PUBLIC FINANCE ALERT
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House tax reform bill eliminates private activity bonds and advance refundings

On November 2, 2017, the House Ways & Means Committee released its tax reform proposal, H.R. 1, the “Tax Cuts and Jobs Act.” If enacted, the bill would make sweeping changes to many areas of the tax law, including dramatically reducing the ability of state and local governments to issue tax-exempt bonds by eliminating advance refundings and all private activity bonds. The changes would apply to all bonds issued after December 31, 2017, with one notable exception for stadium financings that would be effective immediately. The bill contains no transition rules allowing for refundings of bonds issued prior to the effective dates of the rules contained in the bill.

Elimination of private activity bonds

The bill retains the ability to issue “governmental” bonds on a tax-exempt basis, but eliminates *all* private activity bonds that can currently be issued on a tax-exempt basis. More specifically, the following categories of bonds would be repealed:

- *Exempt Facility Bonds.* The bill eliminates all categories of exempt facility private activity bonds including bonds issued for low-income residential rental projects; airports; facilities for the treatment of water, sewage and solid waste; and bonds issued for qualified highway or surface freight transfer facilities, which is the private activity bond program that is heavily utilized for P3 projects. The elimination of bonds for residential rental projects is particularly troubling as bonds issued for these projects can qualify the owner to receive the low-income housing tax credit under the Code, which provides substantial equity for the financing of these projects.
- *Qualified 501(c)(3) Bonds.* Most significantly, the bill eliminates the ability to issue bonds to finance activities conducted by qualified nonprofit organizations. The elimination of this category of private activity bonds would have an enormous impact on the cost of financing nonprofit hospitals, universities, secondary schools, museums and other charitable activities.
- *Mortgage Revenue Bonds.* The bill eliminates mortgage revenue bonds and veterans mortgage revenue bonds issued to provide financing for low-income and other qualified persons to acquire owner-occupied residences, a program utilized in most areas of the country. The bill would similarly eliminate mortgage credit certificates issued to

homeowners under the Code, which is used by state and local governments in lieu of issuing bonds to subsidize the purchase of owner-occupied residences.

- *Small Issue Bonds and Student Loan Bonds.* The bill eliminates the ability to issue bonds for manufacturing facilities that are utilized by many small businesses. It also eliminates bonds issued to finance student loans, which are an important tool for students dealing with the increasing costs of higher education.

Elimination of advance refundings and other changes impacting governmental bonds

While the bill retains the ability to issue governmental bonds, it makes some significant changes that impact how those bonds are issued:

- *Repeal of Advance Refunding Bonds.* The bill eliminates the ability to advance refund governmental bonds after December 31, 2017. As a result, governmental bonds could only be current refunded after that date. The inability to advance refund bonds could cause issuers to forego traditional no-call periods or to lose opportunities to refinance debt at a lower cost, both of which would result in increased borrowing costs to state and local governments.
- *Elimination of Financing for Professional Sports Stadiums.* The bill eliminates the ability of governmental issuers to finance professional sports stadiums. A professional sports stadium is defined as any facility (or appurtenant real property) that is used as a stadium or arena for professional sports exhibitions, games or training for at least five days in any calendar year. This provision would be effective immediately for bonds issued after November 2, 2017.
- *Elimination of $15 Million Limit.* On a minor, positive note, the bill eliminates the $15 million per issue cap on private use that currently impacts large governmental issuers.

Repeal of tax credit bonds

The bill eliminates direct-pay tax credit bonds for any category of bonds that can still be issued (e.g., new clean renewable energy bonds for which the IRS is currently taking applications from public power providers under Notice 2017-66). Issuers would continue to receive payments for tax credit bonds already issued, but no new bonds could be issued after December 31, 2017.

No transition rules

Notably, the bill does not contain any transitional relief that would allow for advance refundings of governmental bonds issued prior to January 1, 2018; refundings of private activity bonds or tax credit bonds issued before January 1, 2018; financing after 2017 of private activity bond projects that are under construction or otherwise in progress; or refundings of stadium bonds issued before November 3, 2017.

Next steps

The Ways & Means Committee is expected to debate the bill starting Monday, November 6, and then vote to report the bill to the full House. The Senate Finance Committee is considering its own tax reform legislation that is expected to be released in mid-November.

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