

**§ 1.148-8 Small issuer exception to rebate requirement.**

(a) *Scope.* Under section 148(f)(4)(D), bonds issued to finance governmental activities of certain small issuers are treated as meeting the arbitrage rebate requirement of section 148(f)(2) (the “small issuer exception”). This section provides guidance on the small issuer exception.

(b) *General taxing powers.* The small issuer exception generally applies only to bonds issued by governmental units with general taxing powers. A governmental unit has general taxing powers if it has the power to impose taxes (or to cause another entity to impose taxes) of general applicability which, when collected, may be used for the general purposes of the issuer. The taxing power may be limited to a specific type of tax, provided that the applicability of the tax is not limited to a small number of persons. The governmental unit’s exercise of its taxing power may be subject to procedural limitations, such as voter approval requirements, but may not be contingent on approval by another governmental unit. See, also, section 148(f)(4)(D)(iv).

(c) *Size limitation*—(1) *In general.* An issue (other than a refunding issue) qualifies for the small issuer exception only if the issuer reasonably expects, as of the issue date, that the aggregate face amount of all tax-exempt bonds (other than private activity bonds) issued by it during that calendar year will not exceed \$5,000,000; or the aggregate face amount of all tax-exempt bonds of the issuer (other than private activity bonds) actually issued during that calendar year does not exceed \$5,000,000. For this purpose, if an issue has more than a de minimis amount of original issue discount or premium, *aggregate face amount* means the aggregate issue price of that issue (determined without regard to pre-issuance accrued interest).

(2) *Aggregation rules.* The following aggregation rules apply for purposes of applying the \$5,000,000 size limitation under paragraph (c)(1) of this section.

(i) *On-behalf-of issuers.* An issuer and all entities (other than political subdivisions) that issue bonds on behalf of that issuer are treated as one issuer.

(ii) *Subordinate entities*—(A) *In general.* Except as otherwise provided in paragraph (d) of this section and section 148(f)(4)(D)(iv), all bonds issued by a subordinate entity are also treated as issued by each entity to which it is subordinate. An issuer is subordinate to another governmental entity if it is directly or indirectly controlled by the other entity within the meaning of § 1.150-1(e).

(B) *Exception for allocations of size limitation.* If an entity properly makes an allocation of a portion of its \$5,000,000 size limitation to a subordinate entity (including an on behalf of issuer) under section 148(f)(4)(D)(iv), the portion of bonds issued by the subordinate entity under the allocation is treated as issued only by the allocating entity and not by any other entity to which the issuing entity is subordinate. These allocations are irrevocable and must bear a reasonable relationship to the benefits received by the allocating unit from issues issued by the subordinate entity. The benefits to be considered include the manner in which—

- (1) Proceeds are to be distributed;
- (2) The debt service is to be paid;
- (3) The facility financed is to be owned;
- (4) The use or output of the facility is to be shared; and
- (5) Costs of operation and maintenance are to be shared.

(iii) *Avoidance of size limitation.* An entity formed or availed of to avoid the purposes of the \$5,000,000 size limitation and all entities that would benefit from the avoidance are treated as one issuer. Situations in which an entity is formed or availed of to avoid the purposes of the \$5,000,000 size limitation include those in which the issuer—

(A) Issues bonds which, but for the \$5,000,000 size limitation, would have been issued by another entity; and

(B) Does not receive a substantial benefit from the project financed by the bonds.

(3) *Certain refunding bonds not taken into account.* In applying the \$5,000,000 size limitation, there is not taken into account the portion of an issue that is a current refunding issue to the extent that the stated principal amount of the refunding bond does not exceed the portion of the outstanding stated principal

amount of the refunded bond paid with proceeds of the refunding bond. For this purpose, *principal amount* means, in reference to a plain par bond, its stated principal amount plus accrued unpaid interest, and in reference to any other bond, its present value.

(d) *Pooled financings*—(1) *Treatment of pool issuer*. To the extent that an issuer of a pooled financing is not an ultimate borrower in the financing and the conduit borrowers are governmental units with general taxing powers and not subordinate to the issuer, the pooled financing is not counted towards the \$5,000,000 size limitation of the issuer for purposes of applying the small issuer exception to its other issues. The issuer of the pooled financing issue is, however, subject to the rebate requirement for any unloaned gross proceeds.

(2) *Treatment of conduit borrowers*. A loan to a conduit borrower in a pooled financing qualifies for the small issuer exception, regardless of the size of either the pooled financing or of any loan to other conduit borrowers, only if—

- (i) The bonds of the pooled financing are not private activity bonds;
- (ii) None of the loans to conduit borrowers are private activity bonds; and
- (iii) The loan to the conduit borrower meets all the requirements of the small issuer exception.

(e) *Refunding issues*—(1) *In general*. Sections 148(f)(4)(D) (v) and (vi) provide restrictions on application of the small issuer exception to refunding issues.

(2) *Multipurpose issues*. The multipurpose issue allocation rules of §1.148-9(h) apply for purposes of determining whether refunding bonds meet the requirements of section 148(f)(4)(D)(v).

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**§ 1.148-9 Arbitrage rules for refunding issues.**

(a) *Scope of application*. This section contains special arbitrage rules for refunding issues. These rules apply for all purposes of section 148 and govern allocations of proceeds, bonds, and investments to determine transferred proceeds, temporary periods, reasonably required reserve or replacement funds, minor portions, and separate issue

treatment of certain multipurpose issues.

(b) *Transferred proceeds allocation rule*—(1) *In general*. When proceeds of the refunding issue discharge any of the outstanding principal amount of the prior issue, proceeds of the prior issue become transferred proceeds of the refunding issue and cease to be proceeds of the prior issue. The amount of proceeds of the prior issue that becomes transferred proceeds of the refunding issue is an amount equal to the proceeds of the prior issue on the date of that discharge multiplied by a fraction—

(i) The numerator of which is the principal amount of the prior issue discharged with proceeds of the refunding issue on the date of that discharge; and

(ii) The denominator of which is the total outstanding principal amount of the prior issue on the date immediately before the date of that discharge.

(2) *Special definition of principal amount*. For purposes of this section, *principal amount* means, in reference to a plain par bond, its stated principal amount, and in reference to any other bond, its present value.

(3) *Relation of transferred proceeds rule to universal cap rule*—(i) *In general*. Paragraphs (b)(1) and (c) of this section apply to allocate transferred proceeds and corresponding investments to a refunding issue on any date required by those paragraphs before the application of the universal cap rule of §1.148-6(b)(2) to reallocate any of those amounts. To the extent nonpurpose investments allocable to proceeds of a refunding issue exceed the universal cap for the issue on the date that amounts become transferred proceeds of the refunding issue, those transferred proceeds and corresponding investments are reallocated back to the issue from which they transferred on that same date to the extent of the unused universal cap on that prior issue.

(ii) *Example*. The following example illustrates the application of this paragraph of (b)(3):

*Example*. On January 1, 1995, \$100,000 of nonpurpose investments allocable to proceeds of issue A become transferred proceeds of issue B under §1.148-9, but the unused portion of issue B's universal cap is \$75,000 as of that date. On January 1, 1995, issue A has unused universal cap in excess of \$25,000. Thus,