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IRS provides relief for municipal bond issuers in response to COVID-19 pandemic

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On May 4, 2020, the Internal Revenue Service (IRS) released Revenue Procedure 2020-21 and Notice 2020-25, which provide relief for issuers of tax-exempt bonds in two ways. Revenue Procedure 2020-21 permits telephonic "TEFRA" hearings related to the approval of tax-exempt private activity bonds under the Internal Revenue Code (Code). Notice 2020-25 permits issuers to purchase and hold their "qualified tender bonds" and commercial paper for an extended period without resulting in a reissuance or deemed retirement of the debt for purposes of the tax-exempt bond rules under the Code. This guidance is further discussed below.

Revenue Procedure 2020-21 — Allows TEFRA hearings held by teleconference

In order for interest on an issue of private activity bonds (PABs), including 501(c)(3) bonds and exempt facility bonds, to be exempt from federal income taxes, the issuance must be approved by applicable governmental units following a public hearing (a "TEFRA" hearing) for which reasonable public notice has been provided. The Treasury Regulations provide that a public hearing for this purpose means a forum providing a reasonable opportunity for interested individuals to express their views, orally or in writing, on the proposed issue of bonds and the location and nature of the proposed project. Further, a public hearing must be held in a location that, based on the facts and circumstances, is convenient for residents of the approving governmental unit.

As a result of the COVID-19 pandemic, many governmental issuers have been restricted or prohibited from holding in-person meetings, including TEFRA hearings. In response, many state governments have approved the holding of public meetings and hearings by teleconference or webinar. Issuers have been concerned that holding TEFRA hearings via teleconference or webinar may not meet the requirements of the Treasury Regulations due to IRS statements, including that "[t]he Treasury Department and the IRS have determined that, although these technologies may be effective for other purposes, they cannot replace a conventional public hearing conducted in-person because they are not sufficiently reliable, publicly available, susceptible to public response, or uniform in their features and operation." (T.D. 9845).

Revenue Procedure 2020-21 resolves these concerns by allowing TEFRA hearings to be held by teleconference. Specifically, the Revenue Procedure provides that a hearing that is held by a teleconference that is accessible to the residents of the approving governmental unit by calling a toll-free telephone number will be treated as an effective public hearing under the Treasury Regulations. The Revenue Procedure further provides that as long as a teleconference with a toll-free number is utilized, issuers are not precluded from also offering additional access to the hearing by other telephone numbers or by internet-based meeting technology (e.g., Zoom or Webex). Public hearings held solely via such internet-based meeting technology will not meet the requirements of the Revenue Procedure.

The foregoing relief is available for hearings held during the period beginning on May 4, 2020, and ending on December 31, 2020. For public hearings in which public notice was provided on or before May 11, 2020, the foregoing relief is available provided the toll-free number is provided at least 48 hours prior to the hearing by a posting on the issuer's website that complies with the requirements of the existing Treasury Regulations. In addition, issuers are permitted to apply the Revenue Procedure to public hearings that were held telephonically before May 4, 2020, in the manner permitted by the Revenue Procedure.

Notice 2020-25 — Allows issuers to purchase and hold their own tax-exempt qualified tender bonds and commercial paper for extended period

During the 2008 financial crisis, the IRS released a series of notices that dealt with the failure to remarket auction rate bonds and variable rate demand obligations ("qualified tender bonds") as a result of market disruptions at the time. As part of that guidance, IRS Notice 2008-41 provides as a general rule that a bond purchased by or on behalf of a governmental issuer pursuant to a qualified tender right will not be treated as retired until not later than the end of the 90-day period after the date of such purchase. A key result of a bond being treated as retired is that it may not be resold on a tax-exempt basis. To provide further temporary relief during the 2008 financial crisis, Notice 2008-41 extended the 90-day period to 180 days with respect to any purchase by or on behalf of a governmental issuer pursuant to a qualified tender right as long as the purchase occurred before a certain date. This relief was later expanded in a separate notice to include tax-exempt commercial paper.

In 2018, the IRS and Treasury Department issued proposed Treasury Regulations (the "Proposed Treasury Regulations"), which provide guidance similar to that in Notice 2008-41, including the ability of governmental issuers to purchase and hold their own tax-exempt qualified tender bonds for a 90-day period. Issuers currently have the option to apply either the rules in the Proposed Treasury Regulations or Notice 2008-41.

Notice 2020-25 addresses and updates the guidance provided in Notice 2008-41 and the Proposed Treasury Regulations in the context of the market disruption caused by the COVID-19 pandemic and extends the periods in which issuers may purchase and hold their own qualified tender bonds and commercial paper. First, for purpose of the tax-exempt bond rules, issuers may purchase their qualified tender bonds and commercial paper during calendar year 2020 without causing such bonds to be treated as retired as long as they do not hold the bonds beyond December 31, 2020. For any purchased commercial paper, a refinancing with tax-exempt commercial paper during calendar year 2020 will be treated as part of the same issue as the issue of which the purchased tax-exempt commercial paper was a part.

Second, the Notice extends the 90-day period in Notice 2008-41 and the Proposed Treasury Regulations described above to 180 days for any purchase of qualified tender bonds (but not commercial paper) by an issuer pursuant to a qualified tender right as long as such purchase occurs during calendar year 2020. This differs from the first relief provided in the Notice in that a bond purchased pursuant to this provision may be held beyond December 31, 2020, as long as the 180-day requirement is satisfied.

Notice 2020-25 further provides that for arbitrage purposes under Section 148 of the Code, a qualified hedge (for example, an interest rate swap) with respect to bonds purchased and held pursuant to the Notice is not deemed terminated as a result of the governmental issuer's purchase and retention of the hedged bonds during calendar year 2020.

Notice 2020-25 is effective May 4, 2020, and may also be applied retroactively to purchases on or after January 1, 2020.

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