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After the Bond Issuance

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Presented by:
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Outline

- Federal Tax Law Considerations
  - Investment and Spending of Bond Proceeds
  - Private Business Use
  - Additional Post-Issuance Compliance Items
- Securities Law Considerations
  - Annual Continuing Disclosure Filings
  - Reportable Event Disclosure Filings
  - Disclosure Policies and Procedures

Investing Bond Proceeds; Arbitrage Rebate

- Arbitrage for Tax Purposes
  - Difference between (i) what would have been earned if tax-exempt bond proceeds were invested at bond yield and (ii) the earnings on the investment of such tax-exempt bond proceeds in higher yielding securities.
- Rebate
  - Issuer must pay (or rebate) arbitrage profits to federal government.
  - Anything above bond yield gets paid to the US Treasury, unless you meet one or more exceptions
    - Small Issuer Exception
    - Spend-Down Exceptions

Spend Down of Bond Proceeds

- 3-Year Spend Down Requirement
  - Bonds issued for capital projects generally qualify for a 3-year temporary period
    - A temporary period is a period of time during which bond proceeds may be invested at materially higher yields than the bond yield
  - Based on reasonable expectations at the time of issuance
    - Must expect to spend sale and investment proceeds:
      - Expenditure Test – 85% within 3 years
      - Time Test – 5% within 6 months

Have Unspent Proceeds?

- Beginning on the third anniversary of the issuance of the bonds, any unspent proceeds must:
  - Be yield-restricted
    - Yield on investments can’t exceed the yield on the bonds
  - Be invested in investments which are not guaranteed by the federal government
    - No FDIC-insured CDs
    - Exception for U.S. Treasury Securities

Arbitrage Rebate Post-Issuance Tasks

- Track Arbitrage Rebate (investment returns against bond yield)
- Keep separate account/accounting of expenditure of bond proceeds and bond-financed projects
- Monitor compliance with temporary period expectations for expenditure of bond proceeds
- Monitor compliance with 6-month, 18-month or 2-year spending exceptions to rebate, if relevant
- Arrange for timely computation of rebate liability and, if rebate is payable, for timely filing of Form 8038-T and rebate payment

Private Business Use

- Tax-exempt Bonds cannot be private activity bonds
- A Private Activity Bond is a bond that fails both:
  - The Private Business Use Test
  - The Private Payments/Security Test
- De Minimis Allowance
  - Private business use is limited to 10%, but
  - 5% limit for “unrelated” or “disproportionate” private business use (with little guidance from the IRS), so most tax counsel use the 5% limit as the baseline

Private Business Use and Payments

- "Private business use"
  - More than 5% of bond proceeds finance a public facility used by a non-governmental trade or business
  - Examples of private use:
    - Sale, transfer or lease of property to private user
    - Management of property by private user under a management contract
- "Private payment or security"
  - More than 5% of debt service on the bonds is secured by an interest or derived from payments related to private use
  - Example of private payment:
    - Payments of lease rentals to the issuer by a private operator

Private Business Use Post Issuance Tasks

- Allocate bond proceeds and funds from other sources to ensure that bond proceeds are used for qualifying costs
- Monitor private use of bond-financed facilities
  - Ensure compliance with applicable percentage limitations
- New sale, lease license, management contract?
  - Determine whether applicable exception applies or whether it triggers failure of test
- Keep records of leases and management contracts even if expired

Final Post-Issuance Tax Tasks

- Record Retention
  - Retain records related to expenditure of bond proceeds and use of facilities for term of bonds plus 3 years
  - Term of refunding bonds plus 3 years for refunded issues
- Post Issuance Compliance Policy with the following components:
  - Designate a compliance officer
  - Retain accurate records
  - Implement procedures to timely identify and correct non-compliance
  - Report periodically to elected officials

Continuing Disclosure Requirements

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Continuing Disclosure

- Applies to any Issuer that has publicly-sold bonds outstanding
  - Does not apply to private placements
  - Exception – Par amount of Bonds is less than $1 million
- Three Components
  - Reportable Events
  - Audited Financial Statements
  - Annual Financial Information
    - Does not apply if, at time of issuance, issuer had less than $10 million outstanding

Filing Timelines

- Reportable Events
  - Within 10 business days after occurrence of the event
- Audit/Annual Financial Information
  - Determined by the Agreement
  - Typically 210 days after the close of the fiscal year

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Reportable Events

- Most common
  - Rating Change
  - Bond Call
  - Payment Delinquency
- Two new events added after February 27, 2019

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New Reportable Events

- Either
  - Incurrence of a Financial Obligation if Material, or
  - Agreement to covenants, events of default, remedies, priority rights, in a Financial Obligation which affect security holders, if material
- Default, Acceleration, Termination, Modification of Terms or similar event with respect to a Financial Obligation reflecting financial difficulty

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Consequence of CDU Filing Failure

- Bondholders may sue for specific performance
- Rule 15c2-12 requires issuers to disclose CDU non-compliance in official statements (five year look back)
- May impact access to market or result in increased interest rates on new issuances
- Districts that fail to make CDU filings may also face SEC action for other statements that reach the market, if materially misleading

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