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A NEW CENTURY OF SERVICE 1912 | 2012

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November 2, 2011

IRS Authorizes Optional TEDB Volume Cap Extensions, Requests Comments on Reallocation of Volume Cap

On October 31, 2011, the Internal Revenue Service (the "IRS") published an Announcement describing two new features for the existing tribal economic development bond ("TEDB") program.

First, the IRS is providing an optional three-month extension process for existing volume cap allocations. Under current IRS guidelines, existing allocations expire December 31, 2011. The new extension process requires written extension requests to be submitted by November 30, 2011.

In addition, the Announcement proposes certain changes intended to improve the existing IRS allocation methodology for TEDBs. These proposed changes would govern the reallocation of the national $2 billion volume cap for TEDBs, upon the expiration or forfeiture of existing allocations. The IRS estimates that up to 95% or more of the $2 billion in Volume Cap allocations for TEDBs may become available for reallocation as of January 1, 2012. The IRS is seeking public comment on its proposed reallocation process, and the deadline for submitting comments is December 12, 2011.

As described in our earlier Alerts, TEDBs are a financing tool created by the American Recovery and Reinvestment Act of 2009 ("ARRA"). This financing tool allows Indian tribal governments, for the first time, to issue tax-exempt bonds for the same purposes as states and local governments without regard to two existing limitations: (1) the "essential governmental function" test, which the IRS has interpreted to bar certain projects that it believes are "commercial" in nature, and (2) the prohibition against the issuance of "private activity bonds" (other than for certain manufacturing facilities).

This Alert summarizes the key points set forth in the Announcement. This Alert also raises questions tribes and industry groups may wish to consider in providing comments in response to the Announcement.

Optional Three-Month Extensions of Existing Allocations

The Announcement provides a process for tribes that have received existing Volume Cap allocations to request extensions from the current administrative deadline for issuing their TEDBs (December 31, 2011). If the IRS grants an extension request, the deadline would be extended from December 31, 2011, to March 31, 2012.

Extension requests must be in writing and must include the following information:

1. A copy of the original IRS allocation letter;
2. Certain statements from an authorized official of the Indian tribal government, under penalty of perjury, including: (a) an explanation of the reason for the extension request; (b) a statement that the TEDBs are reasonably expected to be issued by March 31, 2012 for the project described in the original allocation application; (c) a statement that, upon issuance of the TEDBs, the proceeds will be spent with due diligence; and (d) a statement that the government official signing the extension request has knowledge of the facts and circumstances relating to the request and the original application, has examined the request and the original application, and that the information in the request and the original applications true, complete and correct.
3. Documentation demonstrating the reasonableness of the statements in the request that the TEDBs will be issued by March 31, 2012, and the proceeds will be spent with due diligence for the project described in the original application.

In the Announcement, the IRS stated that it does not expect to grant extensions unless a request demonstrates both a substantial and a reasonable basis for the expectation that the TEDBs will be issued by March 31, 2012, and that the proceeds will be expended with due diligence on the qualified project. The IRS further stated that an extension request should not include an inquiry relating to deviations from information submitted in an original application. A separate process for addressing such deviations was previously announced by the IRS in Notice 2009-51.

For extension requests submitted in accordance with the Announcement, the IRS expects to confirm the extensions by December 31, 2011. If an applicant is granted an extension and the TEDBs are not issued by March 31, 2012, any unused part of the allocation will be treated as forfeited. Any amounts treated as forfeited may be available for reallocation by the IRS at a future date.

Proposed Reallocation Process

The Announcement also proposes and solicits comments from tribes and other interested members of the public on certain changes (described as “improvements”) to the application process for Volume Cap allocations. The changes are summarized below.

1. Project Cost. The IRS may require that applicants provide information on the costs of a proposed project and how the estimated cost was determined.
2. Plan for Financing. The IRS may require that applicants provide certain additional information with respect to their proposed plans of financing, including the following: (a) the expected schedule for spending the proceeds of the proposed financing, taking into account required permits, engineering studies, architectural plans, etc.; (b) a requirement that applicants state whether the proposed TEDBs are marketable, taking into account the type and location of the project, the creditworthiness of the applicant and other considerations; and (c) whether the applicant can obtain financing from other

sources if required for project costs.

3. Evidence of Readiness to Issue. The IRS may require that applicants demonstrate an ability to use the allocation prior to the forfeiture deadline, including information related to project readiness, marketability of the TEDBs, availability of other required financing, and a demonstration that the proposed TEDBs will satisfy applicable tax law requirements (for example, through a discussion with or preliminary analysis from a recognized public finance attorney or firm). *The IRS seeks specific comments on what should constitute appropriate evidence of readiness and whether documentation should be required.*
4. Allocation Process. The IRS is considering a two-step allocation process. The first step would be to award written commitments in "the order of priority based on the application submission date and amount requested." Granting the actual allocation would be a second step and would occur a certain number of days prior to closing on the TEDB financing (eg, 60 days). *The IRS seeks specific comments on the number of days an allocation would be "locked in," and the maximum number of days that should be allowed from the date of the IRS commitment to the date of the actual allocation.*
5. Reduced Allocations. The IRS is considering awarding allocations in amounts less than requested if the total amount of Volume Cap requested exceeds what is available. Generally, a reduced allocation would not be awarded unless the applicant demonstrates that it has the additional financing resources to complete the project.

The IRS expects to hold multiple telephone consultations prior to the December 12 deadline for submitting comments. Following these consultations and consideration of comments received, the IRS expects to publish guidance on the new process.

Comments may be submitted by mail, hand delivery or electronically. All submissions will be available for public inspection and copying.

Questions to Consider in Providing Comments

Commenters may wish to consider several questions in commenting on the new reallocation process described in the Announcement, including the following:

(A) Are the current limitations of the TEDB allocation process successfully addressed by having the IRS require additional information from applicants on costs, financing plans and readiness? Specifically, how can marketability of an applicant's TEDBs be assessed or verified?

(B) The IRS is considering a requirement that reallocation applications include a certification that the applicant will make up for any financing shortfall if it receives an allocation in a reduced amount from what it requested. But how can such a certification be given without knowing the amount of the shortfall? Further, are the goals of the TEDB program successfully met where applicants are required to rely on *other* sources of financing in order to use TEDBs? Finally, can the TEDB program become more viable without altering the existing requirement that all requested TEDB allocations be reduced pro rata, if requested amounts exceed what's available?

(C) Current allocation guidelines impose a $30 million limit on any allocation,

regardless of the cost of a project. In light of the minimal use of the TEDB program to date, and various public comments suggesting that the $30 million limit might have impeded some potentially viable projects, does retaining this limit continue to serve an important purpose?

Forum for Further Discussion

Since issuing the Announcement, the IRS has scheduled two public telephone consultations to take comments. The telephone consultations can be accessed by dialing 1-888-285-4585, and then entering Participant Code 775860. Each call can accommodate 200 participants. The dates and times of the telephone consultations are:

- November 17, 2011, 10 – 11 a.m. (Eastern Time)
- December 7, 2011, 2 – 3 p.m. (Eastern Time)

Please call any of us if you have questions regarding the Announcement or would like us to assist in the preparation of comments.

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