

IRS launches compliance initiative for Build America Bonds

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Last week, the Internal Revenue Service began an effort to verify compliance with the tax code requirements applicable to Direct Pay Build America Bonds and Recovery Zone Economic Development Bonds. The interest on Build America Bonds and Recovery Zone Economic Development Bonds (collectively known as "Direct Pay Bonds") is taxable, but issuers are entitled to a 35% or 45% interest reimbursement from the Federal government depending on the type of Direct Pay Bonds. To be entitled to the credits, certain requirements must be satisfied at the time the Direct Pay Bonds are issued and for so long as the Direct Pay Bonds remain outstanding.

The IRS has begun sending questionnaires to all governmental issuers of Direct Pay Bonds to confirm that the various requirements for the credits paid to issuers of Direct Pay Bonds were satisfied at closing and will continue to be satisfied over time, as well as to confirm that such issuers are keeping sufficient records to show such compliance.

This compliance initiative is not unexpected. In April, 2009, the IRS indicated that future procedures for Direct Pay Bonds would include ongoing compliance safeguards that would involve periodic information returns on such Bonds at least annually. For this reason, on transactions where we have acted as Bond Counsel, we informed issuers that annual compliance checks were likely at the time such bonds were issued.

The questionnaire seeks information with respect to compliance with the specific requirements applicable to Direct Pay Bonds. The specific requirements for qualification include limitations on the amount of premium generated on initial sales of the Direct Pay Bonds, limitations on the amount of costs of issuance payable from Direct Pay Bond proceeds, the requirements to expend all proceeds on capital expenditures (other than proceeds used for issuance costs and to fund a reserve fund, if any), and limitations on the private use of the facilities financed with the Direct Pay Bonds, among other items. The IRS is seeking information regarding any written plans that an issuer of such Direct Pay Bonds has put in place to help in ensuring such compliance.

The questionnaire (and its related cover letter) are available from the Internal Revenue Service website.

The IRS also released a revised Form 8038-CP, the return used to claim the credits on Direct Pay Bonds. The major change from the prior version of 8038-CP is that issuers are now able to request an electronic payment of their credits, rather than be subjected to the delay waiting for a paper check to be mailed to them by the IRS. View the revised Form 8038-CP and its instructions.

If you have any questions or would like our advice in connection with completing a questionnaire for your bonds or developing a written plan to ensure ongoing compliance, please contact:

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