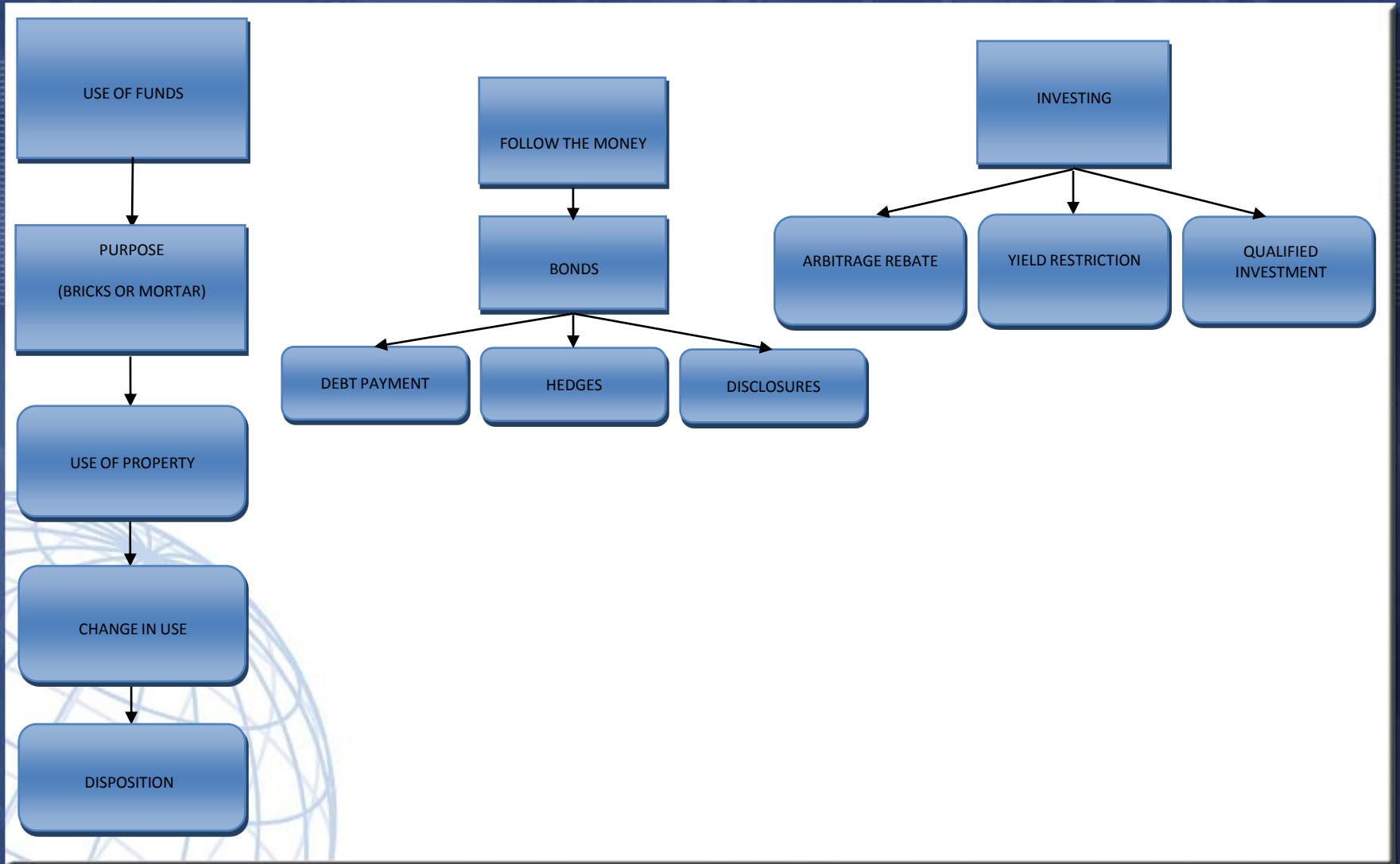


**Why Post-Issuance Compliance Matters
in Tax-Exempt Bond Financings
and How Localities Can Better
Prepare Themselves for an IRS Examination**

**Virginia Government Finance Officers Association
Fall Conference**

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- **Post-issuance tax compliance begins with the debt issuance process itself and provides for a continuing focus on investments of bond proceeds and use of bond-financed property. It will require identifying existing policies, the responsible people, the applicable procedures, and the affected population.**

After the Bonds Are Issued Then What?

**Advisory Committee on Tax-Exempt and
Governmental Entities**

June 13, 2007

IRS Enforcement Efforts

- Originally contained in Exempt Organizations
- Became distinct office in 1990
- Today has staff of approximately 100
- www.irs.gov/ top bar-upper right hand corner:
“Tax-Exempt Bond Community”

- Two Operations:
 - Field Operations (Agents)
 - Compliance and Program Management (Legal – Bond Law Specialists)



- Facilitate voluntary compliance (“soft contacts”)
- Enforce requirements of the law (“hard exams”)

- Outreach and Education Events
 - June 2011 Webinar on Direct Pay Bonds
 - September 2011 Teleconference on Voluntary Compliance Program
- Compliance Questionnaires
 - Not an audit or investigation
 - Voluntary
- Voluntary Closing Agreement Program
 - Now “rewards” written, post-issuance compliance procedures

Form 14002 (September 2008)	Department of the Treasury — Internal Revenue Service Governmental Bond Financings Compliance Check Questionnaire	OMB No. 1545-2071
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This questionnaire asks for information regarding your post-issuance bond compliance and record retention practices. Please complete the questionnaire and follow the instructions in the accompanying letter for returning it to us.

Name of Governmental Entity: _____

Employer Identification Number: _____

PART I - POST-ISSUANCE COMPLIANCE - GENERAL

1. Do you have written procedures to ensure that governmental bond financings remain in compliance with the following federal tax requirements after the bonds are issued:

a. Proper use of bond proceeds? If Yes, date they were implemented? _____ (dd/mm/yyyy)	<input type="checkbox"/> Yes	<input type="checkbox"/> No	
b. Timely expenditure of bond proceeds? If Yes, date they were implemented? _____ (dd/mm/yyyy)	<input type="checkbox"/> Yes	<input type="checkbox"/> No	
c. Proper use bond-financed property? If Yes, date they were implemented? _____ (dd/mm/yyyy)	<input type="checkbox"/> Yes	<input type="checkbox"/> No	
d. Arbitrage yield restriction and rebate? If Yes, date they were implemented? _____ (dd/mm/yyyy)	<input type="checkbox"/> Yes	<input type="checkbox"/> No	
e. Timely return filings and other general requirements? If Yes, date they were implemented? _____ (dd/mm/yyyy)	<input type="checkbox"/> Yes	<input type="checkbox"/> No	
f. Documenting compliance with other general requirements? If Yes, date they were implemented? _____ (dd/mm/yyyy)	<input type="checkbox"/> Yes	<input type="checkbox"/> No	

Describe in detail your procedures for each of the above items (a-f) and how you implement them, including dates of revisions, if any. In lieu of the above descriptions, you may attach a copy of your written procedures. If you have no written procedures, explain what guidelines you have in place and from what source these guidelines are derived that ensure bond financings are in compliance with federal tax requirements. *(Attach sheet with description)*

2. Who is primarily responsible for monitoring post-issuance compliance of bond financings?

<input type="checkbox"/> Elected or appointed officials	What is the person's title? _____
<input type="checkbox"/> Non-elected or non-appointed officials	What is the person's title? _____
<input type="checkbox"/> Staff Person	What is the person's title? _____
<input type="checkbox"/> Other Person	What is the person's title? _____
<input type="checkbox"/> None	

3. If more than one individual is responsible for maintaining the records related to bond financings, do you have written procedures for assigning responsibilities that would ensure compliance with these financings? Yes No N/A
 If Yes, date they were implemented? _____ (dd/mm/yyyy)

Describe in detail your procedures for assigning responsibility to each party involved and how you implement them, including dates of revisions, if any. In lieu of the above description, you may attach a copy of the written procedures used to assign responsibility to those individuals handling the bond financings. If you have no written procedures, explain what guidelines you have in place and from what source these guidelines are derived that ensure bond financings are in compliance with federal tax requirements. *(Attach sheet with description)*

- Tax Exempt Bonds Voluntary Closing Agreement Program

- Section 7121 of the Code

- Notice 2008-31 and IRM 7.2.3

- Must identify a violation
 - Anonymous requests
 - Identified violations for which voluntary closing agreements may be obtained:

- For example-

- Too much private use
 - Exceeding capital expenditure limitations
 - Failure to timely reinvest proceeds in 0% SLGs

- Voluntary closing agreement typically pre-empts later examination

- Updated administrative procedures for VCAP IRM 7.2.3 released August 5, 2011
 - Reduced settlement amount if written post-issuance compliance procedures are in place

Plan – 200 issues each year

- 2001 – Private Activity Bonds
- 2002 – Governmental issuers
- 2003 – Test Form 8038-T compliance
- 2004 – Escrows with 0% Rolls
- 2005 – Open Market Escrows
- 2006 – Charitable Financings
- 2007 – Tax Exempt Bond Checklist
- 2009 – Governmental issuers Checklist
- 2010 – Busy with BABs
- 2011 – Audits of Advance Refundings; TRANs; Multifamily bond issues;
Developer – driven bond issues (private use; private payments)

- **Compliance Check Questionnaires**
 - A compliance check is not an examination
 - No penalty for failing to respond; however refusal to participate will likely lead to an examination
- **Focused Correspondence**
 - “We have been provided with certain information”
 - “We have learned the following; please voluntarily explain”
- **Full Exams**
 - Random exams selected on Form 8038-G, Form 8038-CP, Form 8038 data
 - Program exams selected on type of bond purpose (multifamily; advance refunding)
 - Targeted exams for potential abuse
 - Examination and audit mean the same thing
- **Rebate Refund Claims**
 - Will seeking refund trigger an exam/audit?

Historically:

- Random audits
- Issues identified by third parties
- Issues with possible abuses (GICs, Escrows, etc.)
- Correspondence audits
- Issuer refund requests (refund only)
 - Form 8038-T questions
- Coordination with the SEC
 - Memorandum of Understanding between IRS and SEC
- Form 8038-T questions
- Coordination with the Department of Justice (GIC-bidding investigation)

In examination of 8038 series returns today, main focus is on:

- General Classification (random audits)
- Follow-up on focused correspondence
- Specific initiatives
 - Bond issues at 5 year computation date; allocations and unspent proceeds
 - Refundings – both current and advance

- In traditional role, Tax Certificate (“TC”) spoke solely to reasonable expectations of issuer at date of issue
- Traditionally only an “acknowledgement” of continuing rebate monitoring
- In early responses to 501(c)(3) bond questionnaires and then governmental bond questionnaires, TC was often referenced as the sole “written procedure” for post-issuance compliance
 - New VCAP procedures: looking to bond documents as “written procedure” is insufficient
- New context: governmental bond questionnaires, post-issuance compliance checks, increased random exams, increased number of program exams, TC is looking beyond the date of issuance.

- New sections to many TC:
 - Acknowledging that TC constitutes the “written procedures” (but, after new VCAP procedures, is this enough?)
 - Committing a “Designated Individual” of an issuer to monitor/compare post-issuance actual facts against procedures and requirements set forth in TC
 - Training
- Designated individual particularly important for large systematic issuers in which responsibilities for bond issues are spread across several departments
 - IRS has noted this concern
 - By analogy San Diego and State of New Jersey SEC enforcement actions in which City or State departments failed to communicate, leading to material misstatements or omissions

- Form 14002
- Carrot versus stick
- 13% non-response rate

- Form 14127
- Record-keeping for “tax advantaged treatment”
- Issue price and EMMA (focus between sale date and closing date)
- Reportedly even lower response rate
- IRS has said that there are very few follow-up exams

***Seven Elements of an
Effective Post-Issuance Tax
Compliance Program***

1. Written policies & procedures
2. Team assigned to manage compliance process
3. Record retention
4. Arbitrage rebate & yield restriction compliance
5. Private business use compliance
6. Periodic review process
7. Staff training and education

- IRS wants exempt organizations to create/adopt written procedures to manage tax compliance
 - Currently not a federal tax law requirement
 - Organizations with procedures are viewed as more likely to comply
- 2007 Non-Profit compliance check, 2009 Governmental Issuer compliance check, and Build America Bond compliance check repeatedly ask about the existence of written procedures

- IRS Form 8038-B (identifies Build America Bond issues) includes Miscellaneous Section (VII)
 - Asks about written procedures to manage tax compliance
- Instructions for 8038-CP state that it should not be filed unless bonds are currently in compliance
- Line 43 of new, revised Form 8038 (4/11) and Lines 43, 44 of new, revised Form 8038-G (9/11) ask if issuer has established written procedures:
 - (1) “to ensure that all nonqualified bonds of an issue are remediated”
 - (2) “to monitor the requirements of Section 148”

- Start by documenting your current unwritten procedures
- Review and incorporate current written procedures
- Use bond documents and Governmental Bond Compliance Check as guides
 - Bond documents: Non-Arbitrage Certificate, Arbitrage Rebate Compliance Instructions, Trust Indenture requirements, etc.
 - Gov't Compliance Check Questionnaire – Form 14002 (can be found at <https://www.irs.gov/pub/irs-tege/f14002.pdf>)
 - Direct Pay Bonds Compliance Check Questionnaire – Form 14127 (can be found at https://www.irs.gov/pub/irs-tege/form_14127.pdf)

- Other Resources:
 - NABL/GFOA Post-Issuance Compliance Checklist
(www.gfoa.org/downloads/PostIssuanceCompliance.pdf)
 - ACT Paper – “After the Bonds Are Issued, Then What?”
(www.irs.gov/pub/irs-tege/bonds_act_0607.pdf)

- Assign individual(s) responsible for compliance management
- Address succession issues

- IRS Guidance – IRC Section 6001 – general rule for proper retention of records for federal tax purposes.
 - Basic Records (e.g. Transcript)
 - Documentation on expenditures of bond proceeds
 - Documentation on use of bond finance property (public vs. private use, management contracts, research agreements)
 - Documentation on all sources of payment or security for the bonds
 - Documentation on investment of bond proceeds

Sample Records to Retain:

- Board minutes, resolutions
- Feasibility studies, appraisals
- Bond transcripts
- Newspaper ads, misc. correspondence
- Investment records – bank statements, investment transaction information (e.g., trade confirms), etc.
- Expenditure histories – invoices, check images, documents showing and supporting disbursements
- IRS Filings – 8038T (and related checks), 8038CP
- Records related to acquisition of investment agreements and interest rate swaps
- Payments for a letter of credit or standby bond purchase agreement
- Arbitrage rebate and yield restriction compliance reports

IRS Tax-Exempt Bond FAQs regarding Record Retention Requirements

(www.irs.gov/taxexemptbond)

- Why keep records?
- Who may maintain records?
- What are basic records to maintain?
- Are these the only records to be maintained?
- In what format must records be kept?
- How long should records be kept? (“For as long as bonds are outstanding plus 3 years after final redemption date”)
- How does general rule apply to refundings?
- What happens if records are not maintained?
- Can failure to properly maintain records be corrected?
- Are there exceptions to the general rule regarding record retention for certain types of records?

- Code Section 148 – Arbitrage and Yield
 - Expenditure of bond proceeds
 - Temporary Periods
 - Rebate – Spenddown Exceptions, Small Issuer Exemption
 - Yield Calculation – Bond, Investments
 - Yield Reduction Payments
- Rebate Consultant

- Tax law limits private use of TE financed facilities to 5% unrelated use, 10% for related use
 - Average use measured over the life of the finance facility
- Maintain records of business activities
 - Rental of tax-exempt financed facilities for private functions
- Legal counsel review of all management & service agreements, leases, sub-leases, naming rights contracts, etc.
- Coordinate use of tax-exempt bond financed facilities with administrative team to ensure compliance
- Deliberate Actions – Remedial Actions

- Don't let a good plan go to waste
- Individuals must review; ask questions and monitor compliance

- Educate staff about applicable rules, written procedures
- Internal communication between departments
- Procedures to train new staff
- Continuing education – Evolving regulatory landscape
- Use of outside vendors

- New event notices under SEC Rule 15c2-12 pick up 5701 notices of issues and preliminary adverse letters
- No materiality threshold
- Many more exam notices being posted on EMMA
 - Ease of filing, more occurrences

Questions?

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