GUIDE TO TAX CREDIT AND TAX EXEMPT BOND PROGRAMS
AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009

Recovery Zones

Recovery Zone bonds. The bill would create a new category of tax credit bonds for investment in economic recovery zones and expand access to tax-exempt bonds. The bill would authorize $10 billion in tax credit recovery zone economic development bonds and $15 billion in tax-exempt recovery zone facility bonds. These bonds could be issued during 2009 and 2010. Each state would receive a share of the national allocation based on that state's job losses in 2008 as a percentage of national job losses in 2008 (each state will receive a minimum allocation of these bonds). These allocations would be sub-allocated to local municipalities. Municipalities receiving an allocation of these bonds would be permitted to use these bonds to invest in infrastructure, job training, education, and economic development in areas within the boundaries of the State, city or county (as the case may be) that has significant poverty, unemployment or home foreclosures. Allocation amounts will be announced by the Department of Treasury.

Tribal Economic Development bonds. Under current law, tribal governments are limited in their ability to issue tax-exempt bonds. Projects funded by bonds issued by tribal governments must satisfy an "essential governmental function" requirement. This requirement is not imposed on projects funded by bonds issued by State and local governments, and can limit the ability of tribal governments to use tax-exempt bonds for economic development. The bill would temporarily allow tribal governments to issue $2 billion in tax-exempt bonds for projects without this restriction in order to spur economic development on tribal lands, and would require the Secretary of the Treasury to study whether this restriction should be repealed on a permanent basis. Allocation amounts will be announced by the Department of Treasury.

School Construction

Qualified School Construction bonds. The bill creates a new category of tax credit bonds for the construction, rehabilitation, or repair of public school facilities or for the acquisition of land on which a public school facility will be constructed. There is a national limitation on the amount of qualified school construction bonds that may be issued by State and local governments of $22 billion ($11 billion allocated initially in 2009 and the remainder allocated in 2010). There is a national limitation on the amount of qualified school construction bonds that may be issued by Indian tribal governments of $400 million ($200 million allocated initially in 2009 and the remainder allocated in 2010). Allocation amounts will be announced by the Department of Treasury.

Extension and increase in authorization for qualified zone academy bonds (QZABs). The bill would allow an additional $1.4 billion of QZAB issuing authority to State and local governments in 2009 and 2010, which can be used to finance renovations, equipment purchases, developing course material, and training teachers and personnel at a qualified zone academy. In general, a qualified zone academy is any public school (or academic program within a public school) below college level that is located in an empowerment zone or enterprise community and is designed to cooperate with businesses to enhance the academic curriculum and increase graduation and employment rates. QZABs are a form of tax credit bonds which offer the holder a Federal tax credit instead of interest.

"Build America" and High-Speed Rail bonds

Tax credit bond option for State and local governments ("Build America Bonds"). The Federal government provides significant financial support to State and local governments through the federal tax exemption for interest on municipal bonds. Both tax credit bonds and tax-exempt bonds provide a subsidy to municipalities by reducing the cash interest payments that a State or local government must make on its debt. Tax credit bonds differ from tax-exempt bonds in two principal ways: (1) interest paid on tax credit bonds is taxable; and (2) a portion of the interest paid on tax credit bonds takes the form of a Federal tax credit. The Federal tax credit offsets a portion of the cash interest payment that the State or local government would otherwise need to make on the borrowing. For 2009 and 2010, the bill would provide State and local governments with the option of issuing a tax credit bond instead of a tax-exempt governmental obligation bond. Because the market for tax credits is currently small given current economic conditions, the bill would allow the State or local government to elect to receive a direct payment from the Federal government equal to the subsidy that would have otherwise been delivered through the Federal tax credit for bonds.

Modify speed requirement for high-speed rail exempt facility bonds. Under current law, States are allowed to issue private activity bonds for high-speed rail facilities. Under current law, a high-speed rail facility is a facility for the transportation of passengers between metropolitan areas using vehicles that are reasonably expected to operate at speeds in excess of 150 miles per hour between scheduled stops. The bill would allow these bonds to be used to develop rail facilities that are used by trains that are capable of attaining speeds in excess of 150 miles per hour.

Other Bond Financing Tools

De minimis safe harbor exception for tax-exempt interest expense for financial institutions. Under current law, financial institutions are not allowed to take a deduction for the portion of their interest expense that is allocable to such institution's investments in tax-exempt municipal bonds. In determining the portion of interest expense that is allocable to investments in tax-exempt municipal bonds, the bill would exclude investments in tax-exempt municipal bonds issued during 2009 and 2010 to the extent that these investments constitute less than two percent (2%) of the average adjusted bases of all the assets of the financial institution.

Modification of small issuer exception to tax-exempt interest expense allocation rules for financial institutions. As described above, financial institutions are not allowed to take a deduction for the portion of their interest expense that is allocable to such institution's investments in tax-exempt municipal bonds. For purposes of this interest disallowance rule, bonds that are issued by a "qualified small issuers" are not taken into account as investments in tax-exempt municipal bonds. Under current law, a "qualified small issuer" is defined as any issuer that reasonably anticipates that the amount of its tax-exempt obligations (other than certain private activity bonds) will not exceed $10,000,000. The bill would increase this dollar threshold to $30,000,000 when determining whether a tax-exempt obligation issued in 2009 and 2010 qualifies for this small issuer exception. The small issuer exception would also apply to an issue if all of the ultimate borrowers in such issue would separately qualify for the exception. For these purposes, the issuer of a qualified 501(c)(3) bond shall be deemed to be the ultimate borrower on whose behalf a bond was issued.

Eliminate costs imposed on State and local governments by the alternative minimum tax. The alternative minimum tax (AMT) can increase the costs of issuing tax-exempt private activity bonds imposed on State and local governments. Under current law, interest on tax-exempt private activity bonds is generally subject to the AMT. This limits the marketability of these bonds and, therefore, forces State and local governments to issue these bonds at higher interest rates. Last year, Congress excluded one category of private activity bonds (i.e., tax-exempt housing bonds) from the AMT. The bill would exclude the remaining categories of private activity bonds from the AMT if the bond is issued in 2009 or 2010. The bill also allows AMT relief for current refunding of private activity bonds issued after 2003 and refunded during 2009 and 2010.