Internal Revenue Service

Department of the Treasury

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LEGEND

Authority =
Borrower =
Project Issue =
State =

$a =
$b =
$c =
$d =
$e =
$f =

g percent =
h percent =
i percent =

Bank =

Dear :

This responds to your request for a ruling that the bonds of the Project Issue will not be issued earlier than necessary for purposes of § 1.148-10(a)(4) of the Income Tax Regulations.

FACTS

The Borrower is a State not-for-profit corporation which the Internal Revenue Service has determined to be exempt from Federal income tax pursuant to § 501(a) of the Internal Revenue Code as a charitable organization described in § 501(c)(3).

The Borrower plans to construct a new continuing care retirement community (the "Project"). Due to market conditions, the Borrower will construct the Project in five phases rather than constructing the entire Project at this time. According to this plan, when the Borrower completes a phase and that phase is substantially sold or leased, the Borrower will begin construction of the next phase of the Project. If all five phases of the Project are built, the construction period is expected to be approximately five years.

The Authority plans to issue the Project Issue to the Bank in the aggregate amount of $a and loan the proceeds to the Borrower in order for the Borrower to finance the costs of constructing the Project. The Authority will receive proceeds of the Project Issue from the Bank on multiple dates when the Borrower requests that a portion of $a be advanced to it. Advances are expected to be made over the five-year construction period in the following amounts: $b for Phase I; $c for Phase II; $d for Phase III; $e for Phase IV; and $f for Phase V. Pursuant to instructions from the Authority, the Bank will make advances directly to the Borrower.

For the Bank to make an advance on the Project Issue, the Borrower will be required to submit a written request accompanied by invoices for completed construction work on a Project phase. The Borrower will submit requests for an advance when a particular phase of the Project is at or near completion. On the day that the Borrower receives the advance, the Borrower will be required to apply that advance to pay the construction costs reflected in the request.

Interest will begin to accrue on the unpaid balance of each advance on the date that the advance is made. A formula for determining the interest rate for each advance will be established on or before any advances of the Project Issue proceeds are made. The formula will provide that the interest rate will be g percent of the Bank's then-current prime rate of interest, but, in no event, will the interest rate be less than h percent or greater than i percent.

LAW AND ANALYSIS

Generally, § 1.150-1(c)(1) provides, in part, that the term "issue" means two or more bonds that are sold at substantially the same time, are sold pursuant to the same plan of financing, and are reasonably expected to be paid from substantially the same source of funds, determined without regard to guarantees from parties unrelated to the obligor. Generally, under § 1.150-1(b), the issue date of an issue is the first date on which the issuer receives the purchase price in exchange for delivery of the evidence of indebtedness representing any bond included in the issue. Under § 1.150-1(b), the issue date of a bond is the date on which the issuer receives the purchase price in exchange for that bond. In no event is the issue date earlier than the first day on which interest begins to accrue on the bond or bonds for Federal income tax purposes.

Section 1.150-1(c)(4)(i) sets forth a special rule where the issue of bonds is a draw-down loan. Under § 1.150-1(c)(4)(i), bonds issued pursuant to a draw-down loan are treated as part of a single issue. In addition, § 1.150-1(c)(4)(i) provides that the issue date of the issue is the first date on which the aggregate draws under the loan exceed the lesser of $50,000 or 5 percent of the issue price. There is no special rule for the issue date of bonds issued pursuant to a draw-down loan.

Section 1.148-10(a)(1) provides, in part, that bonds of an issue are arbitrage bonds under § 148 if an abusive arbitrage device under § 1.148-10(a)(2) is used in connection with the issue. Except as described in § 1.148-10(c) with respect to advance refunding issues, any action that is expressly permitted by § 148 or §§ 1.148-1 through 1.148-11 is not an abusive arbitrage device. Under § 1.148-10(a)(2), any action is an abusive arbitrage device if the action has the effect of (i) enabling the issuer to exploit the difference between tax-exempt and taxable interest rates to obtain a material financial advantage; and (ii) overburdening the tax-exempt bond market. Under § 1.148-10(a)(4), an action overburdens the tax-exempt bond market under § 1.148-10(a)(2)(ii) if it results in issuing more bonds, issuing bonds earlier, or allowing bonds to remain outstanding longer than is otherwise reasonably necessary to accomplish the governmental purposes of the bonds, based on all the facts and circumstances. One factor evidencing an early issuance is the issuance of bonds that do not qualify for a temporary period under § 1.148-2(e)(2), (e)(3), or (e)(4).

The Project Issue will be a draw-down loan subject to § 1.150-1(c)(4)(i). Although the issue date of the Project Issue under § 1.150-1(c)(4)(i) is the first date on which the Borrower's aggregate draws exceed the lesser of $50,000 or 5 percent of the issue price, interest will not begin to accrue on the $a aggregate amount of the Project Issue on that date. Instead, interest will begin to accrue only on the date that the Bank makes an advance for the Authority and only on that portion of the aggregate amount of $a that the Bank actually advances pursuant to the Borrower's request. Because § 1.150-1(b) provides that no bond can be issued earlier than the first day on which interest begins to accrue on the bond for Federal income tax purposes, we conclude that each advance actually made by the Bank for the Authority should be treated as a bond of the Project Issue, the issue date of which is the date on which the Bank actually makes the advance to the Borrower.

We next consider whether, based on all facts and circumstances, the Project Issue will be issued earlier than otherwise reasonably necessary for purposes of § 1.148-10(a)(4). As noted above, each advance made should be treated as a bond of the Project Issue, the issue date of which is the date that the advance is actually made. On the date of the advance, the Borrower will be required to apply proceeds of each bond within the Project Issue to construction expenditures. Under these circumstances, we conclude that the Project Issue will not be issued earlier than necessary for purposes of § 1.148-10(a)(4).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax treatment of the transaction involved herein under the provisions of any other section of the Code and regulations that may be applicable that is not specifically covered by the above, including, but not limited to, any issues under § 1.150-2 and § 265(b).

This ruling is directed only to the taxpayer(s) requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,
Assistant Chief Counsel (Exempt Organizations/Employment Tax/ Government Entities)
By: Timothy L. Jones
Assistant Branch Chief
Tax Exempt Bonds Branch

Enclosure (1)