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Content

Editor's Notes

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In this Edition

Tony Martini's column in this edition includes a look back and a look forward on federal tax matters, including finalization of Section 6417 Regulations, the opening of the pre-filing registration tool, and Revenue Procedure 2024-8, as well as an update on his personal ongoing challenges with the IRS "secure messaging" platform.

Drew Kintzinger reports on developments in federal securities enforcement actions of interest to the municipal market and the new final rule on "conflicted transactions" involving asset-backed securities.

Basel III Endgame

I am a bond lawyer, not a bank regulatory lawyer. Understanding the so-called "Basel III Endgame"[1] is not in my wheelhouse but bond lawyers and their clients may feel the ripple effect if the current bank regulatory proposal is implemented as proposed. At least, I *think* so. The question is whether this effect will be a ripple like a small stone creates being skimmed across still waters (which is nice to watch and not likely to get your shoes wet) or a rogue wave bringing potential financial turmoil. The proposed regulations implementing the Basel III Endgame,[2] which are jointly proposed by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation, are intended to "strengthen the calculation of risk-based capital requirements to better reflect the risks of" large banking institutions. Very, very simply put, the regulations would, among other things, standardize how risk is assessed (weighted, actually) in conjunction with determining capital requirements for banking institutions with more than $100 billion in assets. One commentator likened the Basel III Endgame proposed regulations to "the perfect storm," paraphrasing remarks by one U.S. Senator regarding the potential "compounding effect of tougher capital standards, high interest rates, and disruptions in the

[1] The Basel III Endgame marks what should be the final implementation of measures developed by the Basel Committee on Banking Supervision in response to the financial crisis of 2007-2009. See https://www.bis.org/bcbs/basel3.htm; and https://www.reuters.com/business/finance/what-is-basel-iii-endgame-why-are-banks-worked-up-about-it-2023-07-24/.
[2] https://www.federalreserve.gov/newsevents/pressreleases/bcreg20230727a.htm

commercial real estate market."[3] The Federal Reserve estimated it would increase capital requirements by 16%.[4]

The calculations in the proposed regulations are very complicated with multiple variables, making it very difficult, if not impossible, to interpolate with any certainty how the cost of this 16% increase can or would be allocated to loans generally and municipal debt, in particular. As several commentators have opined, any increase in cost to banks will be passed along to consumers, including borrowers, in some manner, whether through a decrease in funds available to lend, more selective lending decisions, increased borrowing costs, or (more likely) a combination of these approaches. That opinion appears logical (and obvious). The question I have been struggling with is whether the Basel III Endgame will have any impact on existing municipal loans. Will banks subject to the new requirements (if adopted) who currently hold municipal loans as direct lenders (or provided credit enhancement through a letter of credit or other product) attempt to pass along this increased cost to existing borrowers under the "increased costs" or other yield protection provisions in loan agreements and/or letter of credit and reimbursement agreements? Yield protection provisions in loan and credit agreements have been around for a long, long time with varying specificity regarding reserve and capital requirements but in the last several years typically include new regulatory actions under both the Dodd-Frank Wall Street Reform and Consumer Protection Act and the Basel Committee on Banking Supervision (and specifically Basel III). When discussing these provisions with bank counsel and trying (with only marginal success) to limit these provisions I have been assured by bank counsel that the provisions have not actually been used to recoup costs related to regulatory changes. No assurance, of course, there would not be a first time.

To try to satisfy my curiosity, I read the proposed regulations. Actually, I read them a few times. Then I had to find secondary resources to explain what I had read in the regulations and then still more resources to explain what I had read in the secondary resources. Right or wrong, here is how I currently understand it.

1. Generally, and very simply, the capital requirement for a bank is expressed as a minimum ratio of its capital to its risk. There are multiple types of capital and multiple types of risk. Total risk is calculated based upon the bank's total "risk weighted assets" or RWAs. Different asset classes are assigned different risk weights. The lower the weight, the lesser amount of that asset that is included in the calculation of total RWA.[5] Think of this as a mathematical equation with the bank's capital in the numerator and total RWA in the denominator. Reducing the denominator increases the resulting ratio

[3] https://fortune.com/2023/12/06/us-economy-could-face-perfect-storm-basel-iii-endgame-goes-into-effect-finance-banks-kevin-fromer/
[4] From the Federal Reserve Fact Sheet available via the link in Note 1.
[5] https://corporatefinanceinstitute.com/resources/career-map/sell-side/risk-management/risk-weighted-assets/

while increasing RWA decreases the resulting ratio. That is overly simplified, but it highlights the points needed to have a base for understanding at least some aspects of the Basel III Endgame.

2. Current regulations allow for a bank to use internal models to assess the risk weight of assets but also provide for a standard approach. Under the standard approach in the current regulations U.S. Government guaranteed securities are in a "zero" risk category, for example, so U.S. Government obligations do not figure into the denominator for risk calculation. Public Sector Entities (PSEs), on the other hand, garner a 20% risk weight for general obligation debt or a 50% risk weight for revenue-based debt. Other types of assets have other weights.
3. The proposed regulations would remove the option of using an internal model for most calculations and provide for standardized measurement of "credit risk" which, with respect to U.S. Government debt and PSE debt, as best I can tell, is the same as in current regulations, at least for U.S.-based PSEs. There are numerous other aspects of credit risk addressed in the proposed regulations, but I did not notice anything else applicable to municipal debt generally.
4. The proposed regulations include requirements for the expanded assessment of other risks associated with both lending and trading activities of banks, with the latter seemingly the primary driver of the estimated increase in capital reserves. This is confirmed in the economic analysis portion of the proposed regulations wherein the effect on lending activities is described as "modestly increasing capital requirements" while the effect on capital requirements for trading activity is described as "estimated to increase substantially."
5. In the end, I did not find anything in the proposed regulations that changes the actual reserve requirement, which is confirmed several times in the proposal.

So, turning back to increased costs and yield protection provisions mentioned above, whether there is a toehold for a lender to justify passing any financial burden of the proposed regulatory change to current municipal borrowers remains to be seen. The answer, of course, depends on the applicable contractual provision, as well as market acceptance, business relationships, market competition, and other matters (i.e. even if a bank *could* pass these costs along, *would* it?). To the extent the weighted asset value of a municipal loan remains unchanged in the calculation and the contractual provision is limited to increased costs directly related to the particular municipal loan, it would seem to be somewhat high hurdle for a lender to justify invoking the increased cost provision. A deeper dive into the "before and after" treatment for other non-municipal loans would be needed to draw any preliminary conclusions regarding those transactions.

There are other aspects of the proposed regulations that may affect the municipal market in other ways. One commentator suggested the proposed regulations could increase the cost of capital needed to utilize municipal paper as posted collateral from 8% to 20%[6]. How this and other ripple effects may ultimately affect pricing of municipal bonds in the public market and bonds or loans in the private or direct placement market remains to be discovered.

For more reading on this subject see some of the sources listed in the footnote.[7]

2023 Closing Thoughts

As 2023 comes to a close, I tried to make of list of the more important (or not as important, but interesting) developments in the municipal market. It was a short list.

1. **Kirschner, v. JPMorgan Chase Bank 2nd circuit decision.** Syndicated loans are still not considered securities. And Generalissimo Francisco Franco is still dead![8]
2. **Banker Layoffs and Moves.** The Citi and UBS Financial Services announcements of their exit from the negotiated municipal market follow (and/or precede) a rash of downsizings, retirements, and other movements in the ranks of investment bankers.
3. **1994 Interpretive Release.** The 1994 SEC Interpretative Release has still not been updated.
4. **ESG Bonds are still a thing.** ESG Bonds are still being issued, but not in Florida.
5. **Arbitrage is a "thing" again.** No explanation needed.
6. **Politics Front and Center (again) in Muniland.** Back in the 80's and 90's there was much consternation about campaign contributions and selection of professionals. Then rules were put in place to ostensibly take the politics out of the business. But a new kind of political influence has emerged in the last couple of years, that of "woke" and "anti-woke" politics. Investments and/or investments banks have been "A" listed or de-listed, depending on the topic and the state.

Best wishes to all for a prosperous (and voluminous) 2024.

And now, enjoy the rest of this edition of *The Bond Lawyer*.

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[6] https://www.bondbuyer.com/opinion/there-are-risks-in-basel-iii-endgames-treatment-of-municipal-bonds

[7] https://www.brookings.edu/articles/what-is-bank-capital-what-is-the-basel-iii-endgame/; https://www.sifma.org/resources/news/how-the-basel-iii-endgame-reforms-will-transform-us-capital-requirements/

[8] Thank you, Chevy Chase. See Saturday Night Live Season 1.

Federal Securities Law

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The final quarter of 2023, since the NABL October Workshop, brought continuing news from the SEC's Enforcement Division, from Commission rulemaking, and from case law developments.

Enforcement News

In November 2023, the SEC announced its Enforcement Results for the federal Fiscal Year 2023. The Commission noted that filed enforcement actions increased by 3% over the prior fiscal year, and original or "stand alone" enforcement actions increased 8% over the prior fiscal year. The Public Finance Abuse Unit commenced one civil action involving two parties and announced five stand-alone administrative proceedings involving six parties. These categories amounted to only 1% of total actions brought by the Enforcement Division. However, the SEC's Enforcement Report encapsulates the prior year and what we observed over the Fall months of 2023. In addition to highlighting enforcement actions brought against gatekeepers generally, the Enforcement Division highlighted Public Finance Abuse Unit results:

> ***"The SEC brought several important enforcement actions in the public finance sector in fiscal year 2023, including:***
>
> - ***Charges against public company Exelon Corporation, its subsidiary, and the subsidiary's former CEO for fraud in connection with a multi-year political corruption scheme;***
> - ***Charges against three broker-dealers for failing to obtain required disclosures for investors when selling new issue municipal bonds; and***
> - ***A case charging an auditor of a municipal issuer for fraud in connection with its audit of financial statements for a Louisiana-based school board."***

The reference to the three broker-dealers actions pertains to the continuing Rule 15c2-12 limited offering exemption cases, now amounting to seven actions since 2022, including six administrative settlements and one litigation proceeding against underwriting firms regarding non-compliance with the limited offering exemption.

The mentioned case against the auditor is described in a lengthy complaint filed by the Commission detailing settled fraud charges against a New Orleans based auditor and its principal, *Securities and Exchange Commission v. Luther C. Speight, III and Luther Speight & Company LLC,* No. 1:23-cv-4384-AT (N.D. GA. Filed September 27, 2023). In this case, the auditor was hired by a school board to perform an audit of the school board's fiscal year 2019 financial statements. According to the SEC, the auditor issued a false report that the audit was conducted in accordance with Generally Accepted Audit Standards ("GAAS") because the auditor did not comply with GAAS in several material respects and the school board's financial statements also contained errors that had to be corrected. The SEC maintained that the auditor knew, or should have known, that the school board would use the auditor's report to sell bonds to investors and that, indeed, the school board unknowingly used the auditor's report, with the false statement of GAAS compliance, to sell $120 million of bonds to an investor in 2020. In sum, a lengthy, very detailed complaint of auditor missteps.

Notable in this auditor case is the theory of liability and the conduct-based injunctions against the auditor principal and the auditing firm. In prior enforcement proceedings against auditors in municipal securities engagements, *see, e.g. College of New Rochelle, KPMG LLP (February 23, 2021),* the Commission has imposed sanctions on auditor individuals under Commission rules of professional conduct, including Section 4C of the Exchange Act and Rule 102(e) of the Commission's Rules of Practice. In the *Speight* matter, the SEC uses Section 17(a)(2) [misstatement liability] and (3) [transaction fraud] of the Securities Act to impose liability and sanctions:

> ***"While employed as the auditor of the financial statements of the School Board between June 2019 and February 2020, Defendants Speight and LSC, in the offer and sale of securities described herein, by use of means and instruments of transportation and communication in interstate commerce and by use of the mails, directly and indirectly:***
>
> ***a. obtained money and property by means of untrue statements of material fact and omissions to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and***

b. engaged in transactions, practices and courses of business which would and did operate as a fraud and deceit upon the purchasers of such securities, all as more particularly described above."

In addition to the Section 17(a) theory of liability, Speight agreed, on a no-admit, no-deny basis, to a conduct-based injunction which would prevent him from serving as engagement manager, engagement partner, or engagement quality reviewer in connection with any audit of financial statements or audit report which Speight should reasonably expect to be submitted to EMMA. The auditing entity similarly agreed to a conduct-based injunction which would prevent it from participating in the audit of financial statements which the entity should reasonably expect to be submitted to EMMA. The settlement terms remain subject to court approval. In short, this enforcement case is another, recent example of the more aggressive use of Section 17(a) as grounds for liability in municipal securities matters and a continued enforcement emphasis on individual accountability through use of conduct-based sanctions.

Asset Backed Securities Rule

In January 2023, as a follow on to Dodd Frank, the Commission proposed a rule that would prohibit participants in asset backed securitizations ("ABS") from engaging in "conflicted transactions." The proposed rule was intended to prevent conflicts of interest that may arise from securitization participants taking positions economically adverse to the interests of ABS investors.

In March 2023, NABL joined eight other municipal market groups, including GFOA and SIFMA, in recommending to the Commission that municipal securities should be excluded from the definition of ABS and issuers should be excluded from the proposed rule's definitions of "securitization participant" and "ABS sponsor." The comment letter noted that impacted municipal transactions could include conduit financings for affordable housing and student loans, other pooled financings offered to entities from an issuer (e.g., bond banks) and offerings that securitize municipal revenues or other sources of income. The comment letter noted these transactions are usually handled by specialized agencies within states that exist for this sole or limited purpose. One example could be joint powers authorities or agencies.

On November 27, 2023, the Commission approved a new final Rule 192 preventing securitization participants from entering into "conflicted transactions." Throughout a lengthy adopting release ("Release") for the final rule, one can delineate that Staff (one can assume the staff of the Office of Municipal Securities) was mindful of the concerns expressed by municipal market participants. Citing, in part, the risks in conduit structures and the elevated risks of conduit defaults, the release concludes that "investors in municipal securitizations should be entitled to the same legal protections as investors in other types of ABS that meet the definition of 'asset backed security' in Rule 192(c). Accordingly, if a municipal security meets the definition of Exchange Act ABS, then the municipal issuer that organizes and initiates such an offering is a sponsor for purposes of Rule 192." At the same time, in the Economic Analysis portion of the Release, it is noted:

> ***"The Commission received comments that municipal ABS issuers are unlikely to engage in conflicted transactions yet may face "unnecessary" or "unjustifiable" costs, burdens, or liability and should be excluded from Rule 192. Since the final rule does not exclude municipal issuers from the definition of sponsor, these issuers may seek legal guidance and incur costs to ascertain that the activities they seek to engage in are not violating the final rule. We expect that the overall impact of the final rule on the municipalities will be modest as it will be limited to those municipalities that issue ABS covered by the rule, an approximated 352 in the baseline year out of over 50,000 issuers of municipal securities in the United States as of 2018. Thus, even among municipalities issuing securities, under 1% of municipalities are expected to be covered by the final rule."***

The foregoing is a summary only of this recently adopted new final rule, and the nuances for affected municipal issuers require further detailed analysis by issuer's counsels. However, it appears the concerns of municipal market participants did not go unheeded by Staff.

Case Note Watch

It has long been a "working assumption" when defending an enforcement proceeding on a municipal securities matter that SEC Enforcement Staff will not view the absence of investor loss as relevant when evaluating violations of the securities laws. In *Securities and Exchange Commission v. Govil,* No. 22-1658, 2023 WL 7137291 (2d Cir. October 31, 2023), the Second Circuit held that the ability to seek disgorgement under 15 U.S.C. Section 78(d)(5) and (7) (disgorgement sanctions in SEC investigations) is limited to situations in which the SEC can demonstrate that investors have suffered pecuniary loss. While noted by municipal securities litigators, it is also observed that the Fifth Circuit has ruled differently. However, as this recent decision is valuated, it renews a frequent target/defendant argument that the absence of investor loss should be relevant when determining financial penalty exposure.

The Tax Microphone

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Looking Back; Looking Forward

As we're nearing the end of 2023, I thought I'd start this column by taking a look back a year or so, to the end of 2022. A year ago, we were looking at borrowing rates coming up substantially from an extended period of historical lows. It wasn't clear at the end of 2022 whether rates would stay high and climb even higher on a sustained basis, through 2023 into 2024 and beyond, or whether we'd see them start to moderate and even ease. Today, a year later, rates are beginning to look like they may be moderating. On December 13, the day on which I am beginning to write this column, the Federal Reserve Bank announced that it would hold steady on short-term interest rates thanks to the progress that has been made this year curbing inflation. Reports on the same day had Fed watchers predicting short-term rates would actually be lowered in the coming year. The Dow Jones Industrial Average reacted to this reporting by hitting a new all-time high. Reports in the financial press suggest, optimistically, that our economy may be threading the needle between tamping down borrowing costs and inflation, while avoiding recession. And recently, *The Bond Buyer* reported there is a fairly broad consensus among municipal market analysts that the coming year will see a considerable uptick in new municipal debt issuances, compared to 2022 and 2023, due both to the anticipated easing of borrowing costs and to the build-up of demand over the last couple of years among municipal issuers, who have been sitting out the market, to secure funding for new capital investments. Let's hope all of this isn't a case of "irrational exuberance," to borrow a memorable line from former Fed Chair Alan Greenspan; let's hope we see a thriving economy in 2024, in which reasonable borrowing costs open paths for the kinds of investment in public and private infrastructure that power sustainable jobs growth and prosperity. That doesn't seem to me to be too much to ask for at the end of 2023; that would be the kind of change we bond lawyers would find most welcome, I should think.

There is one thing that looks like it still isn't changing, though—as at the end of 2022, new, helpful and evolutionary guidance from municipal market regulators remains in notably short supply. For example, as at the end of 2022, guidance is urgently needed on the bond and tax credit provisions of the Inflation Reduction Act that affect state and local governmental entities. NABL's leadership continues to ask Treasury and the IRS to modify and finalize proposed regulations addressing whether and if tax-exempt and other tax-benefited debt instruments are treated as reissued for federal tax law purposes, and for supplemental guidance to simplify and expand the reach of the bond remedial action rules. Municipal market participants were told more than a year ago that Treasury and the IRS working on these issues. I suspect we'll be turning the page on 2023 before we see the fruits of these labors.

Treasury Releases 2023-2024 Priority Guidance Plan

On September 29, 2023, the Treasury Department and the IRS announced the release of their 2023-2024 Priority Guidance Plan, including, as usual, a litany of guidance projects relating to the tax-exempt bond market that the regulators tell us they are allocating resources to on a "priority" basis. The listing is as follows:

1. Guidance under §142, as amended by the Infrastructure Investment and Jobs Act.

2. Revenue procedure providing guidance on the use of average area purchase prices and median income figures for purposes of §143.

3. Guidance under §§144(b) and 150 on qualified student loan bonds.

4. Regulations under §§148 and 150 on refunding bonds.

5. Revenue procedure on the recovery of rebate under §148.

6. Regulations under §149 to update requirements for certain tax-exempt bond information returns.

7. Final regulations on bond reissuance under §150. Proposed regulations were published on December 31, 2018.

It struck me that a number of these topics looked familiar, so I took a look at the regulators' 2022-2023 Priority Guidance Plan, which was released on November 4, 2022. And it turns out that the first, third, fourth, fifth and seventh of the items on the list above were on the 2022-2023 Priority Guidance List, verbatim. In fact, these five items comprised the <u>entirety</u> of the priority work plan for Treasury and the IRS a year ago. So, absolutely nothing has been forthcoming from Treasury or the IRS on any of these topics for a year or more, at least. I may be naïve, but when someone tells me that something is a "priority" I think it may imply that there's some "urgency" about the matter. Judging from the lack of results year-over-year on this part of the Priority Guidance List, I fear the regulators may have a different notion in mind when it comes to "priorities."

Of the two new additions on the 2023-2024 list (the second and sixth on the list above), one appears to align with NABL's June 7, 2023 submission requesting certain priority guidance; namely, the request for regulations under Code Section 149 to update the requirements for information returns like IRS Form 8038 and 8038-G. Two other requests in NABL's June 7 submission are not reflected in the 2023-2024 Priority Guidance List—a request for revisions to Revenue Procedure 2018-26 to clarify and expand the application of the remedial action rules in Treasury Regulations Section 1.141-12 and a request for clarifying guidance regarding the application of the allocation and accounting rules in Treasury Regulations Section 1.141-6. Perhaps we should be relieved about this; one could be forgiven for thinking the regulators have too much on their plates, at least when it comes to providing updated guidance to the tax-exempt bond markets.

Finalization of Section 6417 Regulations; Opening of Pre-Filing Registration Tool

While we're on the topic of the 2023-2024 Priority Guidance Plan, I'll note that Treasury and the IRS also are "prioritizing" the release of final regulations "regarding the elective payment of applicable credits under §6417." This item appears in the plan under the heading of "Energy Security." And, to be fair, this project hasn't been pending nearly as long as some of the tax-exempt bond guidance projects discussed above, because Code Section 6417 was only enacted toward the end of 2022, as part of the Inflation Reduction Act. Still, as I have noted previously in the *Tax Microphone* column, perhaps more than once, there is some urgency for guidance in this area, as eligible entities, including many issuers and borrowers of tax-exempt bonds, are investing today in the renewable and clean energy projects that are supposed make Section 6417 subsidies accessible. Until regulations under Section 6417 are finalized, however, the means by which these valuable cash subsidies are to be captured by eligible entities remain less than clear. Here's hoping there are final Section 6417 regulations to report on in the next number of *The Bond Lawyer*.

Apart from the finalization of the full Section 6417 regulations package, I can report on a related, late-breaking development, which is that on December 22, 2023 the IRS announced the availability for the first time of a "registration tool" enabling state and local governments and 501(c)(3) organizations to register specified information with respect to clean and renewable energy projects that are expected to give rise to Section 6417 direct-pay subsidies. The registration must be completed on a "pre-filing" basis, which is to say prior to the time for applying for payment of a Section 6417 subsidy; apparently, a registrant can only submit one "registration package" for a taxable year, which can (and should) cover as many projects and subsidy elections that the registrant is eligible to make for that year. The registration tool portal can be accessed at https://www.irs.gov/credits-deductions/register-for-elective-payment-or-transfer-of-credits. In addition, the IRS has released Publication 5884, which provides a user guide and instructions regarding this registration tool. Publication 5884 can be found at https://www.irs.gov/pub/irs-pdf/p5884.pdf. I personally have not had any hands-on experience with this registration portal since it went on line; I expect that there will be more to say about the registration process in the next issue of *The Bond Lawyer*.

Revenue Procedure 2024-8

On December 8, 2023, the IRS released Revenue Procedure 2024-8, which provides issuers of tax-exempt qualified mortgage bonds under Code Section 143(a) (as well as issuers of mortgage credit certificates under Code Section 25(c)) with an updated listing of "qualified census tracts" within the meaning of Code Section 143(j)(2) for all fifty states, as well as the District of Columbia and Puerto Rico. These updates are based on the results of the 2020 Census, as reported by the United States Census Bureau, and Revenue Procedure 2024-8 by its terms supersedes Revenue Procedure 2014-14, which would have been based on results of the 2010 Census. The listings in Revenue Procedure 2024-8 are effective as of January 8, 2024.

The identification of currently qualified census tracts is critical to issuers of tax-exempt mortgage revenue bonds under Code Section 143(a) (also known as "single family bonds") because, under Code Section 143(h), these bonds will only be treated as tax-exempt (among many other requirements under Code Section 143 applicable to single family bonds) if at least 20% of the proceeds of the bond issue are made available for owner financing of "targeted area residences" for at least one year after the date on which owner financing is first made available with respect to such residences; and "targeted area residences" in turn is a term defined under Code Section 143(j)(1)(A) to include residences in "qualified census tracts." Thus, as a practical matter, these updated census tract listings will have a fundamental impact on the operations of housing agencies who use single family bond proceeds to originate or invest in mortgages to eligible homeowners, down to the level of the forms used to process and fund eligible mortgage applications from prospective homeowners.

For lawyers who do not practice in the single family bond area, these rules will appear to be an impossibly tangled web, because they are. For bond practitioners who do render approving tax-exemption opinions on single family bond transactions, the situation may be much the same. But only bond lawyers in the latter category will likely have any interest in perusing the 345 pages of Revenue Procedure 2024-8. Happy reading to them.

A Personal Anecdote—IRS Secure Messaging System Update

In the Spring 2023 issue of *The Bond Lawyer*, I wrote a note on my rather frustrating experiences to that point with the "Secure Messaging" platform that was implemented sometime in 2022 by the Tax Exempt & Government Entities Division ("TE/GE") within the IRS. As I mentioned then, Secure Messaging is intended to be a quick and protected way to connect online with the IRS, permitting users to correspond with IRS agents and employees through a web browser interface, to exchange documents quickly and securely and thereby to reduce the need to call the IRS or to await the arrival of mail deliveries. Taxpayers and their authorized representatives are intended to access this messaging and document-sharing platform for all TE/GE "compliance activities" that began on or after June 22, 2022, according to the internal IRS memorandum (Control No. TEGE-04-0622-0018) that was circulated to TE/GE staff on this topic.

Most of the challenges I personally experienced up to Spring 2023 with Secure Messaging were at the front end, having to do with balky communications between the IRS agent and the staff of the bond issuer/taxpayer, who would be required to approve my access, as an authorized representative, to the messaging platform in connection with the audit of its bonds. That balkiness, and the lack of consistency I have observed from agent to agent regarding the use of the Secure Messaging portal for bond audit communications, seemed to me then to be gating issues to the smooth and effective use of Secure Messaging at the taxpayer end.

As it turns out, things did not go much better for me into the summer and autumn months of this year. Once issuer/taxpayer authorization was sorted out, I was told that the Secure Messaging system was rejecting my work email, for reasons that were not adequately described to me. After taking a fair amount of time and making considerable efforts to sort the problem with the IRS agent, I was ultimately stymied and could not gain access to the messaging platform in connection with the audit I was then working on. At the agent's request, I wound up mailing a physical copy of an audit submission, running several hundred pages, via the U.S. postal service.

Months later, on a different bond audit involving a different issuer and a different IRS agent, I was asked again to use Secure Messaging for communications. I explained to this agent the troubles I had experienced on my first attempt to validate my credentials on the platform. This agent suggested that we proceed notwithstanding, and shortly after I was told again that the platform was rejecting my work email address. I was asked whether I'd be willing to use my personal email address for Secure Messaging communications. I demurred. Again, the reasons why my work email was being rejected were not clearly explained. It appears that it may be that the use of my work email for other IRS interactions in the past, such as for registration for a Preparer Tax Identification Number (PTIN), may have "confused" the Secure Messaging system; I am not entirely sure whether or why that would have been the case. This agent persisted, however, and I believe he consulted with at least two IRS information technology specialists behind the scenes. Finally, after some additional effort, a workaround solution was identified: with the help of the IT group at my firm, a "secondary" or "dummy" work email was established for me, for use on a dedicated basis with the Secure Messaging system. And so, after the better part of six months, I finally have access to the platform.

I hope that other NABL members have not experienced the same challenges. All I can say is that there must be a better way.

Another Personal Anecdote—Outlook for IRS-TEB Staffing

Speaking of bond audits and IRS agents, I will close with a few personal observations on current levels of IRS bond audit activity. In my practice, I am beginning to see an uptick in the numbers of audits that are opening and a proliferation of new faces within TE/GE handling these audits. Based on the IRS funding commitments that are currently in place (though perhaps not entirely secure—see the recent press reports about the proposal in the House of Representatives to rescind the stepped-up IRS funding levels, which were enacted in 2022 under the Inflation Reduction Act, as a pay-for to provide aid to Israel and Ukraine), we can reasonably anticipate that the trend will continue and that we will see more IRS audits of bond transactions in the coming year, and more new IRS agents conducting business for TE/GE.

As we know from past experience, upticks in the level of IRS audit activity in the municipal market can present real challenges for issuers and borrowers. On top of the inconvenience and expense associated with every bond audit, upticks in audit activity and particularly new IRS staffing can impose incremental, but very real, costs on our client base. Just recently, on a site visit conducted by an IRS agent in connection with an ongoing bond examination (IRS agents seem to be insisting on these site visits across the board lately), the agent was accompanied by a “trainee” who, I was told, was not otherwise involved in the matter but was tagging along to observe how a site visit of a bond-financed facility should be conducted. Fair enough. Presumably this other TE/GE staffer will be out on her own soon conducting bond audits. The real issue, though, is that too often, IRS agents newly arrived at TE/GE, who have no prior experience with the tax-exempt bond market nor perhaps with the public sector, require prodigious amounts of on-the-job training from people like me in order to carry out their bond audits, and especially to get to the right results. The level of errancy in terms of red-herring issues raised and unsupportable interim positions taken by “green” agents can be very high. Better and more in-depth training and closer supervision by senior IRS staff can help, but I’m afraid this is a structural issue that many of us will be dealing with face-to-face in 2024. Be prepared.

My very best wishes to all of you at year’s end; may you all thrive in 2024.