

CITY COUNCIL AGENDA ITEM

CITY OF SHORELINE, WASHINGTON

AGENDA TITLE:	Post-Issuance Compliance Policies for Tax Exempt Bonds
DEPARTMENT:	Finance
PRESENTED BY:	Debbie Tarry, Finance Director

PROBLEM/ISSUE STATEMENT:

The Internal Revenue Service ("IRS") requires that organizations have written policies and procedures for ensuring that federal tax requirements applicable to any City tax-exempt bonds are met. The City has issued tax-exempt bonds as a result of the voter approved 2006 Park Bonds and for City Hall. The IRS may from time to time issue a compliance check questionnaire to governmental entities to inquire about these policies. Although the City has not received such a questionnaire, the City has issued tax-exempt bonds and should be in compliance with the IRS requirements.

The IRS specifically wants to insure that an entity has written policies that provide guidance in the following areas:

Investments and Arbitrage: Arbitrage occurs when unspent bond proceeds are invested and earns interest. Since City bonds are tax-exempt, the IRS limits the investment earnings that the City can earn on unspent bond proceeds to the rate of interest being paid on the bonds. Any interest earned in excess to the interest cost of the bonds has to be remitted to the IRS, which is called arbitrage rebate.

Use of Bond Proceeds: The City must have policies that require that all required documentation on expenditures related to the use of bond proceeds are kept until the bonds are completely paid off plus three years. This includes costs related to the acquisition, construction and/or renovation of property and includes documents such as purchase contracts, construction contracts, progress payment requests, invoices, cancelled checks, and payment of bond issuance costs.

Limits on Private Business Use: The IRS has strict guidelines on the amount of private use for facilities built with tax-exempt bonds. Records must be kept to demonstrate any private use and compliance by the City.

Providing Education on Tax Requirements: The IRS wants to assure that appropriate training/education is provided to the appropriate officials and personnel on the federal tax requirements for tax-exempt bonds.

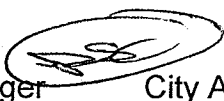
FINANCIAL IMPACT:

There is not direct financial impact in adopting these policies. Failure to comply with policies could revoke the tax-exempt status of bonds resulting in higher interest rates.

RECOMMENDATION

Staff recommends that Council adopt Resolution 308 and the attached policies on post-issuance tax compliance for tax-exempt bonds.

Approved By:

City Manager 

City Attorney 

Attachments:

Resolution No. 308

FIN 051

RESOLUTION NO. 308

A RESOLUTION OF THE CITY COUNCIL, CITY OF SHORELINE, WASHINGTON, ADOPTING POST-ISSUANCE TAX COMPLIANCE POLICIES FOR TAX-EXEMPT BONDS IN ACCORDANCE WITH REQUIREMENTS OF THE INTERNAL REVENUE SERVICE ("IRS").

WHEREAS, The IRS requires that issuers of tax-exempt bonds have written policies and procedures for ensuring that federal tax requirements applicable to their tax-exempt bonds are met; and,

WHEREAS, The IRS plans to issue an IRS Compliance Check Questionnaire to governmental entities to inquire whether the entity has written policies and procedures in place to help ensure proper and timely use of bond proceeds and compliance with arbitrage yield restriction and rebate requirements, including the identification of which official or officials of the issuer is primarily responsible for monitoring post-issuance compliance; now therefore

THE CITY COUNCIL OF THE CITY OF SHORELINE, WASHINGTON, HEREBY RESOLVES:

That the Shoreline City Council adopts Post-Issuance Tax Compliance Policies for Tax Exempt Bonds as detailed in Policy and Procedure FIN 05-1 attached hereto.

ADOPTED BY THE CITY COUNCIL ON OCTOBER 25, 2010.

Keith A. McGlashan, Mayor

ATTEST:

Scott Passey, City Clerk

Shoreline Policy and Procedure

FIN051 – POST-ISSUANCE COMPLIANCE POLICIES AND PROCEDURES FOR TAX-EXEMPT BONDS

Subject: POST-ISSUANCE COMPLIANCE POLICIES AND PROCEDURES FOR TAX- EXEMPT BONDS	Authority: Resolution 308
Effective Date:	Approved By:
Prior Versions and Related Policies: None	

1.0 PURPOSE

The purpose of these post-issuance compliance policies and procedures (“Compliance Policy”) for tax-exempt bonds issued by the City of Shoreline (the “City”) is to ensure that the City will be in compliance with requirements if the Internal Revenue Code of 1986, and amended (the “Code”), that must be satisfied with respect to tax-exempt bonds and other obligations (“bonds”) after the bonds are issued so that interest on the bonds will be and remain tax-exempt.

2.0 DEPARTMENTS AFFECTED

The Shoreline City Council has the overall, final responsibility for monitoring whether the City is in compliance with post-issuance federal tax requirements for the City’s tax-exempt bonds. However, the Shoreline City Council assigns the City Manager or his/her designee the primary operating responsibility to monitor the City’s compliance with post-issuance federal tax requirements for the City’s tax-exempt bonds.

3.0 POLICY

3.1 Arbitrage Yield Restriction and Rebate Requirements. The City Manager shall maintain or cause to be maintained records of:

- A. Purchases and sales of investments made with bond proceeds (including amounts treated as “gross proceeds” of bonds under section 148 of the Code) and receipts of earnings on those investments;
- B. Expenditures made with bond proceeds (including investment earnings on bond proceeds) for the governmental purposes of the bonds, such as for the costs of purchasing, constructing and/or renovating property and facilities;

- C. Information showing, where applicable for a particular calendar year, that the City was eligible to be treated as a "small city" in respect of bonds issued in that calendar year because the City did not reasonably expect to issue more than \$5,000,000 of tax-exempt bonds in that calendar year;
- D. Calculations that will be sufficient to demonstrate to the Internal Revenue Service ("IRS") upon an audit of a bond issue that, where applicable, the City has complied with an available spending exception to the arbitrage rebate requirement in respect of that bond issue;
- E. Calculations that will be sufficient to demonstrate to the IRS upon an audit of a bond issue for which no exception to the arbitrage rebate requirement was applicable, that the rebate amount, if any, that was payable to the United States of America in respect of investments made with gross proceeds of that bond issue was calculated and timely paid with Form 8038-T timely filed with the IRS; and
- F. Information and records showing that investment held in yield-restricted advance refunding of defeasance escrows for bonds, and investments made with unspent bond proceeds after the expiration of the applicable temporary period, were not invested in higher-yielding investments.

3.2 Restrictions on Private Business Use and Private Loans. The City Manager shall adopt procedures that educate and inform the principal operating officials of City departments (the "users") for which land, buildings, facilities and equipment ("property") are financed with proceeds of tax-exempt bonds about the restrictions on private business use that apply to that property after the bonds have been issued, and of the restriction on the use of proceeds of tax-exempt bonds to make or finance any loan to any person other than a state or local government unit.

In particular, following the issuance of bonds for the financing of property, the City Manager shall provide to the users of the property a copy of this Compliance Policy and other appropriate written guidance advising that:

- A. "Private business use" means use by any person other than a state or local government unit, including business corporations, partnerships, limited liability companies, associations, nonprofit corporations, natural persons engaged in trade or business activity, and *the United States of America and any federal agency*, as a result of ownership of the property or use of the property under a lease, management or service contract (except of certain "qualified" research contracts), "naming rights" contract, "public-private partnership" arrangement, or any similar use arrangement that provides special legal entitlements for the use of the bond-financed property;
- B. Under section 141 of the Code, no more than 10% of the proceeds of any tax-exempt bond issue (including the property financed with the bonds) may be used for private business use, of which no more than 5% of the proceeds of the

tax-exempt bond issue (including the property financed with the bonds) may be used for any "unrelated" private business use – that is, generally, a private business use that is not functionally related to the governmental purposes of the bonds; and no more than *the lesser* of \$5,000,000 or 5% of the proceeds of a tax-exempt bond issue may be used to make or finance a loan to any person other than a state or local government unit;

- C. Before entering into any special use arrangement with a nongovernmental person that involves the use of bond-financed property, the user must consult with the City Manager, provide the City Manager with a description of the proposed nongovernmental use arrangement, and determine whether that use arrangement, if put into effect, will be consistent with the restrictions on private business use of the bond-financed property;
- D. In connection with the evaluation of any proposed nongovernmental use arrangement, the City Manager should consult with nationally recognized bond counsel to the City as may be necessary to obtain federal tax advice on whether that use arrangement, if put into effect, will be consistent with the restrictions on private business use of the bond-financed property, and, if not, whether any "remedial action" permitted under section 141 of the Code may be taken by the City as a means of enabling that use arrangement to be put into effect without adversely affecting the tax-exempt status of the bonds that financed the property; and
- E. The City Manager and the user of the property shall maintain records of such nongovernmental uses, if any, of bond-financed property, including copies of the pertinent leases, contracts or other documentation, and the related determination that those nongovernmental uses are not inconsistent with the tax-exempt status of the bonds that financed the property.

3.3 Records to be Maintained for Tax-Exempt Bonds. It is the policy of the City that, unless otherwise permitted by future IRS regulations or other guidance, written records (which may be in electronic form) will be maintained with respect to each bond issue for as long as those bonds remain outstanding, plus three years. For this purpose, the bonds include refunding bonds that refund the original bonds and thereby refinance the property that was financed by the original bonds.

The records maintained are to include:

- A. The official Transcript of Proceedings for the original issuance of the bonds;
- B. Records showing how the bond proceeds were invested, as described in 3.1(A) above;
- C. Records showing how the bond proceeds were spent, as described in 3.1(B) above, including purchase contracts, construction contracts, progress payment requests, invoices, cancelled checks, payment of bond issuance costs, and

records of “allocations” of bond proceeds to make reimbursement for project expenditures made before the bonds were actually issued;

- D. Information, records and calculations showing that, with respect to each bond issue, the City was eligible for the “small issue” exception or one of the spending exceptions to the arbitrage rebate requirement or, if not, that the rebate amount, if any, that was payable to the United States of America in respect of investments made with gross proceeds of that bond issue was calculated and timely paid with Form 8038-T timely filed with the IRS, as described in 3.1(C) (D) and (E) above; and
- E. Records showing that special use arrangements, if any, affecting bond-financed property made by the City with nongovernmental persons, if any, are consistent with applicable restrictions on private business use of property financed with proceeds of tax-exempt bonds and restrictions on the use of proceeds of tax-exempt bonds to make or finance loans to any person other than a state or local government unit, as described in 3.2 above.

The basic purpose of the foregoing record retention policy for the City’s tax-exempt bonds is to enable the City to readily demonstrate to the IRS upon an audit of any tax-exempt bond issue that the City has fully complied with all federal tax requirements that must be satisfied after the date of the bonds so that interest on those bonds continues to be tax-exempt under section 103 of the Code.

3.4 Education Policy With Respect to Federal Tax Requirements for Tax-Exempt Bonds.

It is the policy of the City that the finance staff, as well as the principal operating officials of those departments of the City for which property is financed with proceeds of tax-exempt bonds should be provided with education and training on federal tax requirements applicable to tax-exempt bonds. The City recognizes that such education and training is vital as a means of helping to ensure that the City remains in compliance with those federal tax requirements in respect of its bonds. The City therefore will enable and encourage those personnel to attend and participate in educational and training programs offered by, among others, the Washington Municipal Treasurers Association and the Washington Finance Officers Association with regard to the federal tax requirements applicable to tax-exempt bonds.

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