New Tax Bill Threatens Important Tax-Exempt Bond Provisions

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This alarm is somewhat diminished with the Senate Finance Committee's proposed tax bill, which does not change the current treatment of PABs but still eliminates advance refundings. The tax bill has industry groups lined up in opposition, and for good reason: the potential loss of PABs and advance refundings would most likely lead to increased cost to state and local governments and nonprofit organizations seeking to finance vital public services.

PABs provide critical funding for nonprofit health care providers, universities and research institutions, schools, multifamily housing projects, nonprofit organizations, public-private partnerships, and infrastructure projects. These projects benefit communities, foster job creation, and entice private sector investment in communities around the county. More than $84.6 billion in PABs were issued last year, representing almost 19 percent of the new issue municipal bond market.

Meanwhile, advance refundings, which made up almost 27 percent of the market in 2016, allow governmental issuers to take advantage of favorable interest rates to lower overall costs, resulting in substantial savings to taxpayers. More than $120 billion in advance refundings were issued last year, saving taxpayers at least $3 billion. Current federal law sets the limit for advance refunding to one, curbing any kind of abuse while allowing advance refundings to lower the cost of borrowing for projects that directly benefit taxpayers.

The potential elimination of PABs and advance refundings could increase costs of borrowing for state and local governments and nonprofit organizations, as interest rates would need to increase to remain attractive to investors when their interest earnings are subject to taxation. The Council of Development Finance Authorities (CDFA) estimates that interest rates for borrowers would need to increase by 1.5-2.5 percent for private activity bonds, an increase that would cause the cost of borrowing for issuers to rise by as much as 25-35 percent. This cost will ultimately be borne by

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taxpayers and individuals relying on facilities, projects, and public services, who would see a rise in local taxes, tolls, low-income housing rent and mortgage payments, and hospital charges. Ultimately, eliminating PABs could lead to a reduction in the amount of infrastructure projects that could be undertaken, as issuers struggle to finance capital projects.

Municipal bond market industry groups have joined together to strongly oppose the provisions of the proposed tax bill. As the House and Senate deliberate on their bills, Congress will hear from municipal bond market industry groups of the benefits that PABs and advance refundings provide to both local communities and the nation's economy as a whole.

For more information, please contact David Rogers, Emmett Kelly, Michael Elliott or any other attorney in Frost Brown Todd's Public and Project Finance Practice Group.

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