue bonds to pay the remaining claims and the bonds will be repaid from either premium surcharges assessed on policyholders or assessments on all property insurers licensed to do business in the state. The IRS concluded that the bonds meet the private business use test because the commercial policyholders who receive bond proceeds in satisfaction of their claims are private business users. The IRS noted that the association is not able to avail itself of the public use exception because there are enough differences between residential and commercial policies that each policy type must be rated separately, and the policy terms exceed 200 days. However, the IRS concluded that the premium surcharges and assessments used to repay the bonds are taxes of general application and, therefore, the bonds fail the private security or payment test.

j. PLR 201049003. The IRS concluded that an agreement with a university to broadcast and televise its college sports games did not result in private business use of the bonds. In the private letter ruling, a corporation received under the agreement (i) broadcast and telecast rights, (ii) advertising sales and corporate sponsorship program rights, and (iii) publishing and vending rights. The agreement did not give the corporation any rights to control the teams, ticket sales, security, personnel management, or general management of the venues. For the rights granted under the agreement, the corporation must (a) pay a stated annual fee to the university in semi-annual installments over the term of the agreement, (b) pay the university a royalty in each contract year equal to a percentage of net revenues in excess of specified threshold amounts, (c) make investments in signage and technological upgrades, and (d) promote the university's athletic scholarship fund by providing a media package with a specified value. The IRS concluded that the agreement conveyed special legal entitlements to the corporation to use portions of bond-financed improvements but did not result in private business use. In reaching this conclusion, the IRS stated that the corporation's right to broadcast and televise the sports game and the sale of the advertisements is too remote to be considered use of the bond-financed improvements and provides no control over any element of the game schedules. In addition, the IRS stated that the tangible use of the bond-financed portions of the venues, including the use of

broadcast equipment and certain personnel at the venues, are incidental uses that do not exceed more than 2.5 percent of the bond-financed improvements.

k. PLR 200829008. With this private letter ruling, the IRS continues its favorable line of rulings dealing with the acquisition of separate property interests. A governmental agency sought to issue bonds to refund a taxable financing used to acquire undivided interests in certain mineral and working interests purchased from a nongovernmental seller who retained undivided interests in the same properties, the result being that the total property (mineral interests and interests in depreciable property associated with the mineral interests) was jointly owned by the private seller and the agency. The purchase price paid for the property by the agency was adjusted in accordance with trade usage to reflect the existence of the seller's and other interests in the property. Largely because the purchase price and operations of the various interests reflected separate rights and obligations associated with the interests, the IRS, relying heavily on Example 1 in Treas. Reg. §1.141-7(i) (recognizing and respecting separate ownership interests in output facilities), ruled that no portion of the purchase price for the interests acquired by the agency would be treated as used in a private business use as a result of seller's retained interests in the property.

l. PLR 200827023. The IRS ruled that the transmission and distribution of electricity that was generated or purchased with the proceeds of tax-exempt obligations issued by a governmental utility through distribution and transmission facilities owned by a for-profit, investor owned utility did not constitute private business use of the electricity where the for-profit utility did not enter into any arrangement to purchase the bond-financed electricity, the arrangement did not convey to the private party any special legal entitlements with respect to the bond-financed electricity, and where the private parties were simply using their private facilities to transmit the bond-financed electricity to customers of the governmental utility.

m. PLR 200718021. County prison facility with 100-day contracts with a federal agency for housing prisoners and with an expectation that there will be up to 90 percent non-federal prisoner use over time will not create private business use, because facility is available for use by the county on the same basis as the federal contracts and is not constructed for the principal purpose of providing the facility for federal use.

n. PLR 200542032. The IRS considered whether the transfer of "firm transmission rights" (FTR) under a regimen established by an electric transmission independent system operator (ISO) and approved by the FERC would be treated as a "deliberate action" causing bonds issued to provide the municipally-owned transmission facilities to which the FTR's related to be private activity bonds. A central question presented was whether the transfer of an FTR, which gave to the holder the right to participate in the receipt of special fees charged by the ISO as a market mechanism to control "congestion" over specific transmission interfaces, constituted a transfer of an ownership interest in the bond-financed facilities. The FTR's, which were to be sold by the ISO through public auction, were to have a term of one year. While the FTR could be held by any person, they would be particularly attractive to a power generation or distribution utility as a hedge against the adverse impact of high congestion charges across points necessary to its business. Looking to guidance under section 1001 of the Code and general tax cases, the IRS set forth several factors in concluding that no ownership interest in the financed transmission facilities was transferred: Incidence of ownership include (1) legal title, (2) contractual duty to

pay for capital investment, (3) responsibility to pay maintenance and operating costs, (4) duty to pay taxes, (5) risk of loss and (6) risk of diminution of value. The benefits and burdens indicative of ownership include (1) right to possession, (2) obligation to pay taxes, (3) responsibility to insure property, (4) duty to maintain property, (5) right to improve property, (6) risk of loss and (7) legal title.

o. PLR 200502012. The IRS considered whether the acquisition of various interests in land and certain related arrangements gave rise to private business use. An authority created to acquire, operate and maintain property for a city would acquire the property interests through arms' length negotiations with the sellers and would pay no more than FMV for the interests. The authority described five types of property interests. The IRS focused its analysis on identifying the bond-financed property, identifying the seller's distinct property, determining whether the seller's use of that distinct property impinged on the authority's use of the bond-financed property, and determining whether and on what basis the seller used the authority's property. The IRS specifically noted that the type of property interest was not controlling.

(i) A Conservation Easement in Perpetuity, Restricting the Seller's Use of the Property Subject to the Easement. The bond-financed property is the easement. The Authority is the owner of the easement in perpetuity and the seller does not have any interest (such as a reversionary interest) in the easement. The seller has a distinct interest in the property and the seller's use of the retained interest does not impinge on the Authority's use of its interest. The seller's only use of the easement is as a member of the general public. Other than that use, the seller's use of the parcel is not the use of bond-financed property. The Authority's acquisition of the conservation easement does not give rise to private business use of the bond proceeds.

(ii) A Future Interest in Fee Simple, with the Seller Retaining a Life Estate. The bond-financed property is the future interest. The Authority and the seller have distinct interests in the parcel, which occur at different times. The use of the parcel by the seller during the life estate does not impinge on the Authority's use of the future interest. The seller's use of the parcel will end with the termination of the life estate and, therefore, the seller will not use the bond-financed property. The Authority's acquisition of the future interest in fee simple does not give rise to private business use.

(iii) Fee Simple, with a Subsequent Lease to the Seller or a Third Party that Grants the Lessee Certain Agricultural Rights. The bond-financed property is the present interest in fee simple. The subsequent lease to a nongovernmental person results in private business use during the term of the lease of 100% of the proceeds used to acquire the fee simple interest.

(iv) Fee Simple, with the Seller Retaining a Profit A Prende Interest that Allows the Seller to Enter the Parcel for Limited Purposes, which are Less Extensive than those Permitted under a Lease. The bond-financed property is the fee simple, subject to (or less) the *profit a prende* interest. The Authority has a possessory right to use the parcel while the seller holds a non-possessory interest to use the parcel for limited purposes. The seller has a distinct interest in the parcel and the seller's permitted uses under the *profit a prende* interest will not impinge on the Authority's use of its interest in the parcel. The seller's only use of the

Authority's interest will be as a member of the general public. The Authority's acquisition of a present interest in fee simple subject to *profit a prende* interest will not give rise to private business use of bond proceeds.

(v) Fee Simple, With a Subsequent Conveyance of a Profit A Prende Interest to a Third Party. In this case, the fee simple is the bond-financed property. When the Authority sells the *profit a prende* interest, it is conveying a portion of the fee simple to a nongovernmental person. The *profit a prende* interest, like a discrete portion of a facility, is a distinct property interest. Therefore, the private business use may be measured on a reasonable basis that reflects the proportionate benefit to the users, such as fair market value of the interests.

p. PLR 200524015. Use of tax-exempt bond proceeds by a nonprofit corporation consisting of natural gas and electric joint action agencies and natural gas and electric distribution systems that were all political subdivisions will not in and of itself cause private business use. Private business use was determined based on the ultimate use of bond proceeds by the members. In addition, the ruling held that use by a subsidiary of the non-profit formed as a limited liability company similarly did not constitute private business use.

q. PLR 200336001. The distribution of a district's cable television programming by a cable television provider does not constitute a special legal entitlement of the facilities used by the district to produce and distribute such programming.

r. PLR 200323006. The IRS determined, in the context of a governmental stadium financing, that the sale of naming rights to a private business user for a term of years during which the private business would pay the city a certain dollar amount per year in exchange for the identification of the facility by the name selected by the private business in all advertising, communications, etc., would constitute a private business use for purposes of the private business use tests. The IRS concluded that the naming rights agreement resulted in the conveyance of legally enforceable rights with respect to the facility for a term of years; that is, the right to require the facility to be referred to with the name of the private business user. The IRS stated that the naming rights did not result in the private party being a private business user due to ownership, lease, management or other incentive payment contract. However, the "contract provides specific rules regarding the manner in which the facility will be operated, that is, the right to require the facility to be referred to with the name of the private business user's selection and this gives the private business user special legal entitlements to control the use of the facility. The private business use of the facility is described as being simultaneous with the governmental use thereof and was held to be a related use to the governmental use of the facility. The naming rights use is measured by reference to the fair market value of the contract as compared to the fair market value of the facility for each year of the contract. As no information was provided in the recitation of the facts in respect of the fair market value of all of the other uses of the facility, the IRS used the cost of construction of the facility as a reasonable proxy for the minimum value of the facility.

s. PLR 200309003. A new building to be constructed by a 501(c)(3) organization on its campus with bond proceeds would not be built specifically to meet the needs of certain federal agencies with which the Section 501(c)(3) organization had contracts to perform certain services for such agencies and would be available for general public use.

t. PLR 200250004. Notwithstanding the fact that a harbor channel was used mainly by business shippers, the harbor was available for general public use and therefore met the general public use exception to private business use.

u. PLR 200240028. Agency, a joint powers agency, requests on behalf of several of its members (the “Cities”) a ruling that their becoming participating transmission owners in an Independent System Operator (ISO) by entering into an Agreement will not be treated as a deliberate action that causes outstanding Bonds, issued to finance the projects, to be private activity bonds under Section 141 of the 1986 Code or industrial development bonds under Section 103(b) of the 1954 Code. The Agency owns an undivided ownership interest in, or is otherwise entitled to the transfer capability of, each of the projects. The Agency represents that, if it is relying on this ruling, it will apply the provisions of Temporary Regulations Section 1.141-7T(f)(5) to the Bonds. The IRS concludes (1) that entering into the Agreement with the ISO is an action described in Temporary Regulations Section 1.141-7T(f)(5)(ii) because (i) the action is being taken to implement the offering of non-discriminatory, open access tariffs for the use of transmission facilities financed by an issue in a manner consistent with the rules promulgated by the FERC, and (ii) there is no sale, exchange, or other disposition of the projects to a nongovernmental person, and (2) that entering into the Agreement with the ISO will not be treated as a deliberate action for purposes of either the 1986 Code or the 1954 Code.

v. PLR 200222006. A ruling is requested as to whether a Hotel Management Contract will result in private business use. The Management Contract has a stated term of 15 years beginning on the placed-in-service date of the Hotel, but the Hotel Owner and the Manager also entered into a Technical Services and Preopening Agreement that will have a term of about 3 years and will terminate when the Hotel is placed in service. Under the Management Contract, Manager will be paid: (1) a management fee that is a fixed amount per year subject to an annual adjustment beginning in year 5 based on the percentage change in total revenues per available room for a comparable group of hotels in the City, excluding the Hotel; (2) a single productivity reward during the term of the Management Contract; and (3) a centralized services fee that is a stated dollar amount per year, subject to a CPI adjustment, for certain group services that the Manager provides to a majority of hotels that it owns or manages. The management fee, beginning in the third year, and the productivity reward are subject to deferral based on available net revenues but in all events must be paid by or at the termination of the Management Contract. A feasibility study projects that no deferrals will occur. The Manager is required under the Management Contract to pay the Owner an “inducement fee.” The Owner is deemed to repay the Manager a fixed amount per month over the term of the Management Contract. If the Owner terminates the Management Contract other than for cause, the Owner is obligated to repay the remaining outstanding balance of the inducement fee. The Owner will reimburse the Manager for third-party expenses and for the salaries of the Manager’s on-site employees and off-site employees who provide services to the Hotel, but not the salaries of the Hotel executive staff. Ruled: The Management Contract does not result in private business use because: (1) the non-deferrable amount of the management fee and the centralized services fee constitute periodic fixed fees; (2) the deemed repayment of the inducement fee and the expense and salary reimbursement are not compensation to the Manager; (3) although the deferred elements of the Manager’s compensation do not satisfy the requirements of Rev. Proc. 97-13, these deferred elements do not indicate private business use under Regulation Treas. Reg. §1.141-3 (b)(4); and (4) the term of the

Preopening Agreement should not be aggregated with the term of the Management Contract in testing the term of the Contract.

w. PLR 200211022. The Agency, a political subdivision whose 32 members are all municipalities, was created to permit its members to secure a supply of electric power. The Agency issued the Bonds to refinance the acquisition of certain Transmission Facilities. While the Agency is not subject to the jurisdiction of the FERC, the regulatory changes made by the FERC have changed the marketplace for electricity transmission and, in response to these changes, the Agency entered into the Agreement with other transmission facilities owners to form an independent system operator (ISO). Under the Agreement, the Agency will transfer operational control of the Transmission Facilities to the ISO, but the Agency will retain ownership of the Transmissions Facilities. The ISO will provide non-discriminatory access to the transmission facilities by its members pursuant to an open access transmission tariff approved by the FERC. The Agency represents that it will apply the provisions of Treas. Reg. §1.141-7T(f)(5) of the temporary regulations to the Bonds. Ruled: The Agency's entering into the Agreement will not be treated as a deliberate action because it is an action described in Treas. Reg. §1.141-7T(f)(5)(ii), i.e., an action taken to implement the offering of non-discriminatory, open access tariffs for the use of transmission facilities financed by an issue in a manner consistent with the rules promulgated by the FERC.

x. PLR 200211003. Bonds were issued for the University, a state university, to finance the Center, a multipurpose fitness and recreation center. In addition to students, faculty, and staff already using the Center, the University would like to permit various other groups to use the Center. These groups would include spouses and dependent children of students, faculty, and staff of the University; certain retired faculty and staff of the University; a limited number of guests of members of the Center; participants in on-campus programs and non-credit classes sponsored by the University; students participating in activities conducted by the County Board of Education and a governmental agency of the State; persons being recruited by the University as students, faculty, and staff; members paying a fee to undergo health and fitness appraisals; members paying a fee for University-employed personal trainers; members paying a fee for use of equipment necessary for outdoor recreational activities; and nonmembers using a juice bar. Ruled: The proposed uses of the Center will not constitute private business use.

y. PLR 200205009. Conduit Borrower, a 501(c)(3) organization, has used the Vessel to conduct expeditions. The Borrower is proposing to use the Vessel for several months to provide ferry service to the public by entering into a non-renewable agreement with the Manager to provide this ferry service for a term of less than one year. The Borrower and Manager will each be responsible for specified costs. The Manager will collect passenger fees on behalf of the Borrower and will retain a specified amount for each passenger trip. In addition, the Manager will retain a percentage of the gross revenues from the galley service. These amounts are described as reasonable. The Borrower will reimburse the Manager for costs incurred by the Manager in the operation of the galley service to the extent those costs are owed to third parties and do not exceed the remaining receipts from the galley service. These costs do not include amounts paid to the Manager's employees as salary or wages. Ruled: The proposed agreement complies with Rev. Proc. 97-13 because the Manager's compensation consists of a per-unit fee and a percentage of gross revenues, compensation is not based on net profits, compensation has been represented to be reasonable, reimbursement of expenses is not considered as compensation, the term of the

agreement is less than one year, and this is the commencement of a new activity for the Vessel and the Borrower.

z. PLR 200132017. University/Medical School (University), a 501(c)(3) organization, owns research facilities with respect to which the University enters into Qualified Research Arrangements, which do not result in private business use, and Non-Qualified Research Arrangements, which do not result in private business use. Over the last “a” years, research revenue from Qualified Research Arrangements has averaged “b%” of total research revenue. Authority proposes to issue Bonds to finance new research facilities for the University. More than 5% of the new research facilities will be used for Non-Qualified Research Arrangements each year throughout the term of the Bonds. University makes a series of representations demonstrating that it is not possible for the University to allocate the usage of the research facilities between Non-Qualified Research Arrangements and Qualified Research Arrangements other than based on the relative amounts of revenue from such arrangements. Ruled: Proceeds of the Bonds may be allocated to the portions of the new research facilities that are used for Qualified Research Arrangements, with such portions based on the ratio of the present value of revenues from Qualified Research Arrangements to the present value of total research revenue, using the yield on the Bonds as the discount rate.

aa. PLR 200123057. B, a 501(c)(3) organization and qualified user of bond proceeds that operates a hospital and medical clinics, is the sole member of C, a taxable nonprofit corporation that provides professional services to B. B appoints 3 of 7 members of C’s board of directors. The chief executive officer of B is one of those 3 members of C’s board. One additional director of C’s, must contemporaneously be a community representative (appointed by B) on B’s board of directors. As a result, 4 of the 7 members on C’s board of directors are either appointed by or are on B’s board of directors. B has entered into a professional services agreement with C, pursuant to which C agrees to provide professional medical services to B. B has the power to approve the following with respect to C: (1) amendments to articles of incorporation and bylaws; (2) capital budgets, incurrence of long term debt, and operating budgets; (3) strategic plans; (4) risk management policies; (5) human resources and benefit policies; (6) health plan, payor or risk contracting agreements; and (7) merger, consolidation, dissolution, or sale or transfer of assets other than in the ordinary course of business. In addition, C is required to obtain B’s approval of its proposed budget on an annual basis. Section 5.04 of Rev. Proc. 97-13 requires that a service provider not have any role or relationship with the qualified user that, in effect, substantially limits the qualified user’s ability to exercise its rights, including cancellation rights, under a service contract. A safe harbor is provided, but C and B are related and do not meet the safe harbor. Ruled: C does not have any role or relationship with B that substantially limits B’s ability to exercise its rights, including cancellation rights, under the professional service agreement.

bb. PLR 200026020. City owns and operates a sewage enterprise system that includes a treatment plant and a reservoir for storing treated effluent from the plant. The bond-financed project includes a pipeline running from City’s existing sewage system to a thermally active geyser field. The pipeline will consist of a Multi-Use Pipeline section and a Geyser Field Pipeline section. Under a contract with Company, City will be obligated to deliver to the geyser field a quantity of wastewater per day equal to about 27% of the capacity of the Multi-Use Pipeline. The remaining capacity of the Multi-Use Pipeline will be available to provide

irrigation water to various persons along its route. The aggregate amounts received under irrigation contracts will not exceed 5% of the debt service on the bonds. In general, Company will neither pay City for the wastewater nor share with City any revenues from the sale of electricity it generates at the geyser field. Ruled (reviewable ruling under Section 4 of Revenue Procedure 96-16): Project is not an output facility; even if the project is an output facility, the contract must be analyzed under Regulation Treas. Reg. §1.141-3 and 1.141-4 because it provides Company with specific performance rights; project is not a water facility; project is used in the trade or business of Company and the private business use test is met; sewer fees paid by ratepayers are private payments and the private payment or security test is met. Related case is City of Santa Rosa, California v. Commissioner, 120 T.C. No. 12 (2003).

cc. PLR 19950036. The Authority owns a hydroelectric generating facility (Project). The Federal Act requires the Authority to allocate b percent of the total power produced by the Project (Preference Power) to a group of customers consisting of public body Governmental Preference Customers and nonprofit cooperatives, which are considered nongovernmental persons. The Federal Act further allocates Preference Power between Preference Customers within and outside the State. In selling to out-of-state Preference Customers, the Authority deals with bargaining agents. All Governmental Preference Customers are publicly-owned utilities that sell energy directly to retail end-users and are governmental entities. Currently, the Governmental Preference Customers' aggregate contractual right to Project capacity is f percent of the capacity of the Project. In-state Governmental Preference Customers resell to various end-users, including customers who are natural persons not engaged in a trade or business. No such retail customers purchase Governmental Preference Power under an arrangement that conveys priority rights or other preferential benefits. All Governmental Preference Power that is sold to the out-of-state Governmental Preference Customers is resold to retail customers, including customers who are natural persons not engaged in a trade or business. With respect to certain out-of-state Governmental Preference Customers, no such retail customers purchase Governmental Preference Power under an arrangement that conveys priority rights or other preferential benefits. For all other out-of-state Governmental Preference Customers, payments that are substantially certain to be made in any year by each such out-of-state Governmental Preference Customer do not exceed 0.5 percent of the expected average annual debt service on the Proposed Debt. Bargaining agents are permitted to enter into arrangements with out-of-state Governmental Preference Customers that allow those customers to resell Governmental Preference Power at wholesale (non-conforming sale) if the Authority approves the non-conforming sale, but the Authority has not, and does not expect to, approve any non-conforming sales. The Authority proposes to use the proceeds of the Proposed Debt to finance additional costs relating to a portion of the Project, namely the f percent of Project capacity that is allocable to the use of Governmental Preference Customers. Ruled: (1) the portion of the Project (f percent, based on the Governmental Preference Customers' entitlement to Project capacity) allocable to the Governmental Preference Customers represents an identifiable interest in the Project, and (2) in part because all resales of Governmental Preference Power will satisfy either the Treas. Reg. §1.141-7T(f)(1) exception for small purchases of output or will satisfy the Treas. Reg. §1.141-3(c) exception to the private business use test and because the bargaining agents act on behalf of the out-of-state Governmental Preference Customers and are disregarded under Treas. Reg. §1.141.7T(f)(6) in determining whether the private business tests are met with respect to the Project, the use of the portion of the Project allocable to the Governmental Preference Customers will not cause the Proposed Debt to satisfy the private business tests.

dd. PLR 199931042. Districts Q and I are political subdivisions formed to provide health care for residents of County. Q and I have signed an affiliation agreement to provide for the cooperation and coordination of the Q and I hospital systems to create an integrated health care delivery system. M, a new 501(c)(3) organization the sole members of which are Q and I, has been formed to serve as the parent of the system. M will coordinate any financial sharing between Q and I, as well as between the various entities admitted to the system. Q and I have certain reserved powers. In the past Q and I have issued various issues of governmental bonds and 501(c)(3) bonds. Held: (i) certain affiliates are instrumentalities of Q and I; (ii) M is an instrumentality of Q and I; (iii) M is an “affiliate of a governmental unit” as described in Section 4 of Revenue Procedure 95-48 and relieved of filing Form 990; (iv) the execution of the agreement will not result in the creation of an entity separate from M for tax purposes; and (v) the execution and implementation of the agreement will not result in a change in use of any Q bonds that will cause them to be private activity bonds or in a change in use of any I bonds that will cause them to be other than qualified 501(c)(3) bonds.

ee. PLR 199929041. Two 501(c)(3) organizations formed a joint venture, Q, which includes several tax-exempt and two taxable subsidiaries. The IRS had previously ruled that the joint venture would not affect the exempt status of the organizations. Various portions of the facilities of certain exempt hospital subsidiaries were financed with proceeds of a 1987 bond issue. A 1998 bond issue was issued to finance the construction of a replacement hospital. Q, a limited liability company, will be treated as a partnership for tax purposes. Based on the representations of the 501(c)(3) members as to the application of the revenues of Q, the IRS held that the implementation of the joint operating agreement (which will result in Q being substituted as the sole member of the 501(c)(3) organizations that own the bond-financed facilities) will not cause the facilities to be owned or used in the trade or business of a person other than a governmental unit or a 501(c)(3) organization.

ff. PLR 199927042. A ruling was requested that proposed affiliation and economic integration agreements will not result in private use that could impact outstanding bonds. The parent of an exempt hospital system and an unrelated exempt entity, which has numerous subsidiaries, will enter into these agreements to create a single integrated health care delivery network. The parties will retain their respective assets. The proposed agreements will not result in use of the bond-financed facilities by a Section 501(c)(3) organization.

gg. PLR 199914045. Corporation is a 501(c)(3) organization with the primary exempt purpose of performing “scientific research in the public interest.” Substantially all of Corporation’s research enters the public domain through scientific and technical publications, presentations, use by the Corporation or provisions of services to its clients. Currently, Corporation has numerous scientific research contracts with terms ranging from six months to five years. The typical contract has a one-year term with no renewal requirements. The funding under federal contracts may be reduced at any time by the federal government. Corporation has no affiliation with the federal government, even if much of its research is performed for its agencies. The contracts do not grant clients ownership of any intellectual property developed or discovered in the course of research. Under applicable federal rules, certain special rules apply with respect to licenses, etc. The price to be paid by any federal agency for the use of any discovery will not be less than the price payable by any non-federal agency for the use of any discovery and will not be less than the price payable by any non-federal party for use of same property. Held: The

research contract is for basic research as such term is used in Revenue Procedure 97-14 (“Rev. Proc. 97-14”). Further, the services to the federal agencies will not constitute private business use within the meaning of Code Sections 141(b) or 145(a). Additionally, payments by the federal government under these contracts will not cause the bonds to be federally guaranteed within the meaning of Code Section 149(b).

hh. PLR 9844022 and PLR 9844019. Qualified 501(c)(3) bonds were issued by Q and loaned to 501(c)(3) organization T to finance the construction and acquisition of Clinic. State S issued bonds to refund other bond issues and make improvements to an acute teaching hospital operated by S. Such bonds were issued as governmental bonds. S and T have entered into an operating agreement, forming new entity W. S and T each provided 50% of the initial operating capital of W. W will provide common management of the facilities of S and T. The IRS finds that the arrangement created by the joint operating agreement lacks the essential corporate characteristics of continuity of life and limited liability, making it a partnership. Use by a partnership is generally private business use. However, the purposes of Code Section 145 are realized if partnership is treated as an aggregate instead of a separate entity using the bond-financed facilities. The operating agreement does not create any joint ownership of operating assets now separately owned by S and T. Certain actions, including disposal of property and incurrence of debt, require consent of both S and T. The joint operating agreement does not transfer the benefits of tax-exempt financing to the partnership. Based on the foregoing, none of the bonds will be treated as used for private business use under Code Sections 141(b) or 145(a).

ii. PLR 9842005, PLR 9841008 and PLR 9841009. State R created a special tax district Q to operate a hospital. The members of Q’s governing body are appointed by the governor of R; Q has the power of eminent domain. S, a 501(c)(3) organization, was formed to provide facilities, hospital and related healthcare facilities for Q; Q is the sole member of S. Pursuant to a reorganization, Q will lease or transfer substantially all of its assets to S, which thereafter will be responsible for the operation of the hospital. X, a 501(c)(3) organization the sole member of which is Q, was formed to acquire the assets and business of an HMO. P, another 501(c)(3) organization, was also formed by Q to own certain buildings that will be leased by P to Q. Q has issued various issues of governmental bonds, both for new money and refunding purposes. Held: (i) Q qualifies as a political subdivision of R, (ii) each of S, X and P are instrumentalities of Q, and (iii) the execution and implementation of the transfer and lease arrangements between the various subsidiaries will not result in a change in use of bond proceeds.

jj. PLR 9835032. Prison was constructed with taxable bonds; Issuer R wants to issue tax-exempt bonds to refund them. Prison was not designed to meet specific needs of federal prisoners. However, R has entered into intergovernmental agreement with U.S. Marshals Service (“IGA”). Under IGA, (i) R is not required to reserve any particular number of beds for federal prisoners, (ii) United States to pay negotiated per diem rate comparable to fees paid by nonfederal governments, and (iii) United States has no enforceable right to renew IGA. IGA has 90-day term and is comparable in terms to agreements entered into by R with nonfederal governments. Held: use of prison by federal prisoners is general public use.

kk. PLR 9823008. R, Political subdivision, will issue bonds to (i) acquire common stock of OE, investor-owned utility, (ii) pay the cost of redemption or conversion in cash of OE preferred stock and debt, (iii) finance improvements, and (iv) pay

transaction expenses. After acquisition transaction, R will control new utility, NE, appoint its board, and approve its budgets and major contracts. NE will be managed pursuant to contract (outlined in the ruling) which does not meet Rev. Proc. 97-13. Ruled: (i) transaction meets transition rule exception to 141 (d) limitation on output facilities, (ii) purchase of stock with bond proceeds is an indirect purchase of OE electric system for purposes of Code Section 103 and Code Sections 141 through 150, (iii) NE will be governmental person, making its use of bond proceeds a governmental use, (iv) notwithstanding the fact that the management agreement does not meet Rev. Proc. 97-13, it does not give rise to private use, and (v) use of proceeds to pay property tax settlement is extraordinary item under Treas. Reg. §1.148-6(d). See companion PLR 9823012.

ll. PLR 9816017. State agency to issue bonds for benefit of 501(c)(3), C, and State University U. Bonds will finance public infrastructure projects for U. U's board of trustees is governmental body established to oversee operation of U and other campuses; members are selected by governor of State N and subject to consent of senate. C was formed on initiative of administrators of U as an auxiliary organization. C engages in activities relating to housing, acquisition and development of real estate, and other activities which are "integral part of the educational mission" of U. C is to undertake similar activities in connection with bond-financed facilities. U's president and board of directors together elect C's board of directors. U's board may remove directors of C except for U's president, who serves as ex officio member. C's funds are gifts and grants which must be used under the control and oversight procedures of U. U's board of trustees has access to all of C's records and audits them annually. On dissolution, C's assets are to be distributed to successor 501(c)(3) organization approved by U. Held: C meets the criteria of Revenue Ruling 57-128 as a state instrumentality and that, as such, C's trade or business is that of a governmental unit and, therefore, not private business use for purposes of Code Section 141(b).

mm. PLR 9813003. T, joint powers agency, has as members two cities, X and Y. T has all powers necessary, including power of eminent domain and power to issue bonds, to develop and implement Corridor Project. Among other things, Corridor Project aims to alleviate traffic to and from the ports of X and Y by consolidating rail traffic, thereby increasing their efficiency and competitiveness. Corridor Project will also include many sub-projects including removal of buildings, relocation of water and sewer lines, road and bridge expenditures, highway overpasses, etc. Corridor Project includes construction of Trench to separate the rail facilities from adjacent and crossing roads; Trench is the largest component of Corridor Project and will be utilized by railroads to access ports. Pursuant to Memorandum of Understanding, railroads will pay user fees for use of Trench. Amounts paid by railroads will be used to repay, among other things, the debt incurred to finance Corridor Project. The IRS considered the allocation of bond proceeds to the various components of Corridor Project (street improvements, non-Trench grade separations, Trench bridges, etc.) under the private activity tests and concluded such components constitute governmental improvements to street and roads which are available for use by the public and owned by governmental units and with respect to which the railroads have no special legal entitlement; accordingly, it is held that the railroads are not treated as private business users of these improvements. With respect to Trench, the IRS noted that the public improvements, including Trench, are not appropriately treated as discrete facilities under Treas. Reg. §1.141-3(g)(4)(iv). IRS also noted that railroads will derive substantial benefit and pay fees for the use of Trench. Because Trench is functionally related to the rail facilities and facilities owned by X and Y, Trench is properly treated as "common area" to multiple facilities. IRS

concluded that 50% of the cost of Trench could be allocated to the street improvements. Finally, where utilities are under no legal obligation to relocate the lines, utilities are not treated as private business users of proceeds used for relocation; however, to the extent such relocation is allocable to construction of Trench, relocation costs should be treated accordingly.

nn. PLR 9807015. Authority was formed as a nonprofit membership organization to coordinate the operation of electric generation resources and the purchase and sale of electric power on behalf of its members. The members are governmental units or instrumentalities thereof. No portion of Authority's earnings inures to the benefit of any individual or any private person; in the event of dissolution, assets of the Authority are distributed ratably to the members. Each member has contributed and agrees to contribute additional capital as needed; expenses and gains on transactions not specifically benefiting one member are allocated to members equitably. Authority is treated as a wholly-owned instrumentality of its members for purposes of Code Section 141.

oo. PLR 9741013. State authority issues Notes secured by general obligation notes of Academies. The proceeds of the Notes are used to purchase notes of the Academies, which are temporary debt incurred to pay school operations. The Academy notes are secured by the State school aid allocated to the respective Academies. The Notes were issued prior to the effective date of Treas. Reg. §1.141-1. Academies are created under State law and, for purposes of receiving school aid, tuition policy, etc., are treated on the same basis as public elementary and secondary schools. The board of each Academy is formed so that there is no private inurement in the organization or operation of the Academy, and the board members are subject to control and supervision of the State Board of Education. State law expressly permits and fosters the creation of Academies, and State is a principal source of operating expenses. Ruled: under State law, each Academy is a governmental unit for purposes of determining use under private activity bond tests and private financing loan test.

pp. PLR 9740016 and PLR 9740015. City 1 and City 2, together with private participants, own undivided interests in a nuclear electric generating facility. The various owners propose that the project be operated by O, a nonstock, nonmember, nonprofit corporation under state law that will not be a 501(c)(3) organization. Pursuant to Operating Agreement, O is authorized to maintain and operate the project on behalf of the owners, executing all contracts relating to maintenance, improvement, etc. Each participant will pay its respective share of the costs of operation. O will have no ownership interest. City 1 and City 2 have elected to apply Treas. Reg. §1.141-3(b)(4) to the bonds. Because the project is public utility property, O's operation of it will not be treated as a management contract if the only compensation to O is the reimbursement of actual and direct expenses and of reasonable administrative overhead. Ruled: (1) The Operating Agreement imposes reasonable limitations on O's reimbursable costs; (2) the arrangement will not pass on any benefits of tax-exempt financing to O or any of the private participants; and (3) the Operating Agreement is not an arrangement that gives rise to private business use.

7. City of Santa Rosa, California v. Commissioner, 120 T.C. No. 12 (2003), held that a private entity did not use a bond-financed pipeline for treated wastewater "in any quantifiable amount" when it took delivery of water from the pipeline and used the water to generate steam by injecting the water into a geyser steam-field. The steam-field boiled the water

into steam for use in generating electricity. The IRS had ruled negatively on the question on various theories alleging private business use in excess of 10% (PLR 200026020). Appeal was not sought by the IRS and U.S. Department of Justice. The IRS has published neither an acquiescence nor a non-acquiescence in the case.

C. Qualified Management Contracts.

1. General. Treas. Reg. §1.141-3(b)(4) states the general rule that, except as otherwise provided therein, a management contract may result in private business use of bond-financed property based on all the facts and circumstances. A management contract similarly results in private business use if, based on all the facts and circumstances, the service provider is treated as the lessee or owner of the bond-financed property for federal income tax purposes.

2. Definition. Treas. Reg. §1.141-3(b)(4) defines a management contract to be a management, service, or incentive payment contract between a governmental person and a service provider under which the service provider provides services involving all or a portion of, or any function of, the financed facility. A management contract includes not only a contract that provides for the actual management of a facility (such as an operator of a cafeteria or a hospital or a nursing home), but also one that provides services (such as a contract to provide medical services, other than as an employee, to patients of a hospital whether or not compensation is paid directly by the hospital or by patients or third party payers). Arrangements not treated as management contracts include: (i) contracts for services that are incidental to the primary function of the facility (e.g., janitorial services, office equipment repair, hospital billing), (ii) the granting of admitting privileges by a hospital, (iii) a contract to provide for the operation of public utility property (as defined in Code Section 168(i)(10)) if the only compensation is reimbursement of direct expenses and reasonable administrative overhead expenses, and (iv) a contract to provide services, if the only compensation is the reimbursement of the service provider for direct expenses paid by the service provider to unrelated parties. There appears to be continuing debate, for purposes of this provision and the section of Rev. Proc. 2017-13 that excludes the reimbursement of expenses paid to unrelated third parties from the manager's compensation, whether the reimbursement of employee salaries and wages paid by the management fall within that rule. See PLR 200222006 (statement in facts that employees for whom reimbursement is sought do not include executive staff) and PLR 200205009 (statement in facts that reimbursed costs do not include amounts paid by manager as salaries and wages). These PLRs are referenced below.

3. Qualifying Management Contract Safe Harbor Arrangements. Revenue Procedure 1997-13, as modified by Revenue Procedure 2001 -39 ("Rev. Proc. 97-13") provided certain bright line tests that if satisfied would allow a management or service contract to be treated as not giving rise to private business use. On August 22, 2016, the IRS released Revenue Procedure 2016-44 ("Rev. Proc. 2016-44"), which modified Rev. Proc. 97-13 and section 3.02 of Notice 2014-67 (discussed below), to provide new safe harbor terms under which management contracts will not result in private business use. Rev. Proc. 2016-44 applies a more principles-based approach focusing on governmental control over projects, governmental bearing of risk of loss, economic lives of managed projects, and consistency of tax positions taken by the service provider. The IRS subsequently modified, amplified and superseded Rev. Proc. 2016-44 in Revenue Procedure 2017-13 ("Rev. Proc. 2017-13"). Rev. Proc. 2017-13 provided certain clarifications and amendments to Rev. Proc. 2016-44 to address certain types of compensation, the

timing of payment of compensation, the treatment of land and methods of approval of rates. Rev. Proc. 2017-13 is generally effective for management contracts entered into, materially modified or extended (other than pursuant to a renewal option) on or after January 17, 2017. Issuers may elect to apply Rev. Proc. 97-13 to contracts entered into before August 18, 2017, provided that such contracts are not materially modified or extended (other than pursuant to a renewal option) on or after August 18, 2017.

4. Rev. Proc. 2017-13

Rev. Proc. 2017-13 applies to any management contract involving managed property financed with the proceeds of an issue of governmental bonds or qualified 501(c)(3) bonds. A management contract is defined to mean a management, service, or incentive payment contract between a qualified user and a service provider under which the service provider provides services for a managed property. Rev. Proc. 2017-13 clarifies that a management contract does not include a contract or portion of a contract for the provision of services before a managed property is placed in service (for example, pre-operating services for construction design or construction management). The term “managed property” is defined to mean the portion of a project with respect to which a service provider provides services. Treas. Reg. §1.141-6(a)(3) defines project to mean one or more facilities or capital projects, including land, buildings, equipment, or other property, financed in whole or in part with proceeds of the issue. The definition of qualified user is consistent with the definition as set forth in Rev. Proc. 97-13.

If a management contract meets each of the requirements set forth in Rev. Proc. 2017-13, or is “an eligible expense reimbursement arrangement,” the management contract does not result in private business use (the “2017-13 Safe Harbor”). Rev. Proc. 2017-13 also provides that a service provider’s use of a project that is functionally related and subordinate to performance of its services under a management contract for managed property that meets the 2017-13 Safe Harbor does not result in private business use. For example, the use of storage areas to store equipment used to perform activities required under the management contract that meets the 2017-13 Safe Harbor does not result in private business use.

a. Reasonable Compensation. Payments to the service provider under the contract must be reasonable compensation for services rendered during the term of the contract. Compensation includes payments to reimburse actual and direct expenses paid by the service provider and related administrative overhead expenses of the service provider. Under Rev. Proc. 97-13, reimbursement of the service provider for actual and direct expenses paid by the service provider to unrelated parties is not by itself treated as compensation. For this purpose, employees of the service provider are treated as unrelated parties. Under Rev. Proc. 2017-13, payments for reimbursement to the service provider and administrative overhead of the service provider must be analyzed with other forms and methods of compensation to determine if that compensation is reasonable, is not based on a share of net profit, and does not result in the service provider bearing net losses, as described below.

b. No Net Profits Arrangements. The restriction against sharing of net profits under Rev. Proc. 97-13 and its predecessors was brought forward. Under Rev. Proc. 2017-13 the management contract must not provide to the service provider a share of the net profits from the operation of the managed property. Compensation to the service provider will not be treated as

providing a share of net profits if no element of the compensation takes into account, or is contingent upon, either the managed property's net profits or both the managed property's revenues and expenses (other than any reimbursements of direct and actual expenses paid by the service provider to unrelated third parties) for any fiscal period. The "elements of the compensation" are the eligibility for, the amount of, and the timing of the payment of the compensation. Unrelated parties are defined as persons other than either (i) a related party (as defined in the Regulations) to the service provider or (ii) a service provider's employee. In addition, incentive compensation is not treated as providing a share of net profits if the eligibility for the incentive compensation is determined by the service provider's performance in meeting one or more standards that measure quality of services, performance, or productivity, and the amount and the timing of the payment of the compensation otherwise meet the requirements set forth in this paragraph.

c. No Burden of Net Losses. The management contract must not, in substance, impose upon the service provider the burden of bearing any share of net losses from the operation of the managed property. An arrangement will not be treated as requiring the service provider to bear a share of net losses if: (a) the determination of the amount of the service provider's compensation and the amount of any expenses to be paid by the service provider (and not reimbursed), separately and collectively, do not take into account either the managed property's net losses or both the managed property's revenues and expenses for any fiscal period; and (b) the timing of the payment of compensation is not contingent upon the managed property's net losses. Compensation can however be reduced by a stated dollar amount (or one of multiple stated dollar amounts) for failure to keep the managed property's expenses below a specified target (or one of multiple specified targets) without being treated as bearing a share of net losses as a result of this reduction. Without regard to whether the service provider pays expenses with respect to the operation of the managed property without reimbursement by the qualified user, compensation for services will not be treated as providing a share of net profits or requiring the service provider to bear a share of net losses if the compensation for services is (i) based solely on a capitation fee, a periodic fixed fee, or a per-unit fee; (ii) incentive compensation (as described above) or (iii) a combination of these types of compensation. *Capitation fee* and *periodic fixed fee* retain the definitions under Rev. Proc. 97-13. The definition of *per-unit fee* in Rev. Proc. 97-13 provides that separate billing arrangements between physicians and hospitals generally are treated as per-unit fees; Rev. Proc. 2017-13 removes the word "generally," and confirms the treatment of separate billing arrangements as per-unit fees.

d. Treatment and Timing of Compensation. The deferral of compensation (that otherwise meets the requirements of Rev. Proc. 2017-13) due to insufficient net cash flows from the operation of the managed property will not cause the deferred compensation to be treated as contingent upon net profits or losses if the contract includes requirements that: (i) the compensation is payable at least annually; (ii) the qualified user is subject to reasonable consequences for late payment, such as reasonable interest charges or late payment fees; and (iii) the qualified user will pay such deferred compensation (with interest or late payment fees) no later than the end of five years after the original due date of the payment.

e. Contract Term. The term of the contract, including all renewal options, must be no greater than the lesser of (a) 80 percent of the weighted average reasonably

expected economic life of the managed property or (b) 30 years³. Economic life is determined in the same manner as under Code Section 147(b) as of the beginning of the term of the contract. Thus, land will be treated as having an economic life of 30 years if 25 percent or more of the net proceeds of the issue that finances the managed property is to be used to finance the costs of such land. A contract that is materially modified with respect to any matters relevant to its treatment as a qualified contract under Rev. Proc. 2017-13 is retested for compliance with Rev. Proc. 2017-13 as a new contract as of the date of the material modification.

f. Control over Use of Managed Property. The qualified user must exercise a significant degree of control over the use of the managed property. This requirement is met if the contract requires the qualified user to approve (a) the annual budget of the managed property, (b) capital expenditures with respect to the managed property, (c) each disposition of property that is part of the managed property, (d) rates charged for the use of the managed property and (e) the general nature and type of use of the managed property. A qualified user may show approval of capital expenditures for a managed property by approving an annual budget for capital expenditures described by functional purpose and specific maximum amounts; and it may show approval of dispositions of property that is part of the managed property in a similar manner. In addition, a qualified user may show approval of rates charged for use of the managed property by either (i) expressly approving such rates or a general description of the methodology for setting such rates (such as a method that establishes hotel room rates using specified revenue goals based on comparable properties) or (ii) by including in the contract a requirement that the service provider charge rates that are reasonable and customary as specifically determined by, or negotiated with, an independent third party.

g. Risk of Loss with respect to Managed Property. The qualified user must bear the risk of loss upon damage or destruction of the managed property (for example, due to force majeure). The qualified user will not fail to meet this requirement as a result of insuring against risk of loss through a third party or imposing upon the service provider a penalty for failure to operate the managed property in accordance with the standards set forth in the management contract.

h. No Inconsistent Tax Position. The service provider must agree that it is not entitled to and will not take any tax position that is inconsistent with being a service provider to the qualified user with respect to the managed property. For example, the service provider must agree not to claim any depreciation or amortization deduction, investment tax credit, or deduction for any payment as rent with respect to the managed property.

i. No Circumstances Substantially Limiting Exercise of Rights. The service provider must not have any role or relationship with the qualified user that, in effect, substantially limits the qualified user's ability to exercise its rights under the contract, based on all the facts and circumstances. A service provider will not be treated as having a prohibited role or relationship with the qualified user if: (i) no more than 20 percent of the voting power of the governing body of the qualified user is vested in the directors, officers, shareholders, partners,

³ Note that to fit within the 2017-13 Safe Harbor (other than as an eligible expense reimbursement arrangement), the economic life limitation on the contract term must be satisfied regardless of how short or long the term of the contract.

members, and employees of the service provider, in the aggregate; (ii) the governing body of the qualified user does not include the chief executive officer of the service provider or the chairperson (or equivalent executive) of the service provider's governing body; and (iii) the chief executive officer of the service provider is not the chief executive officer of the qualified user or any related parties of the qualified user.

For purposes of this provision, the term "chief executive officer" includes a person with equivalent management responsibilities. In addition, the term "service provider" includes the service provider's related parties. A "related party" is defined to mean, with respect to a qualified user, any member of the same controlled group (as defined in Treas. Reg. 1.150-1(e)) and, with respect to a person other than a qualified user, a related person (defined by reference to Code Section 144(a)(3)).

5. Eligible Expense Reimbursement Arrangements. For management contracts that are considered to be "eligible expense reimbursement arrangements," such contracts are deemed to meet the safe harbor of Rev. Proc. 2017-13 and will not result in private business use. An eligible expense reimbursement arrangement is defined to mean a management contract under which the only compensation consists of reimbursements of actual and direct expenses paid by the service provider to unrelated parties and reasonable related administrative overhead expenses of the service provider. An "unrelated party" is defined to mean persons other than a related party to the service provider or a service provider's employee. Rev. Proc. 2017-13 treats employees of the service provider as related for purposes of expense reimbursement, a deviation from prior IRS guidance.

6. Net Profits. Management contracts in which the service provider is compensated with a capitation fee, periodic fixed fee, per unit fee, qualitative incentive payment or any combination of such fees will not be deemed to be based, in whole or in part, on net profits of the managed property irrespective of any expense reimbursement paid to the service provider, including expenses paid to related persons (e.g., employees of the service provider). Other forms of compensation such as those based on a percentage of gross revenues or non-qualitative incentive payments are not provided this same protection.

7. Facts and Circumstances Test. A management contract that fails to satisfy a safe harbor from private business use does not automatically create private business use. Instead, the contract should be analyzed under the general rule that a management contract gives rise to private business use based on all the facts and circumstances.⁴ The IRS has issued a number of private letter rulings (for example, PLR 201726007, 201622003 and PLR 201338026) that deal with contracts that fall outside the safe harbors in Rev. Proc. 97-13. The IRS often ruled that the contract did not give rise to private business use under the facts and circumstances test. Because the facts and circumstances test is contained in the Treasury Regulations, which have not changed even after the IRS released Rev. Proc. 2017-13, these rulings should continue to have some value as guidance.

⁴ Bond Counsel may be reluctant to rely on the facts and circumstances test to render an unqualified opinion that interest on the bonds is excluded from gross income for federal income tax purposes without a private letter ruling issued specifically to the qualified user.

8. Revenue Procedure 97-13 (Qualifying Management Contract Safe Harbors). Rev. Proc. 97-13 states that the arrangements set forth below are qualifying management contracts:

a. 95% Periodic Fixed Fee Arrangement/15 and 20 Year Contracts. At least 95% of the compensation is based on a periodic fixed fee. The term of the contract, including all renewal options, must not exceed the lesser of 80% of the reasonably expected useful life of the financed property and 15 years (20 years for “public utility property” as defined in Code Section 168(I) (10)). A one-time fixed dollar incentive award based on a gross revenue or expense target (but not both) is permitted.

b. 80% Periodic Fixed Fee Arrangement/10 and 20 Year Contracts. At least 80% of the compensation is based on a periodic fixed fee. The contract term, including all renewal options, must not exceed the lesser of 80% of the reasonably expected useful life of the financed property and 10 years (20 years for public utility property). Again, a one-time fixed dollar incentive award based on a gross revenue or expense target (but not both) is permitted.

c. 50% Fixed Fee Arrangements/5 Year Contracts. Either 50% of the compensation is based on a periodic fixed fee or 100% of the compensation is based upon a capitation fee or a combination of a capitation fee and periodic fixed fee. The contract term, including renewal options, must not exceed 5 years and the contract must be terminable by the qualified user (governmental entity or qualified 501(c)(3) organization, where applicable) without penalty or cause at the end of the third year of the contract term.

d. Per-Unit Fee Arrangements/Certain 3 Year Contracts. All of the compensation is based on a per-unit fee or a combination of a per-unit fee and a periodic fixed fee. The term of the contract, including all renewal options, must not exceed 3 years. The contract must be terminable by the qualified user without penalty or cause at the end of the second year.

e. Percentage of Revenue or Expense Fee Arrangements/2 Year Contracts. All of the compensation for services is based on a percentage of fees charged or a combination of a per-unit fee and a percentage of revenue or expense fee. The term of the contract, including renewal options, must not exceed 2 years and the contract must be terminable by the qualified user without penalty or cause at the end of the first year of the contract. The contract safe harbor is limited to circumstances involving services to third parties (*e.g.*, radiology services to patients) or certain start-up situations. Periodic fixed fees and, pursuant to the amendments to Rev. Proc. 97-13 set forth in Revenue Procedure 2001-39, capitation fees and per unit fees may be automatically increased according to a specified, objective, external standard that is not linked to the output or efficiency of a facility.

4. Notice 2014-67.

a. Notice 2014-67 “amplifies” the existing safe harbors of Rev. Proc. 97-13. One of the key provisions of Rev. Proc. 97-13 is the prohibition of compensation based on net profits. The Notice states that a productivity reward for services during the term of a contract does not cause the compensation to be based on a share of net profits of the financed facility if:

(1) the eligibility for the productivity award (the Notice renames this as an “award” rather than “reward”) is based on the quality of the services provided under the management contract (for example, the achievement of Medicare Shared Savings Program quality performance standards or meeting data reporting requirements), rather than increases in revenues or decreases in expenses of the facility; and (2) the amount of the productivity award is a stated dollar amount, a periodic fixed fee, or a tiered system of stated dollar amounts or periodic fixed fees based solely on the level of performance achieved with respect to the applicable measure.

b. The Notice created a new safe harbor for certain five-year contracts under the Permissible Arrangements section of Rev. Proc. 97-13. This safe harbor permits compensation for services based on a stated amount, periodic fixed fee, a capitation fee, a per unit fee, or a percentage of gross revenues, adjusted gross revenues, or expenses of the facility (but not both revenues and expenses). In addition, the safe harbor does not require that the contract be terminable by the qualified user of the facility prior to the end of the term. Under the Rev. Proc. 97-13 safe harbors, the permissible two-year, three-year and five-year arrangements require that the governmental or 501(c)(3) organization have the ability to terminate without cause at an earlier date. The Notice did not eliminate the existing two, three and five-year contract safe harbors.

c. The expanded five-year safe harbor is effective for contracts entered into, materially modified, or extended (other than pursuant to a renewal option) on or after January 22, 2015, but may also be applied to contracts entered into before January 22, 2015.

9. Private Letter Rulings.

a. PLR 202229002. A management contract for a hotel under which the manager is paid a management fee consisting of three components: (i) a tiered percentage of gross revenues from hotel operations, (ii) reimbursement to the service provider for operating expenses, including employee costs, such as salaries, fringe benefits, incentive compensation and bonuses, and (iii) reimbursement of the hotel’s allocable share of centralized services the service provider provides, such as promotion and marketing, centralized reservations, guest incentive programs and technology services. The ruling notes that incentive compensation and bonuses to senior management employees for which the service provider is reimbursed are evaluated based on formulas used to measure performance of the hotel, by factors that include the hotel’s financial performance, guest experience and individual goals. Employee bonuses and incentive compensation are payable as a percentage of the employees’ respective salaries and the timing and amount of such bonuses and incentive compensation are not contingent upon net profits from the operations of the hotel. The contract was determined to not satisfy all of the safe harbor conditions under Rev. Proc. 2017-13 because the compensation to the service provider included reimbursement of employee costs of the service provider. Such employee costs included bonuses and incentive compensation paid by the service provider to its employees that are based, in part, on the hotel’s financial performance. However, the ruling concludes that the incentive compensation and bonuses that are reimbursed to the service provider under the agreement are not compensation based, in whole or in part, on a share of net profits from the hotel operations and, under the facts and circumstances, the contract is a management contract that does not result in private use of the hotel by the service provider.

Language in the ruling that the contract did not comply with Section 502(2) of the ruling because the compensation included reimbursement expenses may be overbroad. Such assertion may mistakenly imply that the reimbursement of employee expenses, in and of itself, would cause a contract to not comply with Revenue Procedure 2017-13. Rather, the IRS could have stated that reimbursement of employee expenses constitutes “compensation” for purposes of Revenue Procedure 2017-13, and the elements of such compensation must be examined to determine whether any such element is based on a sharing of net profits.

b. PLR 201726007. A teaching hospital service agreement between a school and a county hospital was determined to be a management contract; however, such management contract did not satisfy all of the safe harbor conditions under Rev. Proc. 2017-13. Thus, the determination of whether the agreement resulted in private business use depended on the facts and circumstances test. Ultimately, the agreement was held not to result in private business use after examination through the lens of the safe harbors under Rev. Proc. 2017-13. There was no compensation to the hospital, the manager, *i.e.*, the school did not bear any share of the costs or losses from the operation of the hospital, the term did not exceed 30 years or 80 percent of the useful of the hospital, the school bore no risk of loss for the facility, the school was not entitled to take any tax position inconsistent with that of a service provider, had no prohibited relationships with the hospital, and had no control over the operations, nature or general use of the hospital.

c. PLR 201622003. A management contract for a hotel under which the manager would receive base fee equal to a percentage of the hotel’s annual gross revenues and incentive pay in any year in which certain tests were met does not result in private use. The contract did not meet all criteria of Rev. Proc. 97-13 as amplified by Notice 2014-67, however, a review of the facts and circumstances supported a ruling that the management contract did not result in private business use of the hotel because the incentive fee, while partly based on a variant of net profits, was not derived from net profits and was treated as a share of gross revenue and the term of the contract was reasonable under the facts and circumstances.

d. PLR 201338026. A management contract under which a hospital would pay a medical group base compensation, incentive compensation and reimbursement of certain expenditures did not result in private business use of the clinical facilities. Using the factors of Rev. Proc. 97-13, the IRS concluded that neither the hospital’s payment or reimbursement of the medical group’s miscellaneous or compensation expenses supported a conclusion that the management contract resulted in private business use of the clinical facilities because those expenses were not calculated based on net profits. Likewise, the facts and circumstances of the incentive pay of the medical group’s president did not support a conclusion that the management contract caused private business use of the clinical facilities because the metric used would not be based on net profits.

e. PLR 201228029. Though the fixed fee component of a manager’s compensation did not qualify as a periodic fixed fee because it allowed for adjustments based on reduced credit support or poor performance, it did not result in private business use because it was not based on net profits and, after adjustment, would remain a stated amount for the particular annual period. Additionally, pass-through expenditures that included mark-up would not create private business use because they were based on federally-regulated cost allocation methods and not net profits of the facility.

f. PLR 201145005. A management contract for a municipally-owned, bond-financed exhibition and convention center provided for three types of compensation: (1) a base fee, (2) an incentive fee, and (3) reimbursement of certain expenses. In order to receive the incentive fee, the manager must attain (1) operating revenues equal to or greater than a target benchmark, (2) a stated net operating surplus/deficit level for the fiscal year, established in advance each fiscal year and (3) an average overall customer satisfaction score equal to or greater than a target benchmark. The amount of the incentive fee was adjustable, but in no event would exceed the annual base fee.

The IRS concluded that the incentive fee (particularly the revenue benchmark and the net operating surplus/deficit benchmark) did not constitute compensation based on a share of net profits because “the amount of the incentive fee paid to the Manager will not vary depending on the margin of increase in revenues and/or decrease in expenses or be based on a percentage of revenue increases, a percentage of expenses decreases, or some combination of both.” Additionally, the IRS stated that “although the net operating surplus/deficit benchmark takes into account both expenses and revenues, it is not based on increases in revenues and decreases in expenses, but on stated surplus/deficit amounts that may reflect decreasing revenues and increasing expenses.”

g. PLR 200926005. A hospital facility financed with the proceeds of qualified 501(c)(3) bonds proposed to enter into professional service agreements with certain contracting physicians. The agreements provided that the hospital would reimburse certain expenses incurred by the physicians, and the physicians would be compensated based on a percentage of net professional patient billings, which under the agreements consisted of gross patient billings provided by each such contracting physician, adjusted for certain items, including certain insurance discounts. The contracting physicians would also receive supplemental compensation paid into a non-qualified deferred compensation plan and could also be compensated for supervising “physician extenders” (nurse practitioners and physician assistants).

The IRS initially found that the agreements were “management contracts” within the meaning of Treas. Reg. §1.141-3(b)(4)(ii), and that the contracts did not satisfy the safe harbors set forth in Rev. Proc. 97-13. The IRS went on to consider whether, under all of the facts and circumstances the agreements resulted in a private business use of the facility. Using the facts and circumstances analysis, the IRS determined that the agreements did not result in a private business use of the facility, largely because (1) the compensation under the agreements consisted of a percentage of fees generated by the physicians, adjusted for items such as bad debts and insurance discounts, which was deemed by the IRS to closely resemble a permissible arrangement under Rev. Proc. 97-13, (2) the agreements provided for reasonable compensation, partly because the agreements allowed the hospital the right to review physician compensation that reaches a certain percentage of an objective industry standard, (3) a physician’s base compensation was based not on a share of the net profits from the operation of the facility, but rather on a percentage of adjusted gross revenues allocable to the physician, (4) none of the expenses of the facility or of the contracting physicians were taken into account in determining a physicians’ base compensation, (5) the physician’s incentive compensation was based on how the physician met specific goals, none of which were based on the number of patients treated by the physician at the facility, the productivity of the facility or the net profits of the hospital, (6) the amount of deferred compensation that a physician was eligible to receive was not based upon the net profits of the

hospital or the productivity of the physician at the hospital, (7) the terms of the agreements were specifically tailored to address the difficulties encountered by the health care industry in the hospital's coverage area in attracting and retaining physicians, and (8) none of the physicians entering into the agreements were related parties with the hospital or the entity owning the hospital for purposes of Code Section 1.150-1(b), and none of the physicians had a role in or relationship with the hospital or the entity owning the hospital that substantially limited the ability of the hospital and the entity to exercise their rights under the respective agreements.

h. PLR 200813016. A 10-year contract with a private manager of a county-owned solid waste disposal facility provided for an arm's-length negotiated 80 percent fixed compensation and 20 percent variable compensation based upon the volume of solid waste handled by the manager. In addition, the manager was to be compensated extra (determined without regard to the 20 percent variable limit) in the event of excessive rainfall in the county and in the event of hurricane or major storm declared emergencies occurred. The contract was held not to meet the requirements of the Rev. Proc. 97-13 safe harbor, but nonetheless did not create private business use under all the facts and circumstances presented by the county, including the likelihood of excessive rainfall.

i. PLR 200651012. A dormitory management contract between a university and its wholly owned taxable subsidiary did not give rise to private business use. The university was the sole shareholder of the manager and appointed all its members of the board of directors and had the power to approve its articles and by-laws, budgets, strategic plans and even its dissolution. The contract was for a period of 15 years, which was less than 80% of the useful life of the facility. Compensation was paid based on a fixed annual fee, adjusted only for changes in the consumer price index, plus reimbursements for direct expenses. The university had the right to terminate the contract on 90 days written notice at the end of each year. Under these facts and circumstances, the IRS concluded that the manager does not have any role or relationship that would limit the university's ability to exercise its rights under the contract (including the cancellation rights) and, thus, the contract did not give rise to private business use.

j. PLR 200330010. Though compensation arrangement did not meet the safe harbor, 20-year public utility contract nonetheless was held not to give rise to private business use.

k. PLR 200222006. Hotel management contract, having a 15-year term, providing several forms of compensation, including some employee expenses, and entered into in connection with a "Preopening Agreement" with a term of about 3 years, is a qualified management contract.

l. PLR 200205009. Management contract with a term of less than one year under which the manager receives a per unit fee plus a percentage of revenues, as well as reimbursement of third-party expenses but not employee costs, complies with Rev. Proc. 97-13.

m. PLR 200123057. Because a Section 501(c)(3) medical organization controls a majority of the board of directors of a taxable professional corporation and has substantial powers over that corporation's budgeting and operations, the Section 501(c)(3) organization is not substantially limited in the exercise of its rights under a service agreement between the Section 501(c)(3) organization and the taxable corporation.

D. Research Agreements.

1. General. Treas. Reg. § 1.141-3(b)(6) states the general rule that, except as otherwise provided therein, an agreement by a nongovernmental person to sponsor research performed by a governmental person may result in private business use of bond-financed property based on all the facts and circumstances. Unless otherwise provided in Treas. Reg. § 1.141-3(b)(6), an arrangement that results in the sponsor being treated as the lessee or owner of the bond-financed property for federal income tax purposes will give rise to private business use of the bond-financed property. Research means basic research or the original investigation of scientific knowledge not having a specific commercial objective. Product testing supporting nongovernmental trades or businesses is not basic research.

2. Revenue Procedure 2007-47. Revenue Procedure 2007-47 (“Rev. Proc. 2007-47”, which superseded Revenue Procedure 97-14), contains two safe harbors for research agreements. The first is for “corporate-sponsored” research agreements. Under this safe harbor, any licensee of the sponsor is permitted to use the results of research only on the same terms which the owner of a bond-financed facility would permit use by an unrelated party. In other words, the sponsor must pay a competitive price for the right to use the results of the research funded by that sponsor, and the price must be determined at the time the technology is available for use.

The second safe harbor is for industry or federally-sponsored research agreements in which one or more sponsors agree to fund basic research. This safe harbor requires that (1) the research to be performed and the manner in which it is to be performed be determined by the owner of the bond-financed property (*i.e.*, the governmental person), (2) title to any product resulting from the research lies exclusively with the issuer and (3) the sponsors be entitled to no more than a nonexclusive, royalty-free license to use the product of that research. Rev. Proc. 2007-47 provides that the rights of the federal government under the Bayh-Dole Act will not cause an arrangement to fall out of second safe harbor so long as (1) and (2) are met and the license to use any resulting product of the research granted to any third party is no more than a “nonexclusive, royalty-free license.”

3. Private Letter Rulings.

a. PLR 200347009. Interprets Rev. Proc. 97-14 to conclude that a license agreement will cause an issue of bonds to meet the private business use tests where a corporation was given an exclusive, perpetual, non-terminable, worldwide license to all of the research created at the bond-financed facility and the exclusive right to sublicense the research to any person of the corporation’s choice.

b. PLR 200309003. Organization’s research contracts with two agencies of the federal government do not give rise to either private business use or federal guarantee where neither of the agency contracts requires that the organization perform any activities at the facility, and the facility will not be constructed to meet the specific needs of the federal agencies.

c. PLR 199914045. Federal research contracts do not give rise to private business use or federal guarantee where research is basic and is not generally being used a

specific commercial objective and the availability of federal revenues is not dependent upon a default on debt service payments.

E. Output Contracts. Certain output contracts (including take-or-pay and take-and-pay arrangements) can give rise to private business use. Output contracts relate to output facilities, which are electric and gas generation, transmission, distribution, and related facilities, and water collection, storage, and distribution facilities. On September 19, 2002, the IRS released final output regulations which generally apply to bonds sold on or after November 22, 2002. The output regulations contain special rules to determine whether arrangements for the purchase of output from an output facility (including water facilities) cause an issue of bonds to meet the private business tests. A detailed description of these rules is set forth in Section VII of this outline. Note, however, that the rules of Treas. Reg. § 1.141-3 still apply for non-output types of uses of an output facility (*e.g.*, pursuant to a management contract or lease).

1. In PLR 201037006, under facts similar to PLR 200915002, the IRS concluded that the sale of “renewable energy certificates” under contract did not result in private business use. The private letter ruling explained that a number of states are now imposing mandatory compliance programs that require some or all electric utilities providing service within those states to demonstrate that a specific portion of their electric supplies are derived from renewable generating resources. Many states imposing such standards allow utilities to meet those requirements by purchasing renewable energy certificates (“RECs”). The RECs represent the environmental attributes of renewable energy, with one REC representing the attributes for one MW hour generated by a renewable energy resource.

The issuer was a public instrumentality that had the authority to acquire, construct, and operate electric generating facilities, to sell electricity generated by such facilities, and in connection with such activities it issued tax-exempt governmental bonds to finance an electric generating project that would give rise to RECs. The issuer will sell all output from the bond-financed facility to a company, which is not currently subject to the REC requirements. The issuer proposed to enter into contracts with nongovernmental purchasers that would require the purchaser to buy the lesser of the stated amount of RECs or all of the RECs associated with the project’s generation of electricity for the period stated. The IRS emphasized that the sale of RECs did not entitle the purchaser to any electric energy from the project, that although the contract provides for liquidated damages in the event of non-delivery of RECs to purchaser, the issuer had exclusive control over the project and its operations, and that because it was unlikely that the purchaser would be awarded specific performance for issuer’s nonperformance under the contract, purchaser could not use legal or equitable remedies to force issuer to operate the facility at any particular level.

2. In PLR 200915002, the IRS concluded that the sale of RECs generated with respect to a bond-financed output facility did not give rise to private business use, because the purchasers of the RECs received no right to use the output property and the RECs did not represent capacity generated by or use of the property.

3. PLR 200739005 concludes that the private business use test was not met where an agreement granted a private utility the rights to all of the capacity and output of a bond-financed generating plant in exchange for agreeing to provide a public water provider with a certain

amount of energy at all times, reasoning that the agreement met the so-called “swapping agreement” safe-harbor of Treas. Reg. § 1.141-7(f)(2).

F. General Public Use.

1. General. Private business use does not include use as a member of the general public. Use of financed property by nongovernmental persons in their trades or businesses is treated as general public use only if the property is intended to be available, and in fact is reasonably available, for use by natural persons not engaged in a trade or business.

2. Use on the Same Basis. Use of the financed facility under an arrangement that conveys priority rights or other preferential benefits is not use on the same basis as the general public. Rates that are generally applicable and uniformly applied do not convey priority rights. Rates may be treated as generally applicable and uniformly applied, even if (i) different rates apply to different classes of users, if the differences in rates are customary and reasonable; and (ii) a specially negotiated arrangement is entered into, but only if the user is prohibited by federal law from paying generally applicable rates and the terms of the arrangement are as comparable as reasonably possible to the generally applicable rates.

3. 200 Day Use Arrangements. General public use property may be subject to an arrangement for temporary exclusive use of up to 200 days, including all renewal options. A right of first refusal to renew is not included in the term of the arrangement if the renewal price is at generally applicable fair market value rates and the use of the property under the same or similar arrangements is predominantly by natural persons not engaged in a trade or business. The maximum number of days permitted usage under this exception is absolute, and not a per-year limit; therefore, a contract that contemplates 50 days use every year for 5 years would not satisfy this use exception.

G. Special Rules for Affordable Care Organizations.

1. Notice 2014-67 provides specific relief for 501(c)(3) organizations participating in “accountable care organizations” (“ACOs”).

2. The Notice provides interim guidance regarding private business use of tax-exempt bond-financed facilities that are used by “accountable care organizations” under the Patient Protection and Affordable Care Act (the “ACA”). The ACA created the “Shared Savings Program” to achieve efficiencies in providing medical care under Medicare through cost savings, improved coordination of services, and investment in infrastructure. This program contemplates that 501(c)(3) organizations could enter into an ACO with physicians or other health care group practices, a network of individual practices, or a partnership or joint venture. The ACO is required to be a separate legal entity, must share “governance” as provided in the ACO guidance, and must distribute Shared Savings Program payments. The arrangement promoted by one federal program raised obvious concerns for 501(c)(3) health care organizations because it would likely be treated as a “partnership” under the private activity bond regulations or potentially give rise to net profits which would take the arrangements out of the management contract safe harbor guidelines.

3. The Notice states that the participation of an organization in the Shared Savings Program through an ACO will not result in private business use of a tax-exempt

bond-financed facility used by the organization or ACO if the following conditions are met: (a) The Centers for Medicare & Medicaid Services has accepted the ACO into the Shared Savings Program, and the ACO has not been terminated from the program, (b) The terms of the organization's participation in the Shared Savings Program through the ACO are established in a written agreement negotiated at arm's length. (c) The organization's share of economic benefits derived from the ACO (including payments received under the Shared Savings Program) is proportional to the benefits or contributions the organization provides to the ACO. If the organization receives an ownership interest in the ACO, the ownership interest received is proportional and equal in value to its capital contributions to the ACO, and all ACO returns of capital, allocations, and distributions are made in proportion to ownership interests. (d) The organization's share of ACO losses does not exceed the share of ACO economic benefits to which the organization is entitled in (c) above. (e) All contracts and transactions entered into by the organization with the ACO and the ACO's participants, and by the ACO with the ACO's participants and any other parties, are at fair market value. (f) The organization does not contribute or otherwise transfer the tax-exempt bond-financed property to the ACO unless the ACO is an entity that is a "governmental person" or, in the case of 501(c)(3) bonds, either a "governmental person" or a "501(c)(3) organization," as such terms are defined for tax purposes.

4. The ACO provisions apply to bonds sold on or after January 22, 2015, but may also be applied to bonds sold before that date. There is no specific election to apply the provision to bonds issued before the effective date

H. Other Exceptions.

1. General. Treas. Reg. §1.141-3(d) provides additional exceptions to private business use for use of bond-financed property by an agent, use incidental to financing arrangements, certain short-term uses not involving ownership by a nongovernmental person (see below), certain temporary use of bond-financed property by developers (see below), "incidental use" and use of proceeds to provide "qualified improvements" (see below).

2. Certain Short-term Arrangements. Certain short-term arrangements for the use of bond-financed property not involving the ownership of the property by a nongovernmental person will not result in private business use.

a. Permitted 100 Day Arrangements. An arrangement for the use of bond-financed property by a nongovernmental person will be permitted for a period of up to 100 days (including renewal options), if the arrangement would be treated as general public use, except that (i) the property is not available for use by natural persons not engaged in a trade or business, and (ii) the property was not financed for the purpose of providing the property to that nongovernmental person.

b. Permitted 50 Day Arrangements. An arrangement for the use of bond-financed property by a nongovernmental person will be permitted for a period of up to 50 days (including renewal options), if (i) the arrangement is a negotiated arm's length arrangement, (ii) the compensation is at fair market value, and (iii) the property was not financed for the purpose of providing the property to that nongovernmental person.

c. These permitted number of day arrangements are applied as described in F.3. above, by reference to the total number of days of use contemplated over the life of the contract, not by reference to the term/duration of the contract.

3. Temporary Use by Developer. Use by developer of a bond-financed improvement that carries out an essential governmental function during an initial development period will not give rise to private business use if the issuer and developer reasonably expect to proceed with all reasonable speed to develop the improvement and property benefited by that improvement and to transfer the improvement to a governmental person, and if the improvement is in fact transferred to a governmental person promptly after the property benefited by the improvement is developed.

4. Incidental Use and Qualified Improvements.

a. Incidental Use. Non-possessory uses of a financed facility that in the aggregate do not involve more than 2.5% of the facility may be disregarded for the purposes of determining private business use if the non-possessory use is not functionally related to some other use of the facility by the same person (e.g., pay telephones, vending machines, advertising displays and use for television cameras).

b. Qualified Improvements. Proceeds that provide “qualified improvements” are not used for private business use. Qualified improvements are governmentally-owned improvements to an existing governmentally-owned building, where the building was originally placed in service more than 1 year before the improvements are acquired or constructed, the improvements do not involve an enlargement of the building or an improvement of interior space used exclusively for a private business use, the improved building is not pledged as security for the bonds and not more than 15% of the improved building is used for private business use.

I. Special Rules for Tax Assessment Bonds. A deemed loan in a tax assessment bond situation is ignored for the purposes of the private loan financing test if the tax assessment bond financing satisfies the requirements of Treas. Reg. §1.141-5(d) (relating to tax assessment bond financings that are permitted under the tax assessment bond exception to the private loan financing test). *See* Section V below.

J. Measurement of Private Business Use.

1. General. The amount of private business use of property is determined according to the average percentage of private business use during the measurement period. In general, the measurement period begins on the later of the issue date or the date the property is placed in service and ends on the earlier of the last date of the reasonably expected economic life of the property or the latest maturity date of any bond of the issue financing the property. The average percentage of private business use is the average of the percentages of private business use during the 1-year periods within the measurement period. (If the private business use arises from ownership by a nongovernmental person or if the bonds are outstanding longer than reasonably necessary, the amount of private business use is the greatest percentage of private business use in any 1-year period.)

Under Treas. Reg. §§1.141-3(g)(3) and (4), the measure of private business use in any year generally is the average percentage of private business use to total actual use (disregarding periods of non-use of bond-financed property) in that year. The measure of such use over the entire measurement period is based on the average of the annual percentages of such use. The focus on average annual use instead of some present value computation is administratively easier. The disregard of non-use, however, while perhaps theoretically sound, can increase administrative tracking burdens for states and local governments because it can produce a frequently-changing denominator in the private business use percentages. It would seem equally sound from a tax policy standpoint and administratively easier to treat unused portions of bond-financed property for which a governmental unit is economically responsible as governmental use.

a. Uses at Different Times. For property used for private business use and governmental use at different times, the average amount of private business use generally is based on the amount of time that the property is used for private business use as a percentage of total time for all actual use. “Dark time” is disregarded.

b. Simultaneous Use. If property is used for governmental use and private business use simultaneously, the entire facility is treated as having private business use; however, if the governmental use and private business use is on the same basis, the average amount of private business use may be determined on a reasonable basis that reflects the proportionate benefit to be derived by the various users of the facility.

c. Common Areas, Neutral Costs. The amount of private business use of common areas is based on a reasonable method that properly reflects the proportionate benefit to be derived by the users of the facility. Neutral costs must be allocated ratably among the other purposes for which the proceeds are used.

d. Discrete Portion Use. In measuring private business use of a discrete portion of a facility, discrete portions are treated as separate facilities. For example, a discrete portion includes a floor of a building or a portion of a building separated by walls.

2. Commencement of Use. Private business use commences on the first date on which there is a right to actual use by the nongovernmental person. However, if ownership or other long-term use is involved, and the issuer enters into an “arrangement” for private business use for a substantial period (10% of measurement period) before the right to actual use commences, private business use commences on the date of the arrangement.

3. Fair Market Value. If private business use is reasonably expected as of the issue date to have a significantly greater fair market value than governmental use, the average amount of private business use must be determined according to the “relative reasonably expected fair market values” of use. The determination of relative fair market value may be made as of the date the property is acquired or placed in service if this determination is not reasonably possible on the issue date. “Relative reasonably expected fair market value” must be determined by taking into account the amount of reasonably expected payments for private business use in a manner that properly reflects the proportionate benefit to be derived from the private business use.

4. Private Letter Rulings.

a. PLR 200323006. Governmental entity's sale of naming rights to stadium meets private business tests. *See* description of private letter ruling at III.B.6. above.

b. PLR 200304015. The bond portion of the cost of constructing a stadium eligible to be financed with the proceeds of a tax-exempt bond issue was determined based upon (i) an allocation method reflecting physically discrete areas and corresponding common area costs; and (ii) an allocation method reflecting relative temporal units of use and the corresponding common area costs.

c. PLR 200132017. A university research facility that is used for both private business use and Section 501(c)(3) use may determine the portion of the facility used for Section 501(c)(3) use based on the ratio of revenue from non-private business use to total research revenue.

K. Treatment of Partnerships.

1. General Rule. Final Allocation Regulations § 1.141-1(e) provides that a partnership "is treated as an aggregate of its partners, rather than as an entity." These Regulations provide flexibility to both state and local government and 501(c)(3) organizations to, in certain instances, finance, with tax-exempt obligations, such entity's "partner's share" of property owned by a partnership. Treas. Reg. § 1.141-3(g)(2)(v).

2. Partner's Share Determination. The Final Allocation Regulations (defined below under Section VI.A) provide that the amount of private business use by a nongovernmental person of property resulting from a partnership is that nongovernmental "partner's share" of the amount of use of the property by the partnership. Treas. Reg. §1.141-3(g)(2)(v). A "partner's share" is defined as the "nongovernmental partner's greatest percentage share under section 704(b) of any partnership item of income, gain, loss, deduction, or credit attributable to the period that the partnership uses the property during the measurement period." Treas. Reg. §1.141-3(g)(2)(v) clarifies that if a partnership item varies, then the "partner's share" will be the highest percentage, and Treas. Reg. §1.141-3(g)(2)(B) provides that guidance may be published in the Internal Revenue Bulletin to assist issuers in determining a "partner's share." Clarification is needed that mandatory allocations under Code Section 704(b) of the Code and the Treasury Regulations promulgated thereunder that, similar to the alternative depreciation system rules for tax-exempt use property under Code Section 168(h)(6), issuers can disregard such mandatory allocations that otherwise comply with relevant Code and regulation provisions.

IV. PRIVATE SECURITY OR PAYMENT TEST - SECTION 1.141-4

A. General Rule.

1. Private Security. The private security portion of the private payment or security test takes into account the payment of any debt service on the issue that is directly or indirectly secured by any interest in (i) property used or to be used for private business use; or (ii) payments in respect of property used or to be used for a private business use.

2. Private Payment. The private payment portion of this test takes into account the payment of any debt service on the issue that is directly or indirectly to be derived from

payments (whether to the issuer or to any related party) in respect of property, or borrowed money, used or to be used for private business use.

3. Aggregation of the Two Tests.

Payments taken into account as private payments and payments or property taken into account as private security are aggregated for the purposes of determining whether private security and/or payments exceed 10% (or in certain cases, 5%) of the debt service on the bonds, provided that no payment is taken into account under both prongs of the test.

4. Underlying Arrangement. Payments include payments made pursuant to an underlying arrangement and may result from agreements among the parties or may be based on facts and circumstances surrounding the issuance of the bonds. The Regulations give an example (Treas. Reg. §1.141-4(g), Example 2) of debt service being secured by a full faith and credit pledge and interest in property used in private business use. *See also* Revenue Ruling 80-251 and Revenue Ruling 73-481, in which, because only tax increments secured the bond issue, the pre-1986 “security interest” test was failed. Compare Revenue Rulings 80-251 and 80-339, which made inroads to the liberal conclusion of Revenue Ruling 73-481, demonstrating the concept of “underlying arrangement.”

B. Measurement of Private Security and Payments.

1. Private Security. For purposes of determining the present value of debt service secured by property, such property is valued at its fair market value as of the first date on which such property secures the bond issue.

2. Private Payment. The present value of any payments or property taken into account is compared to the present value of the debt service to be paid over the term of the issue.

a. General. Debt service on the issue does not include any amount paid or to be paid from sale proceeds or investment proceeds of the issue (*e.g.*, capitalized interest, earnings on a debt service reserve fund applied to the payment of debt service, etc.). Debt service on the issue is adjusted to take into account payments and receipts that adjust the yield on the issue for the purposes of Code Section 148(f) (*e.g.*, qualified guarantee fees). The yield on the issue is used as a discount rate for the purposes of computing present values. In general, yield is determined on the issue date and is not adjusted to take into account subsequent events. For a variable issue yield, the issuer may assume the future interest rate on the variable yield bonds, except as described below.

b. Deliberate Actions and Variable Yield Issues. Deliberate actions require a recomputation of the variable issue’s yield, determined as of the date of the deliberate action, for purposes of determining the present value of the payments to be made pursuant to the arrangement that constitutes the deliberate action.

(i) The Regulations appear not to require a recomputation of the present value of payments made and to be made pursuant to the original arrangement in place prior to the deliberate action. Although Treas. Reg. §1.141-4(g), Example 3, which demonstrates the principle of recomputing the yield for purposes of calculating the present value of payments to be

made under the new arrangement giving rise to the deliberate action, does not explicitly address this point, its silence suggests that the present value of the payments made under the original arrangement are not changed. Additionally, the language in Treas. Reg. §1.141-4(b)(iii)(C) appears to support that conclusion.

(ii) If the deliberate action consists of the modification of the original arrangement (*e.g.*, the leasing of an additional floor to an existing tenant) rather than the issuer's entering into an arrangement with a separate person (as in Example 3), it is not clear whether the present value of payments already made under the original arrangement must be recalculated.

C. Private Payments.

1. General. Payments for a use of proceeds include payments (whether or not to the issuer) in respect of property financed (directly or indirectly) with those proceeds, even if not made by a private business user (*e.g.*, parking fees paid by members of the general public for use of a parking garage that is managed under a nonqualifying management agreement constitute payments taken into account).

2. Payments Not to Exceed Use.

a. General. Payments with respect to proceeds used for a private business use are not taken into account to the extent that the present value of the payments exceeds the present value of the debt service on those proceeds.

b. Allocation Based on Time. Payments are taken into account only to the extent they are made for the period of time proceeds are used for a private business use. For example, payments made by the general public to attend events at a governmentally owned stadium would be taken into account only to the extent allocable to the periods in which there is private business use. Payments for events involving performers who are not considered private business users (*e.g.*, due to the short length of their arrangement) would not be taken into account.

3. Scope of Payments. Payments for a use of proceeds include "payments of debt service on the issue that is directly or indirectly to be derived from payments (whether or not to the issuer or any related party) in respect of property ... used or to be used for a private business use". Treas. Reg. §1.141-4(a)(1).

a. History: 1986 Blue Book. This point historically received much debate. The 1986 Tax Act's Blue Book suggested that only payments actually made by private persons are taken into account. *See Blue Book*, p. 1161: "Payments from persons who are not treated as using the bond proceeds under the trade or business use test, described above, are not counted unless the payments are pledged to pay debt service or otherwise satisfy the prior-law security interest test."

b. Post-1986 Practice. This question came up frequently in the context of land-based financings (*e.g.*, special assessment bonds), in which payments were clearly being made by the general public, and also tended to arise with respect to convention centers, stadiums and the like.

c. Regulations Example. Treas. Reg. §1.141-4(g), Example 5, illustrates the position of the IRS. In that example, hospital is managed pursuant to a nonqualified management contract that results in private business use. Hospital revenues are treated as payments in respect of property used for a private business use. *See also* PLR 200026020 wherein sewage ratepayers are similarly situated to the patients paying for hospital services in Treas. Reg. §1.141-4(g), Example 5, with the consequence that their payment results in private payments.

d. Payments Not in Respect of Financed Property: Utility Relocation. Treas. Reg. §1.141-4(g), Example 4 addresses the relocation of utility lines. There, the theory was that, although the utility lines are privately owned and the utility customers whose property was being assessed make payments to the utility company for the use of the utility lines, the assessments were payments in respect of the cost of relocating the utility lines, and not the cost of the lines themselves.

4. “Fair Market Value of Other Property” Carve-Out. The Regulations provide that payments are not considered made in respect of financed property if those payments are directly allocable to other property directly used by the payor and the payments represent fair market value compensation for the other use. For example, if a person has been previously using city-owned property that was not bond-financed and has been paying fair market value rent for the use of such property, if the city then bond finances a different piece of property which it rents to such person, the amount of previously payable rent will continue to remain allocable to the pre-existing property.

5. The “Use Cap”. Payments with respect to proceeds used for a private business use are not taken into account to the extent the present value of the payments exceeds the present value of debt service on those proceeds. Since the present value of debt service on proceeds will roughly equate to the amount of the proceeds, the amount of the proceeds used for the private business use will serve as a cap on the amount of payments taken into account. This would appear to be relevant only in the context of multiple uses, where the application of the cap would prevent the “crossing over” of payments to a different use.

6. Operating Expenses. Ordinary and necessary expenses (as defined under Code Section 162) directly attributable to the operation and maintenance of the financed property may be used to offset payments paid for the use of proceeds. General overhead and administrative expenses may not be taken into account for these purposes.

7. Refinanced Debt Service.

a. General. Payments of debt service on an issue to be made from the proceeds of a refunding issue will be treated as involving private payments in the same proportion as the present value of the payments taken into account as private payments for the refunding issue bears to the present value of the debt service to be paid on a refunding issue. However, deliberate actions taken more than 3 years after the retirement of the refunded issue that are not reasonably expected on the issue date of the refunding issue, will be disregarded for the purposes of the refunded issue.

b. Example. If all debt service on a note is paid with the proceeds of a refunding issue, the note meets the private security or payment test if and to the extent the refunding issue meets the private security or payment test. To determine whether an issue is a refunding issue for this purpose, the exception in Treas. Reg. §1.150-1(d)(2)(i) (relating to the payment of interest) does not apply.

8. Allocation of Payments.

a. General. The allocation of private payments to the source or sources of funding is based on all the facts and circumstances. In general, this allocation is based upon the nexus between the payment, the financed property and the source of funding.

b. PLR 200747009. Payments of net operating revenues and certain reserves were properly allocable first to certain revenue bonds and equipment leases issued by a state port authority and thus did not cause other bonds issued to finance the same construction to meet the private security and or payment test.

c. Discrete Property. Payments for the use of a discrete facility are allocated to the sources of funding for that facility.

d. Multiple Sources of Funding. In general, a payment made for the use of property financed from two or more sources must be allocated to those sources in a manner that reasonably corresponds to the relative amount of those sources. A payment made for the use of property allocated to two or more issues may be allocated to the relative amounts of debt service (both paid and accrued) on the issues during the annual period for which the payment is made, if this allocation reflects economic substance (*e.g.*, the maturity of bonds reflects' economic life of property, and the debt service is approximately level from year to year).

e. Issuance Arrangements. A private payment for the use of property made under an arrangement entered into in connection with the issuance of bonds that finances the property generally is allocated to the issue.

f. Allocations to Equity. A private payment may be allocated to equity before allocation to an issue, only if (i) the issuer adopts an official intent not later than 60 days after an expenditure indicating that the issuer reasonably expects to be repaid from a specific arrangement; and (ii) the private payment is made not later than 18 months after the later of the date the expenditure is made or the date the project is placed in service.

D. Private Security.

1. Security Taken Into Account.

a. General. Property used or to be used for private business use and payments in respect of that property are treated as private security if any interest in that property or payments secures the payment of debt service on the bonds. The property involved need not be financed with the proceeds of the bonds. Proceeds qualifying for an initial temporary period under Treas. Reg. §1.148-2(e)(2) or (3) or a deposit to a reasonably required reserve or replacement fund described in Treas. Reg. §1.148-2(f)(2)(i) are not taken into account before the date on which those

amounts are either expended or loaned by the issuer to an unrelated party. Private security (other than financed property and private payments) is taken into account only to the extent it is provided, directly or indirectly, by a user of the proceeds.

b. Treas. Reg. §1.141-4(g), Example 9. Example 9 demonstrates the principle that property used need not be financed to be private security and sheds light on determining whether obligations are “secured by an interest in property” (note the Code’s language and see below). In the example, County W issues certificates of participation in a lease of a building it owns (an “asset-transfer” lease) and covenants to appropriate annual payments for the lease. More than 10% of the building is used in a private business use. None of the proceeds of the COPs are used with respect to the building but are granted to Corporation Y for the construction of a factory Y will own. Y makes no payments to W and has no relationship with the users of the building securing the COPs. If W defaults under the lease, the trustee for the COP holders has a limited right of repossession under which the trustee may lease the property to a new tenant at fair market value. The example concludes that the COPs are secured by an interest in property used for a private business use. The private security or payment test is not met, however, because the property, which is not being financed by the COPs, is not provided by a private business user.

2. Payments In Respect of Property. The payments taken into account as private security are payments in respect of property used or to be used for private business use. Payments need not be made by the private business user (*e.g.*, payments by persons using a facility that is the subject of a management contract that results in a private business use). Except as provided in paragraph 3 below, in general, the present value rules described above for private payments apply to determine the amount of payments treated as payments in respect of property used or to be used for private business use. *See* PLR 201519015 where the IRS held that the fare revenues collected by an issuer for bus service along a route subject to a nonqualifying management contract under Rev. Proc. 97-13, were not payments in respect of the managed lanes under Code Section 141(b)(2)(B).

3. Allocation of Security among Issues. Property or payments that are taken into account as a private security are allocated to each issue secured by the property or payments on a reasonable basis that takes into account bondholder’s rights to the payments or property upon default.

E. Generally Applicable Taxes.

1. General. Generally applicable taxes are not taken into account for the purposes of the private security or payment test.

2. Definition of Generally Applicable Taxes. A generally applicable tax is an enforced contribution exacted pursuant to legislative authority in the exercise of the taxing power that is imposed and collected for the purpose of raising revenue to be used for governmental or public purposes. A generally applicable tax must have a uniform tax rate that is applied to all persons of the same classification in the appropriate jurisdiction, and a generally applicable manner of determination and collection. Payments for special privileges, services or special benefit assessments are not generally applicable taxes.

3. Manner of Determination and Collection.

a. General. A tax does not have a generally applicable manner of determination and collection (and is therefore not a “generally applicable tax”) to the extent that one or more taxpayers make impermissible agreements relating to payment of those taxes. An impermissible agreement relating to the payment of a tax is taken into account whether or not it is reasonably expected to result in payments that would not otherwise have been made. If an issuer makes a grant of proceeds to a taxpayer to improve property, agreements that impose reasonable conditions on the use of the grant do not cause a tax on that property to not be a generally applicable tax. If an agreement by a taxpayer causes the tax imposed on the taxpayer not to be treated as a generally applicable tax, the entire tax paid by that taxpayer is treated as a special charge unless the agreement is limited to a specific portion of the tax.

b. Examples of Impermissible Agreements:

(i) An agreement to be personally liable on a tax that does not impose personal liability, to provide additional credit support such as a third-party guarantee or to pay unanticipated shortfalls;

(ii) An agreement regarding the minimum market value of property subject to property tax; and

(iii) An agreement not to challenge or seek deferral of the tax.

c. Examples of Permissible Agreements:

(i) An agreement to use a grant for specified purposes (whether or not that agreement is secured),

(ii) A representation regarding the expected value of the property following the improvement;

(iii) An agreement to insure the property and, if damaged, to restore the property;

(iv) A right of a grantor to rescind the grant if property taxes are not paid; and

(v) An agreement to reduce or limit the amount of taxes collected to further a bona fide governmental purpose.

F. Payments In Lieu of Taxes (“PILOTs”).

1. General. On October 24, 2008, the Treasury Department released final Regulations governing the private payment treatment of PILOT payments (the “PILOT Regulations”). Recall that under Treas. Reg. §1.141-4(e)(1) for purposes of the private security or payment test, generally applicable taxes are not payments from a nongovernmental person and are not payments in respect of property used in a private business use. See IV.E of this outline. Thus,

the purpose of the generally applicable taxes exception is to allow eligible tax payments made with respect to property or services to be used to pay debt service on an issue without causing private payments.

The PILOT Regulations conclude that PILOTs are treated as generally applicable taxes if and only if both (i) the payments are commensurate with and not greater than the amounts imposed by the statute for a tax of general application and (ii) the payments are designated for a governmental or public purpose and are not special charges. *See* Treas. Reg. §1.141-4(e)(5).

2. Commensurate Standard.

By retaining a restrictive “commensurate” standard, the PILOT Regulations take a conservative approach to ensuring a close relationship between eligible PILOTs and generally applicable taxes. The PILOT Regulations do not prohibit any use of PILOTs to pay debt service, but provide instead that a PILOT is commensurate with a generally applicable tax only if it is equal to a fixed percentage of the generally applicable tax that would otherwise apply in each year or it reflects a fixed adjustment to the generally applicable tax that would otherwise apply in each year.

A PILOT based upon a property tax must take into account the current assessed value of the property for property tax purposes for each year in which the PILOT is paid and that assessed value must be determined in the same manner and with the same frequency as property subject to the property tax.

A PILOT is not commensurate with a generally applicable tax if the PILOT is set at a fixed dollar amount (e.g., equal to the fixed debt service on a bond issue) that cannot vary with changes in the level of the generally applicable tax on which the PILOT is based.

Under the PILOT Regulations, PILOTs are commensurate even though the amount of the PILOTs are adjusted to accommodate the development, construction or initial start-up periods for the financed project.

3. Public Purpose Standard.

The Preamble to the PILOT Regulations and the text of the PILOT Regulations state that the underlying generally applicable tax upon which the PILOT is based be for public or governmental purposes. The PILOT Regulations require that use of an eligible PILOT be for the governmental or public purposes for which the underlying generally applicable tax on which the PILOT is based.

4. No Special Charges Requirement.

a. Examples of Special Charges. Special charges are not generally applicable taxes. The PILOT Regulations provide that a special charge includes (i) a payment for a special privilege granted or regulatory function (e.g., a license fee), (ii) a service rendered (e.g., a sanitation services fee), (iii) a use of property (e.g., rent), or (iv) a payment in the nature of a special assessment to finance capital improvements that is imposed on a limited class of persons

based on benefits received from the capital improvements financed with the assessment (e.g., amounts charged for sidewalks, streets, streetlights or utility improvements on property owners in a defined area such as an industrial park).

b. Examples of what is Not a Special Charge. By contrast to the list of special charges above, a PILOT based upon an otherwise-qualified generally applicable tax (e.g., a generally applicable ad valorem tax on all real property within a governmental taxing jurisdiction) is not treated as a special charge merely because the PILOTs received are used for governmental or public purposes in a manner that benefits particular property owners.

c. Existence of Tax-Exempt Bonds Not Relevant for Special Charges Determinations. The PILOT Regulations remove the example in the last sentence of Treas. Reg. §1.141-4(e)(5)(ii) of the prior regulations that stated “[f]or example, a payment in lieu of taxes made in consideration for the use of property financed with tax-exempt bonds is treated as a special charge”. This sentence was removed as a technical clarification rather than a substantive change. The Preamble to the PILOT Regulations states that the substantive determination of whether a payment is or is not a special charge (e.g., is a payment for the use of property such as rent) or is a generally applicable tax does not depend upon the presence or absence of tax-exempt bond financing.

5. Effective Dates.

a. General. The PILOT Regulations generally apply to bonds sold on or after October 24, 2008.

b. New Money Project Transition Exception. The prior Regulations apply to new money projects substantially in progress if (i) a governmental person took official action evidencing its preliminary approval of the project to be financed before October 19, 2006, and the plan of finance for the project contemplated PILOTs as security for the bonds, (ii) before October 19, 2006, significant expenditures were paid or incurred with respect to the project or a contract was entered into to pay or incur significant expenditures with respect to the project, and (iii) the bonds for the project (excluding refunding bonds) are issued on or before December 31, 2009.

c. Refunding Exception. The prior Regulations apply to refunding bonds if either (i) the refunded bonds (or the original bonds in a series of refundings) were sold before October 24, 2008, or (ii) the refunded bonds (or the original bonds in a series of refundings) satisfied the project transition exception and (iii) the weighted average maturity of the refunding bonds does not exceed the remaining weighted average maturity of the refunded bonds.

6. Private Letter Rulings. PLR 200640001 (Yankees) and PLR 200641002 (Mets) provide that payments in lieu of taxes made by a private party in connection with the use of baseball stadiums in New York City do not constitute private payments or private security with respect to bonds issued by an agency of the State of New York to finance construction of those baseball stadiums. Because the PILOTs in question are designated for the public purposes of promoting tourism and economic development and are calculated with respect to generally applicable ad valorem taxes, they are “commensurate with” the amounts otherwise imposed by

statute and do not constitute a special charge as defined in Treas. Reg. §1.141-4(e)(5). It is not at all clear that these private letter rulings would have been issued if subject to the PILOT Regulations.

PLR 201246007 (assessment bonds) and its companion PLR 201246032 (lease revenue bonds), provide that assessment bonds and lease revenue bonds issued by an authority to finance the construction of a new convention center wing to be solely owned by a municipality did not satisfy the private loan test where the assessment bonds would be payable from assessments levied on the property of a private company despite such private company's contractual agreements with the municipality, to among other things, construct the new wing, lease the event center, certain related parking and the stadium, and enter into a signage agreement. The IRS held that no direct loan of the proceeds existed and the transaction did not convey to the private company benefits that were the economic equivalent of a loan of the proceeds of the bonds.

PLR 202144007 provides that a portion of the rates and charges to be paid by customers that are private business users of an Agency's water supply system will be treated as private payments where the agency applies bond proceeds to fund costs of replacing lead service lines with copper service lines owned by such customers. The IRS noted that the only way to eliminate health risks from lead leaching into the water pipes owned by residential and commercial customers is to remove the lead service lines and replace them with copper service lines. The Agency will replace such lines for both residential and commercial customers, including residential customers that treat their homes as rental property or residential customers operating a business from their homes. The Agency's customers will own the replacement lines. The Agency will issue the bonds to pay costs of such lead service line replacements and other capital costs of its water supply system. The Agency will not impose special charges on customers who receive lead service line replacements and instead will use the rates and charges that it imposes on all of its customers to pay such costs, including debt service on the bonds that fund such replacement costs and other projects. No property financed by the bonds, other than the replacement service lines serving customers that are private business users, will be used for a private business use. The IRS held that payments of rates and charges by customers that receive lead service pipe replacements and are private business users are, in part, private payments for the bonds to the extents such payments are attributable to the costs of replacing the lead service lines, but because the payments that are both received from customers that are private business users of the lead pipe replacements and attributable to costs of such lead pipe replacements do not exceed 10 percent of the debt service on the bonds, the bonds do not meet the private security or payment test.

G. Waste Remediation Bonds.

1. Persons that are Not Private Business Users. Payments from nongovernmental persons who are not (other than coincidentally) either users of the site being remediated or persons potentially responsible for disposing of hazardous waste from that site are not taken into account as private security. Payments must be made pursuant to either (i) a generally applicable state or local tax statute or (ii) a state or local statute that regulates or restrains activities on an industry-wide basis for persons who are engaged in generating or handling hazardous waste,

or in refining, producing or transferring petroleum, provided that those payments do not represent in substance payments for the use of proceeds.

2. Persons that Are Private Business Users. If the payments from nongovernmental persons who are either users of the site being remediated or persons potentially responsible for disposing of hazardous waste on a site do not secure the payment of the principal of or the interest on a bond (directly or indirectly) under the terms of the bond, the payments are not taken into account as private payments, provided that at the time the bonds are issued, the payments from those nongovernmental persons are not material to the security for the bonds.

V. PRIVATE LOAN FINANCING TEST - SECTION 1.141-5

A. General Rules.

1. Elements of Test. The private loan financing test is met if more than the lesser of 5% or \$5 million of the proceeds of the issue is to be used (directly or indirectly) to make or finance loans to persons other than governmental persons. Treas. Reg. §1.141-2(d) (relating to reasonable expectations and deliberate actions) applies to the private loan financing test.

2. Amount of Loan. The amount actually loaned is not discounted to reflect present value of the loan repayments.

B. Definition of Private Loan.

1. General Federal Tax Principles. Any transaction that is generally characterized as a loan for federal income tax purposes is a loan for the purposes of the private loan financing test. A loan may arise from the direct lending of bond proceeds as well as transactions in which the indirect benefits are the economic equivalent of a loan. For instance, a lease or other contractual arrangement may in substance constitute a loan if the arrangement transfers tax ownership of the facility to a nongovernmental person.

2. Non-purpose Investments; Prepayments. A loan that is a non-purpose investment does not cause the private loan financing test to be met. Except as otherwise provided in the Regulations, a prepayment for property or services is treated as a loan for the purposes of the private loan financing test if a principal purpose for prepaying is to provide a benefit of tax-exempt financing to the seller. A prepayment is not treated as a loan if (i) prepayments on substantially the same terms are made by a substantial percentage of persons who are similarly situated to the issuer but who are not beneficiaries of a tax-exempt financing, (ii) the prepayments is made within 90 days of the reasonably expected date of delivery of the property or services for which the prepayment is made, or (iii) the prepayment satisfies special rules Treas. Reg. §1.141-1(e)(2)(iii) with respect to prepayments for the acquisition of a supply of natural gas or electricity.

4. Grants, Tax Increment Financing. A grant of proceeds is not a loan. A grant using proceeds of an issue that is secured by generally applicable taxes is not treated as a loan, unless the grantee makes an impermissible agreement that results in taxes not being treated as generally applicable as defined in Treas. Reg. §1.141-4(e). In such case, the entire grant is treated as a loan unless the impermissible agreement is limited to a specific portion of the tax.

5. Hazardous Waste Remediation Bonds. If payments from nongovernmental users of the site or potentially responsible persons do not secure payment of bonds and are not taken into account as private payments under Treas. Reg. §1.141-4(f)(3), no loan will be indicated.

5.

C. Tax Assessment Bond Exception.

1. General Rule. A tax assessment loan meeting the requirements of Treas. Reg. §1.141-5(d)(3)-(5) described below is not treated as a private loan.

2. Mandatory Tax or Assessment. The tax or assessment must be an enforced contribution that is imposed for the purpose of raising revenue to be used for a specific purpose, and the tax or assessment must be imposed pursuant to a state law of general application that “can be applied equally” to natural persons not acting in a trade or business and persons or entities engaged in a trade or business. Fees for services are not taxes or assessments.

3. Essential Governmental Function.

a. General. The tax or assessment must be imposed for an essential governmental function. Essential governmental functions include utilities or systems that are owned by a governmental person and that are available for use by the general public.

b. Other Facilities. The Regulations provide that for other types of facilities (non-governmentally-owned or non-publicly available facilities), the extent to which the service provided by the facility is customarily performed (and financed by governmental bonds) by governments with general taxing powers is a primary factor in determining whether the facility serves an essential governmental function (parks owned by a governmental person and available for use by the general public serve an essential governmental function). Except as otherwise provided, commercial or industrial facilities and improvements to property owned by a nongovernmental person do not serve an essential governmental function.

4. Equal Basis. Owners of business and nonbusiness property must be “eligible or required” to make deferred payments on an equal basis. A tax or assessment does not satisfy the equal basis requirement if the terms for payment are not the same for all taxed or assessed persons. The “equal basis” requirement will not be met if a person or entity subject to a tax or assessment guarantees debt service on bonds or on taxes or assessments provided that it is reasonable to expect on the date of the guarantee that payments will be made under the guarantee.

5. PLR 201246007. In this ruling, the IRS concluded that assessment bonds issued in connection with the financing and construction of convention and exhibition facilities, which are located in the immediate area of existing convention center, parking facilities, a stadium and entertainment complex will not satisfy the private loan financing test. The assessment bonds are secured by and payable from assessments imposed by and payable from assessments imposed on certain interests in property related to the development that is held by a private company, which will end on the last year of the term of the bonds. The private company has agreed to pay such assessments in return for the extension of a stadium lease and for rights to locate advertising signage in certain parts of the development and the amount of the special taxes will correspond to

and be in lieu of fair market value payments that the private business user would otherwise make in exchange for the lease extension and signage rights. Based on these facts (and while it does not appear that the IRS directly addressed the tax assessment bond exception), the IRS concluded that the arrangement was not a private loan because “the special taxes...will be made in exchange for rights and benefits of equal or greater value.” Presumably, the IRS viewed the payments not as a governmental tax imposed to finance a governmental function, but as compensation to the City for the benefits of the lease extension and signage rights.

VI. ALLOCATION AND ACCOUNTING RULES - SECTION 1.141-6

A. Final Allocation Regulations.

1. Background and Scope. The 1997 private activity bond regulations reserved substantial portions of the rules pertaining to the allocation of and accounting for bond proceeds under Code Section 141. Proposed regulations were subsequently issued addressing, among other things, the allocation of bond proceeds under Code Section 141. On October 27, 2015, the Treasury Department published final regulations under Code Section 141 that, among other things, modified general rules under Treas. Reg. §1.141-6 relating to the allocation of bond proceeds to expenditures, and in particular, the allocation of bond proceeds and other moneys applied to pay costs of the same project among qualified use and private use of that project (the “Final Allocation Regulations”).⁵ The Final Allocation Regulations generally apply to all bonds sold on or after January 25, 2016, however, under certain circumstances an issuer may elect to apply the final regulations adopted on October 27, 2015, in whole, but not in part, to any bonds that are subject to the 1997 private activity bond regulations.

2. General Rule. In general, Treas. Reg. §1.141-6(a)(2) provides that if two or more sources of funding are allocated to capital expenditures for a “project,” those sources are allocated to the governmental use and private use proportionally. In addition, Treas. Reg. §1.141-6(a)(1) provides that the allocations of proceeds and other sources of funds to expenditures under Treas. Reg. §1.148-6(d) apply for purposes of Treas. Reg. §§1.141-1 through 1.141-15. Thus, an issuer may use any reasonable accounting method to allocate proceeds to expenditures, provided that the current outlay of cash rule is met and that the accounting for expenditures takes place within the appropriate time period.

(a) Definition of “Project”. Treas. Reg. §1.141-6(a)(3)(i) states that “project” means one or more facilities or capital projects, including land, buildings, equipment, or other property financed in whole or in part with proceeds of the issue.

(b) Timing Considerations. Treas. Reg. 1.141-6(a)(1) provides that the allocation of proceeds and other funds to expenditures under Treas. Reg. §1.148-6(d) applies for purposes of the allocation of proceeds and other sources of funds to expenditures under Treas. Reg. §1.141-6. Thus, an issuer must account for the allocation of proceeds to expenditures not later than eighteen (18) months after the later of the date the expenditure is paid or the project that is financed by the issue is placed in service, but in no event later than sixty (60) days after the fifth

⁵ These regulations also addressed (i) the treatment of certain partnerships, and (ii) remedial actions, including “anticipatory remedial actions”.

(5th) anniversary of the date the bonds are issued. This timing limitation may lead to anomalous results, particularly when project costs are paid following the expiration of such period.

The preamble to the Final Allocation Regulations specifically states that the definition of “Project” “permits an issuer in its bond documents to identify as a single project all of the properties to be financed by a single bond issue” and that “issuers may identify specific properties or portions of properties regardless of the properties’ locations or placed-in-service dates.” Issuers are given broad, but not unrestricted, latitude to identify the components of their “project.” See Example 3 in Treas. Reg. §1.141-6(f), which provides that the financing of a hospital financed in 1998 and placed in service in 2001 is a separate “project” from an addition to the hospital financed with proceeds of bonds issued in 2017 and with other sources of funds.

An issuer may, under the Final Allocation Regulations, define any contemporaneous assets as being part of the same project so long as bond proceeds are being spent on capital costs of at least one of those assets. A broad definition of a “project” encompassing numerous unrelated facilities may dramatically complicate (1) the tracking of expenditures of proceeds and other sources of funds and (2) the tracking of governmental and private use. Issuers might adopt a practice of preliminarily declaring the scope of the project in a tax certificate or similar document and later adopt a final definition of the project no later than the final allocation of bond proceeds. Where a project is financed with more than one bond issue, it may be appropriate to make the final definition of the “project” no later than when the final allocation of bond proceeds is made with respect to the last bond issue financing the project.

It is unclear what happens if an issuer fails to specifically identify the “project” that is being financed. There may or may not be an implicit default rule that in the absence of the issuer defining the “project,” the project will consist of all capital facilities financed in whole or in part with the proceeds of the bonds, based either upon a written allocation of the issuer or based on tracing the proceeds of the bonds to the capital facilities. In this default situation, qualified equity that is spent on the bond-financed capital facilities would also be treated as financing a portion of the “project.”

3. Eligible Mixed-Use Projects.

(a) General. The Final Allocation Regulations contain provisions which provide that, in the case of an eligible mixed-use project, private business use of the project in each year is first allocated to qualified equity that financed the project, and only private business use of the project in excess of the percentage of qualified equity is allocated to the proceeds of the bonds.⁶ Treas. Reg. §1.141-6(b)(1). For this purpose, an eligible mixed-use project is a project

⁶ The allocation rules are meant to be consistent with the rules pertaining to the measurement of private use under Treas. Reg. § 1.141-3(g) in which private use is generally measured over the measurement period of a project based on the average percentage of private use in each annual period. This year-by-year rule does not permit a global allocation of qualified equity throughout the entire measurement period. For example, if 10% of the costs of a project is allocated to qualified equity, no more than 10% of a project may be allocated to qualified equity in any annual period. Thus, if 100% of a project is used in a private use in the first year, and 0% of the project is used in a private use in later years, all of the qualified equity would be allocated to private use in the first year, and all of the equity would be allocated to qualified uses in all subsequent years.

that is financed with bonds that when issued purported to be governmental bonds and with “qualified equity” and is wholly owned by one or more governmental persons or by a partnership in which at least one governmental person is a partner. Treas. Reg. §1.141-6(b)(2). In the case of an issue of qualified 501(c)(3) bonds, a 501(c)(3) organization, acting in furtherance of its exempt purposes, is treated as a governmental person. Questions arise whether a project that is initially financed with equity, together with taxable debt, such as a line of credit, taxable commercial paper or a long-term taxable bond, which is refinanced with tax-exempt proceeds, can be treated as a qualified mixed use project. The issuer may be able to establish that tax-exempt refinancing debt and the equity were spent pursuant to a common plan of financing if tax-exempt refinancing bonds are issued within 18 months after the project was placed in service. It would be helpful for the Service to clarify that in cases where tax-exempt debt is refinancing either interim or even permanent taxable financing the determination of whether a project is an eligible mixed use project should be tested as if the tax-exempt refinancing bonds were issued at the same time or times as the refinanced taxable debt was issued.

(b) Ownership test. The ownership test presents some concerns. It is unlikely that any “floating” qualified equity would be used with respect to a project where it is expected that some components are to be owned by a governmental entity and others by a nongovernmental entity. In such a case, where the private use would exceed 10%, an issuer would generally specifically allocate equity to the privately-owned facilities and would treat only the portion owned by the governmental unit as the “project”. However, once an eligible mixed-use project has been financed, the issuer may later decide to sell some elements of that project. In such a case, the “mixed-use project”, as defined in the Final Allocation Regulations, may not permit an issuer to permanently assign equity to that portion (reducing the percentage of qualified equity remaining for the portion of the project retained by the issuer). In addition, the issuer should have the opportunity to exercise a remedial action (including either redemption of bonds or alternate use of the disposition proceeds) or (if the numbers work) assign the equity to the portion of the project that is sold. It would be helpful in this instance for the Treasury Department to clarify that the “wholly owned” requirement only applies at the time the bonds are issued.

4. Qualified Equity.

(a) General Considerations. In order to be an eligible mixed-use project, a project must be financed with proceeds of bonds and with qualified equity. Qualified equity is comprised of proceeds of bonds that are not proceeds of tax-advantaged bonds and funds that are not proceeds of a borrowing that are spent on the same eligible mixed use project as proceeds of the bonds. Furthermore, the qualified equity must be spent on the project “pursuant to the same plan of financing (within the meaning of Treas. Reg. §1.150-1(c)(1)(ii)).” Treas. Reg. §1.141-6(b)(4) adds restrictions on whether expenditures of qualified equity finance a project under the same plan of financing as a bond issue. These restrictions relate to the timing of the expenditure and are discussed in more detail below.

(b) Same Plan of Financing Requirement. The reference to Treas. Reg. §1.150-1(c)(1)(ii) is confusing. The provision does not provide guidance on when capital project

This inability to move equity across annual periods would pose difficulties where private business use is front loaded (due, for example, to holdover tenants).

expenditures are or are not pursuant to the same plan of financing. Single issues of tax-exempt bonds are often used for project components that are not proximate or functionally related, and a single plan of finance would not be limited to facilities that are proximate or functionally related, as is the case under certain of the examples in Treas. Reg. §1.150-1(c)(1). However, other than the timing restrictions found in Treas. Reg. §1.141-6(b)(4), there are no additional restrictions imposed by Treas. Reg. §1.150-1(c)(1)(ii). The timing restrictions are sufficient to cause the expenditures of qualified equity to be pursuant to a single plan of financing, but the IRS may need to clarify that the rules of Treas. Reg. §1.141-6(b)(4) are the only rules needed to assure that expenditures of qualified equity for a capital project are part of the same plan of finance as those financed by a bond issue.

(c) Expenditure Period Requirement. The Final Allocation Regulations also provide that qualified equity finances the same plan of financing only if the qualified equity pays for capital expenditures of the project within a specified time period. Treas. Reg. §1.141-6(b)(4) states that the time period begins on the date on which the capital expenditures would be eligible for reimbursement by proceeds of the bonds under Treas. Reg. §1.150-2(d)(2). Treas. Reg. §1.150-2(d)(2) describes the reimbursement period for reimbursement bonds. The reimbursement period generally begins between eighteen (18) months and up to three (3) years before the bonds are issued, depending on when the original expenditure is paid and when the related project is placed in service or abandoned. Treas. Reg. §1.141-6(b)(4) states that the determination of when the qualified equity period begins does not depend on whether the applicable bonds are actually issued as reimbursement bonds.

(d) Ambiguities in Expenditure Period Definition. Ambiguity arises when the text of Treas. Reg. §1.141-6(b)(4) is compared to the discussion in the preamble for the regulation. The preamble suggests that an expenditure that is to be counted as qualified equity must be an expenditure that can be reimbursed from the applicable bonds if the bonds were reimbursement bonds. An expenditure that can be reimbursed from a reimbursement bond must not only meet the timing requirement described in Treas. Reg. §1.150-2(d)(2) but must also be an expenditure for which an official intent was adopted, or which satisfies the *de minimis* exception or preliminary expenditures exception. The preamble does not limit its discussion to the specific timing rule that is referenced in Treas. Reg. §1.141-6(b)(4). Clarification that Treas. Reg. §1.141-6(b)(4) does not require the adoption of an official intent or satisfaction of the *de minimis* or preliminary expenditures exceptions and that the extended reimbursement period for *de minimis* and preliminary expenditures is applicable to the determination of qualified equity would be helpful.

A single project can be partially financed by multiple tax-exempt bond issues. If bond issues partially financing the project have different issue dates, the expenditure and placed in service dates may have different permitted timing intervals for the different bond issues. Neither the Final Allocation Regulations nor the preamble explains how to make a determination of qualified equity where proceeds of more than one issue finance an eligible mixed-use project. Assume, for example, that a project placed in service in 2016 is financed with equity contributed in 2012 and with proceeds of bond issue “A” issued in 2015 and bond issue “B” issued in 2016. Presumably, all equity should count towards qualified equity with respect to the project because the equity is contributed within the reimbursement period of the bonds issued in 2015. However, the Final Allocation Regulations are not entirely clear that, in a case such as this, the equity need

not simultaneously qualify within the reimbursement periods of both bond issues to be treated as qualified equity with respect to the project.

Under the Final Allocation Regulations, equity contributed to a project is not counted as “qualified equity” of a mixed-use project for purposes of the special allocation rule if it is contributed after the date on which the measurement period begins. Under Treas. Reg. § 1.141-3(g), the measurement period of property financed by an issue begins not later than the later of the date the bonds are issued or the date the property is placed in service. Thus, the financing of punch list items could need to be treated as a separate project from the remainder of the same capital improvement. The concept of placed in service is particularly difficult to apply in the context of equity contributions because equity contributions cannot necessarily be allocated to specific components of a “project” under the special allocation rule. Instead, equity may be contributed to the project generally. When a determination is made regarding the start of the measurement period for purposes of the special allocation rule, bond counsel may need to decide whether to rely on the placed in service date of the project as a whole or the placed in service dates of functionally separate components of a mixed-use project.

Equity that constitutes a “reasonable retainage” is, under an exception in Treas. Reg. §1.141-6(b)(4), eligible to be included as qualified equity even if contributed after the measurement period begins. Reasonable retainage is defined with reference to Treas. Reg. §1.148-7(h) as an amount that does not exceed five percent of the available construction proceeds of an issue that is retained for reasonable business purposes. A further exception for expenditures that are paid after the placed in service date and that are not included in the definition of reasonable retainage would be useful. For example, it should be possible for an issuer to pay costs of construction of a project component from qualified equity even after the project component is placed in service if the cost is a normal cost of the project.

1. PLR 201507002. In the ruling, the IRS ruled on the allocation of proceeds between governmental and private activity bonds for water distribution facilities. The ruling illustrates the willingness of the IRS to consider multiple allocation approaches within a system of improvements, including the allocation between two supply sources of water such that private business use of one supply source did not taint the measurement of private business use of the other supply source.

2. PLR 201435013. In the ruling, the Issuer could make allocations under Treas. Reg. §1.141-6(a) and Treas. Reg. §1.148-6 that related to both tax-exempt bonds and build America bonds.

3. PLR 200924013. In the ruling, the City used a specific tracing method to account for investments and expenditures of gross proceeds of its bonds (the “Stadium Bonds”), which Stadium Bonds were issued to finance the acquisition, construction, improvement and equipping of a sports stadium (the “Stadium Project”). The Stadium Bonds were not expected to meet the private business use tests of Code Section 141 upon issuance, but certain private business use opportunities arose that the City sought to take advantage of (including naming rights). The City subsequently (approximately two years after the issuance of the Stadium Bonds) issued

taxable bonds (the “Park Bonds”) to finance an expansion of the City’s park network (the “Park Project”). The City sought to allocate proceeds of the Stadium Bonds to expenditures related to the Park Project, and proceeds of the Park Bonds to expenditures incurred for the Stadium Project as a result of the private business use of the Stadium Project. Because the allocations would occur no later than 18 months after the expenditures for the Park Project were paid, the Stadium Project was placed in service during the 18-month period prior to the date the City allocated the proceeds of the Park Bonds to the Stadium Project expenditures, and because the City had on hand at all times since the date of issuance of the Stadium Bonds an amount of proceeds of the Stadium Bonds equal to the amount of such proceeds to be allocated to the Park Project expenditures, plus investment earnings thereon, the IRS ruled that the City’s allocation method was a permissible allocation method under Treas. Reg. §§1.141-6(a) and 1.148-6.

4. Additional PLRs. Additional private letter ruling addressing allocations include PLR 200248002, PLR 200036033 and PLR 9706008.

VII. SPECIAL RULES FOR OUTPUT FACILITIES - SECTION 1.141-7

On September 19, 2002, the IRS released the long-awaited private activity bond regulations for public power and other output facilities (the “Output Regulations”). The Output Regulations provide rules specifically applicable to “output” facilities, which are electric and gas generation, transmission, distribution, and related facilities, and water collection, storage, and distribution facilities. An output contract will meet the private business use tests if it transfers the benefits and burdens of a bond-financed facility to a non-governmental person.

A. Definitions.

1. Available Output. The available output of a facility financed by an issue is determined by multiplying the number of units produced or to be produced by the facility in one year by the number of years in the measurement period of that facility for a bond issue.

a. In General.

(i) With respect to generating facilities, the number of units produced or to be produced in one year is determined by reference to nameplate capacity or the equivalent (where there is no nameplate capacity or the equivalent, its maximum capacity), which is not reduced for reserved, maintenance or other unutilized capacity,

(ii) With respect to transmission, distribution, cogeneration and other output facilities, available output must be measured in a reasonable manner to reflect capacity, and

(iii) With respect to electric transmission facilities, measurement of available output of all or a portion of such facilities may be determined in a manner consistent with the reporting rules and the requirements for transmission networks promulgated by the Federal Energy Regulatory Commission (FERC). An example is provided in the Output Regulations where the use of aggregate load and load share ratios in a manner consistent with the requirements of FERC was determined to be reasonable. Measurement of the available output of

transmission facilities using thermal capacity or transfer capacity may be reasonable, depending on the facts and circumstances of the specific case.

b. Special Rule for Facilities with Significant Underutilized Capacity.

If an issuer reasonably expects on the issue date of a bond issue that persons that are treated as private business users will purchase more than 30 percent of the actual output of the facility financed with the proceeds of the issue, the Commissioner may determine the number of units produced or to be produced by the facility in one year on a reasonable basis other than by reference to nameplate or other capacity, such as the average expected annual output of the facility. The reasonably expected annual output of the generating facility must be consistent with the capacity reported for prudent reliability purposes.

c. Special Rule for Facilities with a Limited Source of Supply.

If a limited source of supply constrains the output of an output facility, the number of units produced or to be produced by the facility must be determined by taking into account those constraints. For this purpose, a limited source of supply shall include a physical limitation on the flow of water, but not an economic limitation such as the cost of coal or gas. The available output with regard to a hydroelectric unit must be determined by reference to the reasonably expected annual flow of water through the unit.

d. PLR 200915002.

In this private ruling, the IRS considered whether the sale of renewable energy certificates (“RECs”) to non-governmental persons generated by a facility that was owned by the District (a political subdivision of the State) constituted a private business use of bond-financed property for purposes of Code Section 141(b)(6) of the Code. The bond proceeds were to be spent on the District’s electrical distribution system and to “replace or rehabilitate turbines, generators, governors and unit controls for each of the facility’s electric generating units.” On completion of the project, the facility at issue was expected to generate the RECs. The District, in turn, expected to sell the RECs to nongovernmental persons for use in a trade or business under contracts with terms exceeding three years. The IRS addressed two questions in the ruling: first, whether the generation of the RECs constituted “output” for purposes of Treas. Reg. §1.141-7, and second, whether the generation and sale of the RECs by the District from the facility constituted a private business use under Treas. Reg. §1.141-3. The IRS relied on the following analytical factors to conclude that the RECs themselves did not constitute “output” for purposes of Treas. Reg. §1.141-7: (i) the generation of the RECs did not impact the nameplate capacity of the facility or the flow of water through a hydroelectric unit; (ii) the sale of the RECs did not affect the units of electricity that may be sold; and (iii) the sale of the RECs does not entitle the purchaser to any generator capacity. As to the second question, the IRS, in concluding that the use of the facilities, in part, to generate the RECs did not give rise to any private business use, emphasized that (i) the purchasers of the RECs received no right to use the property, and (ii) the RECs did not represent capacity generated by or use of the property.

2. Measurement Period has the same meaning with respect to output facilities

as it does in general for purposes of the private business tests. *See* Treas. Reg. §1.141-3(g)(2).

3. Sale at Wholesale means a sale of output to any person for resale.

4. Take Contract means an output contract under which a purchaser agrees to pay for the output under the contract if the output facility is capable of providing the output.

5. Take or Pay Contract means an output contract under which the purchaser agrees to pay for the output under the contract, *whether or not* the output facility is capable of providing the output.

6. Requirements Contract means an output contract other than a take contract or a take or pay contract, under which a nongovernmental person agrees to purchase all or part of its output requirements.

7. Nonqualified Amount means, with respect to a bond issue, the lesser of (a) the proceeds of such issue which are to be used for any private business use; or (b) the proceeds of such issue with respect to which there are private payments (or property or borrowed money). *See Code Section 141(b)(8).*

B. Output Contracts.

1. In General. The purchase pursuant to a contract by a nongovernmental person of available output of an output facility financed with the proceeds of a bond issue is taken into account under the private business tests, if the purchase has the effect of transferring the benefits of owning the facility and the burdens of paying the debt service on the bonds used (directly or indirectly) to finance the facility (the “benefits and burdens test”).

a. Measurement of Private Business Use. If an output contract results in private business use, the amount of private business use generally is the amount of output purchased under the contract.

b. Measurement of Private Payments. The amount of payments made or to be made by nongovernmental persons under output contracts that satisfy the private business test is measured as a percentage of the debt service of an issue the proceeds of which financed the facility from which the output is purchased. The rules set forth in Treas. Reg. §1.141-4 govern this computation.

2. Take or Pay Contracts. Take or Pay Contracts generally will be determined to have satisfied the benefits and burdens test.

3. Requirements Contracts.

a. In General. A requirements contract may satisfy the benefits and burdens test if (i) it contains contractual terms that obligate the purchaser to make payments that are not contingent on the output requirements of the purchaser or that obligate the purchaser to have output requirements, or (ii) it is a sale at wholesale that may satisfy the benefits and burdens test depending on all the facts and circumstances.

b. Wholesale Requirements Contract.

(i) In General. A requirements contract that is a sale at wholesale may satisfy the benefits and burdens test depending on all the facts and circumstances.

(ii) Significant Factors. Significant factors establishing whether wholesale requirements contracts meet the benefits and burdens test include: (A) the term of the contract is substantial relative to the term of the issue or issues that finance the facility and (B) the amount of output to be purchased under the contract represents a substantial portion of the available output of the facility.

(iii) Safe Harbors Against a Wholesale Requirements Contract Meeting the Benefits and Burdens Test. Two safe harbors against a wholesale requirements contract meeting the benefits and burdens test include: (A) the term of the contract, including renewal options, does not exceed the lesser of 5 years or 30 percent of the term of the issue; and (B) the amount of output to be purchased under the contract (and any other requirements contract with the same purchaser or a related party with respect to the facility) does not exceed 5 percent of the available output of the facility.

c. Requirements Contract other than a Wholesale Requirements Contract. A requirements contract that is not a wholesale requirements contract generally will not meet the benefits and burdens test. However, see paragraph 3(a) above.

d. Factors Not Causing a Requirements Contract to Satisfy the Benefits and Burdens Test. A requirements contract will not meet the benefits and burdens test by reason of a provision in the contract that requires the purchaser to pay reasonable and customary damages (including liquidated damages) in the event of a default, or a provision that permits the purchaser to pay a specified amount to terminate the contract while the purchaser has requirements, in each case if the amount of the payment is reasonably related to the purchaser's obligation to buy requirements that is discharged by the payment.

4. Output Contract Characterized as a Lease. An output contract that is properly characterized as a lease for federal income tax purpose will be analyzed under the general rules to determine whether such contract need be taken into account under the private business tests.

C. Certain Contracts Exempted from the Private Business Tests.

1. Small Purchase Contracts. An output contract for the use of a facility is not taken into account for purposes of the private business test if the average annual payments to be made under the contract do not exceed 1 percent of the average annual debt service on all outstanding tax-exempt bonds issued to finance the facility, determined as of the effective date of the contract.

2. Swapping and Pooling Arrangements. An agreement that provides for swapping or pooling of output by one or more governmental persons and one or more nongovernmental persons does not result in private business use of the governmentally owned output facility if:

(i) the swapped output is reasonably expected to be approximately equal in value (determined over periods of 3 years or less); and

(ii) the purpose of the agreement is to enable each of the parties to satisfy different peak load demands, to accommodate temporary outages, to diversify supply, or to enhance reliability in accordance with prudent reliability standards.

3. Short-term Output Contracts. An output contract with a nongovernmental person is not taken into account under the private business tests if:

(i) the term of the contract, including all renewal options, is not longer than 3 years;

(ii) the contract is either a negotiated, arm's length arrangement that provides for compensation at fair market value, or is based on generally applicable and uniformly applied rates; and

(iii) the output facility is not financed for a principal purpose of providing the facility for use by the nongovernmental person.

4. Conduit Parties Disregarded in Certain Circumstances. A nongovernmental person acting solely as a conduit for the exchange of output among governmentally owned and operated utilities is disregarded in determining whether the private business tests are met with respect to financed facilities owned by a governmental person.

D. Special Rules for Electrical Output Facilities Used to Provide Open Access.

1. Operation of Transmission Facilities by Nongovernmental Persons.

a. In General. The operation of an electric transmission facility by a nongovernmental person may result in private business use of the facility based on all the facts and circumstances. A nongovernmental operator who is compensated for transmission services, in whole or in part, based on a share of net profits from the operation of the facility will be considered a private business user of such facility.

b. Independent Transmission Operators. A contract for the operation of an electric transmission facility by an independent entity, such as a regional transmission organization ("RTO") or an independent system operator ("ISO") (each, an "independent transmission operator") does not constitute private business use if:

(i) the facility is governmentally owned;

(ii) the operation of the facility by the RTO or the ISO is approved by the FERC under one or more provisions of the Federal Power Act or by a state authority under comparable provisions of state law;

(iii) no portion of the compensation of the RTO or the ISO is based on a share of net profits from the operation of the facility; and

(iv) the independent transmission operator does not bear risk of loss of the facility.

c. Use by Nongovernmental Persons under Certain Output Contracts.

(i) Transmission Facilities. The use of an electric transmission facility by a nongovernmental person pursuant to an output contract does not constitute private business use of the facility if:

(A) the facility is governmentally owned;

(B) the facility is operated by an independent transmission operator in a manner approved by FERC or a state authority; and

(C) the facility is not financed for a principal purpose of providing that facility for use by that nongovernmental person.

(ii) Distribution Facilities. The use of an electric distribution facility by a nongovernmental person pursuant to an output contract does not constitute private business use of the facility if:

(A) the facility is owned by a governmental person;

(B) the facility is available for use on a nondiscriminatory, open access basis by buyers and sellers of electricity in accordance with rates that are generally applicable and uniformly applied, which includes situations in which different rates apply to different classes of users, such as volume purchasers, if the differences in rates are customary and reasonable or specifically negotiated rate arrangement is entered into, but only if the user is prohibited by federal law from paying the generally applicable rates and the rates established are as comparable as reasonably possible to the generally applicable rates; and

(C) the facility is not financed for a principal purpose of providing that facility for use by that nongovernmental person (other than a retail end-user).

(iii) Ancillary Services. The use of an electric output facility to provide ancillary services required to be offered as part of an open access Transmission tariff under rules promulgated by FERC does not result in private business use.

E. Exceptions to “Deliberate Action” Rules with Respect to Change In Use Situations.

1. Mandated Wheeling. Entering into a contract for the use of electric transmission or distribution facilities is not treated as a “deliberate action” if (a) the contract is entered into in response to (or in anticipation of) an order of the United States or a relevant state regulatory authority; and (b) the terms of the contract are bona fide and arm’s length, and the consideration paid is consistent with the applicable provisions of the Federal Power Act.

2. Actions Taken to Implement Non-Discriminatory, Open Access. An action similarly is not treated as a “deliberate action” if it is taken to implement the offering of

nondiscriminatory, open access tariffs for the use of electric transmission or distribution facilities, in a manner consistent with rules promulgated by FERC. This paragraph does not apply to the sale, exchange or other disposition of transmission or distribution facilities to a nongovernmental person.

3. Certain Current Refunding Bonds. An action to be taken with respect to electric transmission or distribution facilities refinanced by an issue is not taken into account for purpose of establishing “reasonable expectations and deliberate actions” with respect to private business use if (i) the action is described in the two immediately preceding paragraphs, (ii) the bonds are current refunding bonds that refund bonds originally issued before February 23, 1998, and (iii) the weighted average maturity of the refunding bonds is not greater than the remaining weighted average maturity of the prior bonds.

4. The Commissioner May Permit Additional Transactions. Additional circumstances in which the use of electric output facilities in a restructured electric industry does not constitute private business use may be identified by the Commissioner in published guidance.

5. PLR 200850003. The IRS ruled that the sale of financial instruments available through an allocation and auction process that resulted in allocating priority rights to bond-financed electrical transmission facilities during times of high congestion does not constitute deliberate action causing the bonds to become private activity bonds where implementation of the system is done at the direction and guidance of the FERC and undertaken to enhance the goal of providing open and non-discriminatory access to transmission facilities consistent with Treas. Reg. §1.141-7(g)(4)(ii) of the Regulations. The IRS also ruled that implementation of the new system of allocating priority among users during high congestion times does not constitute a sale, exchange, or other disposition of the bond-financed facilities under Code Section 1001(a) for purposes of Treas. Reg. §1.141-7(g)(4)(ii) where the owners of the bond-financed property retained the legal entitlements and burdens associated with the ownership of the facilities.

F. Allocations of Output Facilities and Systems - Treas. Reg. §1.141-7(h).

1. Facts and Circumstances Analysis. Whether output sold under an output contract is allocated to a particular facility (*e.g.*, a generating unit), to the entire system of the seller of that output (out of any uses of that system output allocated to a particular facility) or to a portion of a facility is based on all the facts and circumstances. Significant factors to be considered include:

(i) the extent to which it is physically possible to deliver output to or from a particular facility or system;

(ii) the terms of a contract relating to the delivery of output (such as delivery limitations and options or obligations to deliver power from additional sources);

(iii) whether a contract is entered into as part of a common plan of financing for a facility; and

(iv) the method of pricing output under the contract, such as the use of market rates rather than rates designed to pay debt service of tax-exempt bonds used to finance a particular facility.

2. Transmission and Distribution Contracts. Whether use under an output contract for transmission or distribution is allocated to a particular facility or to a transmission or distribution network is based on all the facts and circumstances, as described above.

3. Allocation of Payments. Payments for output provided by an output facility financed with two or more sources of funding are allocated pursuant to the general rules regarding payment allocations.

4. PLR 201128010. PLR 201128010 concludes that the allocation of output based on reserved net rated capacity of the facility is equivalent to an allocation based upon output of the facility.

G. \$15 Million Limitation for Output Facilities.

1. In General. An issue is considered to be a private activity bond if the nonqualified amount with respect to output facilities (other than a facility for the furnishing of water) financed by the proceeds of the issue exceeds \$15 million. This limitation applies to issues 5% or more of the proceeds of which are to be used to finance output facilities and is in addition to the general \$15 million limitation on private business use.

2. Application of \$15 Million Output Facility Limitation.

a. In General. The private business use tests will be met if more than \$15 million of the proceeds of the issue to be used with respect to an output facility are to be used for a private business use. Investment proceeds are disregarded for this purpose if they are not allocated disproportionately to the private business use portion of the issue. The private business tests will similarly be met if the payment of the principal of, or the interest on more than \$15 million of the sale proceeds of the portion of the issue is used with respect to an output facility is (under the terms of the issue or any underlying arrangement) directly or indirectly secured by any interest in an output facility used or to be used for a private business use (or payments in respect of such an output facility); or to be derived from payments (whether or not to the issuer) in respect of an output facility used or to be used for a private business use.

b. Reduction in the \$15 Million Limit for Outstanding Issues. In determining whether an issue 5% or more of the proceeds of which are to be used with respect to an output facility consists of private activity bonds under the \$15 million output limitation, the \$15 million limitation is applied by taking into account the aggregate nonqualified amounts of any outstanding bonds of other issues 5% or more of the proceeds of which are or will be used with respect to that output facility or any other output facility that is part of the same “project” (as defined below). A tax-exempt bond of another issue is taken into account if:

(i) that bond is outstanding on the issue date of the later issue;

(ii) that bond will not be redeemed within 90 days of the issue date of the later issue in connection with the refunding of that bond by the later issue; and

(iii) 5% or more of the proceeds of the earlier issue financed an output facility that is a part of the same project as the output facility that is financed by 5% or more of the sale proceeds of the later issue.

c. Modification of Private Business Use Tests. The \$15 million limitation with respect to output facilities as it relates to the “benefits and burdens test” described above, is applied by replacing “10%” or “5%” with \$15 million each place it appears. The amount of bonds of an earlier issue that are required to be taken into account in connection with the foregoing analysis equals the nonqualified amount of the earlier issue multiplied by a fraction, the numerator of which is the adjusted issue price of the earlier issue as of the issue date of the later issue, and the denominator of which is the issue price of the earlier issue (pre-issuance accrued interest is disregarded for purposes of this calculation).

3. Definitions.

a. Project. Facilities that are functionally related and subordinate are treated as part of the same project. Facilities having different purposes or serving different customer bases are not ordinarily part of the same project. *e.g.*, (i) generation, transmission and distribution facilities; (ii) separate facilities to serve wholesale customers and retail customers; and (iii) a peaking unit and a baseload unit (regardless of the location thereof).

b. Separate Ownership. Facilities that are not owned by the same person are not part of the same project. If a project is financed as a collaborative effort among different governmental persons, their interests are aggregated with respect to that project to determine whether the \$15 million output limitation has been met (for example as participants in a joint powers authority). Where there are undivided ownership interests in a single output facility, property that is not owned by different persons is treated as separate projects if the separate interests are financed (i) with bonds of different issuers, and (ii) without a principal purpose of avoiding the Output Regulations. In the case of generating property and related facilities, project means property located at the same site. However, separate generating units are not treated as part of the same project if on the issue date of each of the issues that finances the units, the unit is reasonably expected on the issue date to be placed in service more than 3 years before the other. Common facilities or property must be allocated on a reasonable basis.

c. Transmission and Distribution. In the case of transmission or distribution facilities, project means functionally related contiguous property. Separate transmission or distribution facilities are not part of the same project if one facility is reasonably expected, on the issue date of each issue that finances the facilities, to be placed in service more than 2 years before the other.

d. Subsequent Improvements.

(i) In General. An improvement to generation, transmission or distribution facilities that is not part of the original design of those facilities (the original project) is not part of the same project as the original project if the construction, reconstruction, or

acquisition of that improvement commences more than 3 years after the original project was placed in service and the bonds issued to finance that improvement are issued more than 3 years after the original project was placed in service.

(ii) Transmission and Distribution Facilities. An improvement to transmission or distribution facilities that is not part of the original design of that project is not part of the same project as the original project if the issuer did not reasonably expect the need to make that improvement when it commenced construction of the original project and the construction, reconstruction or acquisition of that improvement is mandated by the federal government or a state regulatory authority to accommodate requests for wheeling.

(iii) Replacement Property. For purposes of these provisions, property that replaces existing property of an output facility is treated as part of the same project as the replaced property unless:

(A) the need to replace the property was not reasonably expected on the issue date or the need to replace the property occurred more than 3 years before the issuer reasonably expected (determined on the issue date of the bonds financing the property) that it would need to replace the property; and

(B) the bonds that finance (and refinance) the output facility have a weighted average maturity that is not greater than 120 percent of the reasonably expected economic life of the facility.

H. Effective Dates - Treas. Reg. §1.141-15(f).

1. In General. The Output Regulations apply to bonds sold on or after November 22, 2002.

2. Permitted Elections into Output Regulations. For bonds subject to the Treasury Regulations that implement the private business tests, the Output Regulations apply to output contracts entered into on or after September 19, 2002. An output contract is treated as entered into on or after that date if it is amended on or after that date, but only if the amendment results in a change to the contract or increases the amount of the requirements covered by the contract by reason of an extension of the contract term or a change in the method of determining such requirements.

3. PLR 201114003. In PLR 20114003, the IRS concluded that an agreement between a state authority and rural electrical power cooperative to defer the effective date of any termination of a wholesale electricity requirements contract is not an amendment to the contract for purposes of Treas. Reg. §1.141-15(f)(2) and will not cause the contract to be treated as an output contract entered after September 19, 2002.

4. Refunding Bonds. Except as provided in the two immediately preceding paragraphs, the Output Regulations do not apply to any bonds sold on or after November 22, 2002, to refund a bond to which the Output Regulations do not apply unless the bonds are subject to the applicable provisions of the Tax Reform Act of 1986 and the weighted average maturity of the refunding bonds is longer than: (a) the weighted average maturity of the refunded bonds; or (b) in

the case of a short-term obligation that the issuer expects to refund with a long-term financing, 120 percent of the weighted average reasonably expected economic life of the facilities financed or a principal purpose for the issuance of the bonds is to make one or more new conduit loans.

5. Elective Application of Output Regulations. The Output Regulations may be, at the election of the issuer, applied in whole, but not in part, to outstanding bonds sold before November 22, 2002 or refunding bonds sold on or after November 22, 2002. The exception to the benefits and burdens test for short term output contracts and for electric output facilities used to provide open access may be applied by an issuer to any bonds.

I. Acquisition of Non-Governmental Output Facilities.

A. General Rule. Under Code Section 141(d), which was added by the Budget Reconciliation Act of 1987, an issue will be treated as a “private activity bond” if more than the lesser of five percent or \$5,000,000 of the proceeds of such issue are used (directly or indirectly) to acquire nongovernmental output property. The term “nongovernmental output property” means any property (or interest therein) which before such acquisition was used (or held for use) by a nongovernmental person in connection with an output facility.

B. Exceptions. For this purpose, (i) a facility for the furnishing of water, and (ii) property used in connection with an output facility 95 percent or more of the output of which is consumed in an area treated as a “qualified service area” or a “qualified annexed area” of the governmental unit acquiring such property is not treated as nongovernmental output property for purposes of Code Section 141(d). In addition, property (other than property which is part of the output function of a nuclear power facility) is not nongovernmental output property if such property is converted to a use not in connection with an output facility.

VIII. UNRELATED OR DISPROPORTIONATE USE TEST - SECTION 1.141-9

A. General Rule. Under Code Section 141(b)(3), an issue meets the private business tests if the amount of private business use and private payments or security attributable to unrelated or disproportionate private business use exceeds 5% of the proceeds of the issue.

B. Application of Test.

1. Order. The test is applied by first determining whether a private business use is related to a governmental use. Next, private business use that is “related” is examined to see if it is disproportionate.

2. Aggregation. All unrelated and disproportionate use is aggregated.

C. Unrelated Use. Whether use is related is determined on a case-by-case basis, emphasizing operational relationship. Generally, related use must be located within or adjacent to the governmentally-used facility. Parallel related and unrelated uses (*i.e.*, use of a facility by a nongovernmental person for the same purpose as use by a governmental person, and use of a facility in the same manner both for private business use that is related use and private business use that is unrelated use) are not treated as unrelated use if the government use or the related use,

as applicable, is not insignificant (*e.g.*, parking garage; pharmacy in governmentally-owned hospital used by hospital and nonhospital patrons).

D. Disproportionate Use.

1. Definition of Disproportionate Use. Private business use is defined to be a disproportionate use in Treas. Reg. §1.141-9(c) only to the extent that the amount of proceeds used for that private business use exceeds the amount of proceeds used for the related government use.

2. Aggregation of Related Uses. If two or more private business uses relate to a single government use, those related uses are aggregated in applying the disproportionate use test.

3. Allocation Rule. If a private business use relates to two or more government uses or a government use and a private business use, the amount of any disproportionate use may be determined by allocating the private business use among the related uses, aggregating government uses that are directly related to each other or allocating the private business use to the government use to which it is primarily related.

E. Maximum Use Taken into Account. The determination of the amount of unrelated use or disproportionate use is based on the maximum amount of reasonably expected government use of a facility during the term of the issue.

IX. REMEDIAL ACTIONS – SECTION 1.141-12

A. General Rule. An action that causes the private activity bond tests or private loan financing test to be met is not treated as a deliberate action if the issuer takes a specified remedial action and all of the following requirements are met.

1. Reasonable Expectations. The issuer reasonably expected on the issue date of the issue would not meet either the private activity bond tests or the private loan financing test for the entire term of the bonds. If the issuer reasonably expects to take deliberate action during the term of the bonds and the special redemption requirements described in II.C.2 above are met, the term of the bonds for this purpose may be determined taking into account such redemption provisions.

2. Maturity Not Unreasonably Long. The term of the issue must not be longer than reasonably necessary for the governmental purposes of the issue.

3. Fair Market Value Consideration. Except with respect to the alternative use of facility remedial action described in B.3. below, the terms of any agreements that result in satisfaction of either the private activity bond tests or the private loan financing test are bona fide, and arm's length and the new user pays fair market value for the use of the financed property.

4. Disposition Proceeds. The issuer must treat any disposition proceeds as gross proceeds for the purposes of Code Section 148.

5. Proceeds Expended. Except with respect to the redemption or defeasance remedial action, the proceeds of the issue affected by the deliberate action must have been expended before the deliberate action.

B. Alternatives for Remedial Action.

1. Redemption or Defeasance of Nonqualified Bonds.

a. If there is a transfer exclusively for cash, the requirements are satisfied if the disposition proceeds are used to redeem a pro rata portion of the nonqualified bonds within 90 days of the deliberate action or establish a defeasance escrow within such period. If the deliberate action does not involve a transfer exclusively for cash, funds other than proceeds of a tax-exempt bond must be used to redeem all the nonqualified bonds within 90 days of the deliberate action or a defeasance escrow must be established within such period.

b. Rev. Proc. 2018-26 provides that the investments in the defeasance escrow must either be yield restricted or rebate payments must be made on any excess yield, with the first computation period beginning on the date on which the escrow is established.

c. If a defeasance escrow is established, the issuer must notify the IRS of the establishment of the defeasance escrow within 90 days of the date the escrow is established.

d. Notwithstanding the foregoing, the establishment of a defeasance escrow will not be considered a remedial action if the period between the issue date and the first call date is more than 10.5 years.

2. Alternative Use of Disposition Proceeds-General Rule. Use of disposition proceeds for an alternative use is a remedial action, if:

a. The deliberate action involves a transfer exclusively for cash.

b. The issuer reasonably expects to spend the disposition proceeds within 2 years of the deliberate action.

c. The disposition proceeds are used in a manner that does not cause the issue to meet either the private activity bond tests or the private loan financing test. In the case of use by a Section 501(c)(3) organization, the bonds must be treated as reissued for the purposes of Code Sections 141, 145, 147, 149 and 150.

d. Any disposition proceeds not so used are used for another remedial action.

3. Alternative Use of Disposition Proceeds—Private Business Use Arising from Certain Leases.

(i) Rev. Proc. 2018-26 allows excess private business use resulting from eligible leases to be remediated through expenditure of moneys on eligible projects, even

though private business use does not result from the sale of a bond-financed asset exclusively for cash.

(ii) Eligible leases only include leases whose entire consideration consist of cash payments (regardless of when paid) not financed with an issue of tax-advantaged bonds.

(iii) The term of an eligible lease must either (X) be at least equal to the lesser of 20 years or 75 percent of the weighted average reasonably expected economic life of the leased property or (Y) run through the end of the applicable measurement period.

(iv) Remedial expenditures must be in an amount equal to the present value of all lease payments, using the yield on the bonds, as of the start of the lease, as the discount rate; such amount is treated as disposition proceeds from purposes of Treas. Reg. §1.141-12(e) and must be spent in the manner prescribed by such Regulations Section.

(v) The effect of the alternate use of disposition proceeds is that the assets on which such disposition proceeds are spent, but only for the term of the lease. Once the lease has terminated, the proceeds of the Bonds once again are allocated to the leased property.

4. Alternative Use of Facility. Alternative use of a facility is treated as a remedial action if all of the following are met:

(i) The facility is used in an alternative manner (*i.e.*, use by a nongovernmental person for a qualifying purpose or use by a Section 501(e)(3) organization).

(ii) The nonqualified bonds are treated as reissued as of the date of deliberate action for purposes of Code Sections 55-59, 141-147, 149 and 150. Under this treatment, the nonqualified bonds are treated as qualified bonds throughout the remaining term.

(iii) The deliberate action does not involve a transfer to a purchaser that finances the acquisition with proceeds of tax-exempt bonds.

(iv) Any disposition proceeds other than those arising from an agreement to provide services are used to pay debt service on the bonds on the next debt service payment date or are deposited in a yield restricted escrow within 90 days of receipt to pay debt service on bonds on the next available debt service payment date. (Note that Code Section 147(d), the existing property limitation, does not apply.)

5. Other Remedial Actions.

a. General. The Commissioner may provide additional remedial actions.

b. Notice 2008-31⁷. This Notice extends to Code Sections 54, 1397E and 1400N the remedies under Rev. Proc. 97-15. Rev. Proc. 97-15 established an IRS closing agreement procedure applicable to failures to meet the requirements for excludability of interest from gross income in Code Sections 141 through 150 that can be remediated under Treas. Reg. §§ 1.141-12, 1.142-2, 1.144-2, 1.145-2 or 1.147-2. Rev. Proc. 97-15 had no effect on the application of Code Sections 150(b) and (c).

6. Definition of Nonqualified Bonds. The nonqualified bonds are a portion of the outstanding bonds in an amount that, if the remaining bonds were issued on the deliberate action date, the remaining bonds would not meet the private business use test. Should the “issuance” of the remaining bonds be treated as a refunding or a new money issue? Unless it is treated as a refunding, application of the definition can, depending on the facts, produce results that either amplify the required remediation or eliminate it entirely.

Consider two examples, both involving a 20-year bullet bond that finances the acquisition of a building on the issue date. In the first, on the issue date, the issuer leases 20% of the building for a 10-year period. Total private business use for the issue is 10%, so no remediation is required. Then, on the first day of the 11th year, the issuer leases 10% of the building for the remaining 10 years of the measurement period. Private business use for the issue is now 15%, and remediation is required. If the bonds are treated as reissued on the deliberate action date, and the reissuance is treated as a new money issue with prior private business use disregarded, then no remediation is required, because the reissued bonds have private business use of 10%, which is within permissible limits, and there are no nonqualified bonds.

In the second example, there is no private business use during the first 10 years. Then, on the first day of the 11th year, the issuer leases 30% of the building for the remaining 10 years of the measurement period. Again, private business use for the issue is now 15%, as with the first example. However, private business use for the new issue is now 30%, rather than 10%, and approximately 20% of the bonds (with adjustments for the gross-down) must be remediated.

7. As part of its outreach and educational services program, the IRS posted to its website an article that summarized the remedial action rules found in Treas. Reg. §1.141-12 of the Regulations. It also presented three examples meant to illustrate the application of the remedial action rules. While the IRS expressed its intent that the article not be considered an authoritative source, the content of the examples gave rise to questions. NABL raised some of these interpretive questions in a letter to the IRS dated July 24, 2012 (the “NABL Letter”). Specifically, the NABL Letter focuses on Example 3 of the article, which describes a \$10M facility financed with multiple sources of funds - \$4M provided from funds on hand and \$6M from the proceeds of tax-exempt bonds. Upon sale of the facility for \$12M, the example states that, if the borrower decides to remediate using the “alternative use of disposition proceeds” option, the borrower must use the entire \$12M for an alternative use within two years. Of this \$12M of disposition proceeds, \$6M are to be treated as gross proceeds of the bonds, suggesting that the IRS is reading this provision to mean that, so long as any portion of a piece of property has been financed with proceeds of an issue, then all of the sale proceeds will be “disposition proceeds.” The NABL Letter also raises an

⁷ TD 9777 obsoleted Revenue Procedure 1997-15 on 7/18/2016 because the scope of violations that can be remedied under Notice 2008-31 is broader than what Rev. Proc. 97-15 provided.

interpretive question regarding Example 2 of the article. Example 2 describes an issuer's use of a \$10M bond issue to finance a school (\$8M) and land (\$2M). After sale of the land for \$3M, the IRS notes that, if the issuer chooses to remediate by redeeming nonqualified bonds, it must redeem \$2M of the outstanding bonds (all \$10M of the bonds are assumed to remain outstanding), leaving \$1M to be treated as gross proceeds for purposes of Code Section 148, raising a question regarding whether, when multiple facilities are financed with a single bond issue, an amount greater than the amount of the nonqualified bonds be considered gross proceeds. The IRS has not provided further clarification of its position, however these examples are no longer posted on the IRS website.

C. Anticipatory Remedial Actions.

1. General Rule. Treas. Reg. §1.141-12 of the Final Allocation Regulations expands the remedial action rules to encourage the retirement of tax-exempt bonds before the occurrence of nonqualified use by permitting an issuer to redeem or defease bonds at any time in advance of a deliberate action that would cause the private business tests to be met.

2. Declaration of Intent. To address the concern of issuers potentially treating ordinary bond amortization payments as "anticipatory remedial actions," the Final Allocation Regulations require an issuer to declare its intent to redeem or defease bonds in advance of a deliberate action in a manner similar to the declaration of intent for reimbursement contained in Treas. Reg. §1.150-2(e). The Final Allocation Regulations require the issuer to "describe the deliberate action that potentially may result in the private business tests being met." This description requirement may significantly impair the usefulness of the anticipatory remedial action unless it is clarified.

With regard to official intent for reimbursement, Treas. Reg. §1.150-2(e) provides that a general description is sufficient to describe the project for which the issuer is seeking reimbursement (e.g. highway capital improvement program, hospital equipment acquisition, etc.). Clarification from the IRS that it is permissible to describe a future deliberate action with similar generalization would be helpful.

The following example illustrates the problem: City A sells to a private developer a parcel of unused bond-financed land, the acquisition of which was part of a larger bond-financed project. Prior to the sale of the land, City A calculated a total of 3% cumulative private business use in the Project from the lease of a portion of its City Hall to a small cafe on the ground floor. City A calculates that the sale of the land will generate an additional 6% private business use on the Bonds. City A adopts an Official Intent Resolution outlining the private business use from the cafe lease and land sale and a general description of private business use that may arise in the future with respect to the Project. City A then redeems the nonqualified bonds associated with the land sale with proceeds from the sale.

In the example above, City A only reached a total of 9% private business use from the sale of the land. A requirement that the declaration of intent describe with detail the deliberate action that may result in the private business tests to be met would result in the City being unable to take an anticipatory remedial action with respect to the sale. At the time of the land sale, the City does not know the nature of future use that may provide the additional 1% use to cause the Bonds to meet the private business use test. However, it is at that time that the City is best positioned to

remediate the private use with proceeds of the sale. If the City were instead to invest the land sale proceeds until an additional amount of private business use causes the private business tests to be met, the result is detrimental to both the City (from the negative arbitrage cost of retaining the land sale proceeds) and the federal government (since the nonqualified Bonds remain outstanding until the 10% threshold is reached). Allowing a general description in the intent resolution better serves the stated policy of the Final Allocation Regulations of encouraging redemption of tax-exempt bonds earlier rather than later.

3. Permitted Anticipatory Remedial Action. The Final Allocation Regulations only permit an issuer to take an anticipatory remedial action in the form of a redemption or defeasance of nonqualified bonds.

The Final Allocation Regulations give the example of a sale of bond-financed property that the buyer may then lease to a nongovernmental person. City B, for example, may sell property to State University C, who may (but has not yet taken action to) lease the property to a nongovernmental person. Thus, City B in this example has not yet generated any private business use from the sale of the land. The Final Allocation Regulations would allow the City to declare its official intent to redeem or defease a portion of the bonds from the future nonqualified use.

4. Nonqualified Bonds. The Final Allocation Regulations provide that the amount of nonqualified bonds is equal to the portion of the outstanding bonds that, if the remaining bonds were issued on the date of the deliberate action, the remaining bonds would not meet the private business tests. This language has the effect of only requiring an issuer to redeem or defease enough bonds to reduce the amount of private business use to 10% (or 5%, if applicable).

D. Remedial Actions for Direct Pay Bonds.

1. General. Rev. Proc. 2018-26 authorizes the use of certain remedial actions for Direct Pay Bonds and other tax-advantaged taxable bonds. Significant uncertainties exist regarding the requirements for effective remedial actions under Rev. Proc. 2018-26. While these remedial provisions allow a variety of potential violations to be remediated, a general discussion of the requirements applicable to tax-advantaged taxable bonds is beyond the scope of this outline, and the summary below solely addresses non-qualified use arising from excess private business use under Code Section 141 of the Code.

2. Reduction of Federal Tax Credit for Direct Pay Bonds. Issuers may remediate excess private business use by voluntarily eliminating the federal tax credit on “nonqualified bonds.” The amount and identity of non-qualified bonds are determined using the general principles of Treas. Reg. §§1.141-12(j) and 1.142-2(e) (i.e. it is the portion of bonds that, if the remaining bonds were issued on the date of the deliberate acquisition, the proceeds of the remaining bonds would be used for a qualified use). Issuers must notify the IRS of the voluntary reduction in credits, identify the date of the deliberate action and submit a revised debt service schedule.

Section 6 of Rev. Proc. 2018-26 also includes a puzzling statement that if the deliberate action results in the creation of “disposition proceeds,” the issuer must treat the disposition proceeds as gross proceeds for purposes of Code Section 148 and as proceeds for

purposes of the Code section applicable to the relevant category of tax advantaged bonds. It is unclear if the Revenue Procedure really intends to require an issuer to both surrender the tax credit with respect to the nonqualified bonds and to be subject to expenditure requirements with respect to disposition proceeds allocable to the nonqualified bonds; if it does, no issuer of Direct Pay Bonds taking a deliberate action involving a disposition exclusively for cash would ever use this remedial action, since it also would have to use the alternate use of disposition proceeds described in Section IX.C.4 below.

3. Redemption or Defeasance of Direct Pay Bonds and Tax Credit Bonds. Section 7 of the Rev. Proc. 2018-26 also permits issuers of certain tax credit bonds and direct pay bonds to remediate excess private business use by redeeming or defeasing nonqualified bonds within 90 days of the deliberate action. Issuers may either yield restrict or pay rebate on the investments in a remedial defeasance escrow. These provisions do not contain an analogue to Treas. Reg. §1.141-12(d)(2), which reduces the redemption/defeasance requirement in certain cases of dispositions exclusively for cash in which the cash received is insufficient to redeem or defease all the nonqualified bonds. This remedial action, like that applicable to termination of the credit in the prior paragraph of this outline, also requires the issuer to treat any disposition proceeds as gross proceeds for purposes of Code Section 148 and as proceeds for purposes of the Code section applicable to the relevant category of tax advantaged bonds. It is unclear if the Revenue Procedure really intends to require an issuer to both defease or redeem the nonqualified bonds and to be subject to expenditure requirements with respect to disposition proceeds allocable to the nonqualified bonds; if it does, no issuer taking a deliberate action involving a disposition exclusively for cash would ever use this remedial action, since it would also have to also use the alternate use of disposition proceeds described in Section IX.C.4 below. A special rule provides that defeasance of nonqualified bonds will not trigger a reissuance of the defeased bonds.

4. Alternate Use of Disposition Proceeds of Direct Pay Bonds and Tax Credit Bonds. Finally, if the deliberate action involves a disposition of financed property exclusively for cash, Section 7.05 of Rev. Proc. 2018-26 permits issuers to make use of an alternate use of disposition proceeds remedial action like that found in Treas. Reg. §1.141-12.

X. OTHER REMEDIAL ACTION RULES

A. Exempt Facility Bonds - Treas. Reg. §1.142-2.

1. General. If, with respect to an exempt facility bond issued under Code Section 142, there is a failure to meet the requirement that 95% of the net proceeds actually be used to provide an exempt facility, such bond will be treated as meeting the requirements of Code Section 142(a) if (i) the issuer reasonably expected on the date of issue that 95% of the net proceeds of the issue would be used to provide an exempt facility and (ii) all nonqualified bonds are redeemed on the earliest call date after the date on which the failure to properly use the proceeds occurs. If bonds are not redeemed within 90 days of the failure to properly use proceeds, a defeasance escrow must be established for those bonds within this period. In the case of the establishment of a defeasance escrow, the issuer must give notice to the IRS within 90 days and, in addition, the bonds must have an initial call date that is not more than 10.5 years from the issue date.

2. Application. The remedial action rules in Treas. Reg. §1.142-2 apply to Code Sections 147(c)(3), (d)(2) and (3), (e) and (f).

B. Small Issue and Qualified Redevelopment Bonds - Treas. Reg. §1.144-2. Treas. Reg. §1.144-2 provides that the remedial action rules of Treas. Reg. §1.142-2 apply to qualified small issue bonds issued under Code Section 144(a) and qualified redevelopment bonds issued under Code Section 144(c).

XI. REGULATIONS FOR APPLYING PRIVATE ACTIVITY BOND RESTRICTIONS TO REFUNDING ISSUES - SECTION 1.141-13

The Treasury Department published final Regulations, addressing the application of the private activity bond restrictions to refunding bonds in the Federal Register in February 2006 (the “Refunding Regulations”).

A. Private Business Use.

1. Rules with respect to Private Activity Bonds.

a. General. The Refunding Regulations as they apply to private activity bonds apply the private activity bond rules to the refunded issue and the refunding issue separately. Treas. Reg. §1.141-13(a). The proceeds of the refunding issue are allocated to the same expenditures and purpose investments as the refunded issue. Treas. Reg. §1.141-13(b)(1). The amount of private business use associated with a bond issue is based upon the respective measurement period of the refunded issue and the refunding issue, calculated separately. Treas. Reg. §1.141-13(b)(2).

b. Example. Airport issues taxable bonds to construct a facility because it knows that the management contract creates private business use. The management contract terminated, and a “good” management contract is executed. Airport issues refunding bonds to refund the taxable bonds. This means that the refunding bonds do not carry over the “bad use” caused by the original management contract.

2. Rules with respect to Governmental Bonds and Qualified Section 501(c)(3) Bonds.

a. In General. The private business use test is applied to a combined measurement period with respect to a refunding of a governmental obligation, so that the measurement period begins on the issue date of the refunded bond or the date the facility financed with the proceeds of such bond is placed in service, whichever is later, and ends on the date the refunding bonds are retired. Treas. Reg. §1.141-13(b)(2)(ii)(A). In a series of refundings, the measurement period begins by reference to the earliest bond issue. Treas. Reg. §1.141-13(b)(2)(iii).

b. Optional Election To Apply Measurement Period Separately. If the refunded issue did not, based upon actual use, satisfy the private business use test by reference to the measurement period beginning on the date the refunded bonds were issued or the date the facility financed with the refunded bonds is placed in service, whichever is later, and ending on

the issue date of the refunding bonds, for purposes of applying the private business use tests, the issuer has the option to treat the measurement periods for refunded bonds and refunding bonds as separate. Treas. Reg. §1.141-13(b)(2)(ii)(B).

c. Qualified 501(c)(3) Bonds. Use of property refinanced with the proceeds of a refunding issue by a Section 501(c)(3) organization in activities that are not unrelated trade or business activities under Code Section 513(a) is treated as governmental use. Treas. Reg. §1.141-13(b)(v). Solely, for purposes of the Refunding Regulations, the use of proceeds of a Qualified Section 501(c)(3) Bond for the purpose of paying costs of issuance (ordinarily a private business use) is treated as a governmental use of proceeds.

3. Private Payments and Security Tests.

a. Separate Issue Treatment. The private payment or security interest test is measured separately for the refunded and the refunding issue, if the private business use is measured separately. Treas. Reg. §1.141-13(c)(1).

b. Combined Issue Treatment.

(i) In General. The private payment or security interest test is measured on a combined basis if the private business use test is measured on a combined basis.

(ii) Computing the Present Value. The present value of the private security and private payments is compared to the present value of the debt service on the combined issue (other than debt service paid with the proceeds of the refunding bond). The present value is computed using the earliest issue date in a series of refundings. Except as set forth in 4. below, the present values are determined by using the yield on the combined issue as the discount rate, using payments on the refunding issue and all earlier issues (other than payments made with the proceeds of refunding bonds) and using as the target price, the issue price of the earliest bond issue in the measurement period. In the case of partial refundings, only the payments with respect to the refunded debt is taken into account. Treas. Reg. §1.141-13(c)(2).

4. Arrangements Not Entered into in Contemplation of a Refunding. The issuer may use the yield on the refunded issue in applying the private payment or security interest test, in determining the present value of private payment and private security interest under arrangements that were not entered into in contemplation of the refunding issue. An arrangement entered into more than 1 year prior to the issue date of the refunding issue is treated as not having been entered into in contemplation of a refunding issue. Treas. Reg. §1.141-13(c)(3).

B. Multipurpose Allocation Rules. The multipurpose allocation rules of Treas. Reg. §1.148-9(h) apply for purposes of applying the Refunding Regulations, unless such allocation is unreasonable in that it achieves more a favorable result under the private activity bond tests than could be achieved with actual separate issues. Treas. Reg. §1.141-13(d). Allocations made under Treas. Reg. §1.141-13(d) must be consistent with allocations made under Treas. Reg. §1.148-9(h). Treas. Reg. §1.141-13 (d) by its terms, does not apply to private loan financing test determinations under Code Section 141(c)(1) or determinations regarding the acquisition of nongovernmental output property to be treated as private activity bonds pursuant to Code Section 141(d)(1).

C. Application of Reasonable Expectations Test in Certain Refunding Bond Situations. An action that would otherwise cause a refunding bond to satisfy the private business tests or the private loan financing test is not taken into account under the reasonable expectations test of Treas. Reg. §1.141-2(d) (including the mandatory redemption provisions hereof) if (i) the action is not a deliberate action within the meaning of Treas. Reg. §1.141-2(d)(3), *i.e.*, an action taken by the issuer that is within its control, and (ii) the weighted average maturity of the refunding bonds is not greater than the remaining weighted average maturity of the refunded bonds.

D. Miscellaneous. The Refunding Regulations provide that the term “private activity bond” in the context of these rules does not include taxable bonds.

E. Effective Dates. The Refunding Regulations apply to bonds sold on or after the date of publication of final regulations in the Federal Register; the Refunding Regulations will not apply to refunding bonds issued to refund bonds issued prior to the effective date of the private activity bond regulations of May 16, 1997, unless the weighted average maturity of the refunding bonds exceeds the remaining weighted average maturity of the refunded bonds.

XII. ANTI-ABUSE RULES - SECTION 1.141-14

If an issuer enters into a transaction or series of transactions with respect to one or more issues with a principal purpose of transferring to nongovernmental persons significant benefits of tax-exempt financing inconsistent with the restrictions of Code Section 141, the Commissioner may take any action to reflect the substance of the transaction, including: (i) treating separate issues as a single issue for purposes of the private activity bond tests; (ii) reallocating proceeds to expenditures, property, use or bonds; (iii) reallocating payments to use or proceeds; (iv) measuring private business use on a basis that reasonably reflects the economic benefit; or (v) measuring private payments or security on a basis that reasonably reflects the economic substance. *See* PLR 201148005 for analysis by the IRS of the anti-abuse rules in responding to a request for a ruling on whether the refinancing of taxable debt with the proceeds of a 501(c)(3) bond issue would cause the issue to fail to qualify as a 501(c)(3) issue.

XIII. EFFECTIVE DATES - SECTION 1.141-15; SECTION 1.141-15T

A. General Effective Date. Treas. Reg. §§1.141-1 through 1.141-6(a), Treas. Reg. §§1.141-9 through 1.141-14, Treas. Reg. §§1.145-1 through 1.145-2, Treas. Reg. §1.150-1(a)(3) and the definition of bond documents contained in Treas. Reg. §1.150-1(b) (collectively, the “May 1997 Regulations”) apply to bonds issued on or after May 16, 1997, that are subject to the Tax Reform Act of 1986.

B. Refunding Bonds. The May 1997 Regulations do not apply to refunding bonds issued on or after May 16, 1997, unless (i) the weighted average maturity of the refunding bonds is greater than (A) the remaining weighted average maturity of the refunded bonds, or (B), in the case of certain short-term obligations, 120% of the weighted average reasonably expected economic life of the facilities financed, or (ii) a principal purpose for the issuance of the refunding bonds is to make one or more new conduit loans.

C. Permissive Application of Regulations. The May 1997 Regulations may be applied in whole but not in part to actions taken before February 23, 1998, with respect to (1) bonds

outstanding on May 16, 1997, and subject to Code Section 141, or (2) refunding bonds issued on or after May 16, 1997.

D. Permissive Retroactive Application of Sections. The following may be applied to any bonds issued before May 16, 1997: Treas. Reg. §1.141-3(b)(4) (management contracts), Treas. Reg. §1.141-3(b)(6) (research agreements) and Treas. Reg. §1.141-12 (remedial actions).

E. Output Regulations. Treas. Reg. §1.141-15(f) provides special effective dates applicable to regulations pertaining to the treatment of output facilities under the private activity bond tests.