

Airports Council International - North America
American Public Power Association
Council of Infrastructure Financing Authorities
Education Finance Council
Government Finance Officers Association
Large Public Power Council
National Association of Counties
National Association of Higher Educational Facilities Authorities
National Association of Local Housing Finance Agencies
National Association of State Auditors Comptrollers and Treasurers
National Association of State Treasurers
National Council of Health Facilities Finance Authorities
National Council of State Housing Agencies
National League of Cities
US Conference of Mayors

March 1, 2005

The Honorable Charles Grassley
Chairman
Committee on Finance
United States Senate
Washington, DC 20510

The Honorable Max Baucus
Ranking Member
Committee on Finance
United States Senate
Washington, DC 20510

Dear Chairman Grassley and Ranking Member Baucus:

The organizations listed above that are members of the Public Finance Network, appreciate the opportunity to comment on the Joint Committee on Taxation's (JCT) report, *Options to Improve Tax Compliance and Reform Expenditures* released on January 27, 2005. Specifically, our broad coalition of groups represent local and state governmental entities and other issuers of tax-exempt bonds. Our members provide public services, and issue tax-exempt bonds to finance essential public and non-profit infrastructure.

This coalition is extremely concerned about the provisions in the report pertaining to tax-exempt financing and the adverse impact these provisions would have on the cities, counties, states, universities, public power facilities, and health care institutions that provide infrastructure and services to our citizens. We urge you to note that the proposals contained in the Joint Committee on Taxation's report increase federal tax revenues at the expense of local and state governments but do nothing to fix any problems that currently exist in the marketplace or relieve state and local governments of the significant costs and regulatory burdens associated with issuing tax-exempt bonds.

Tax-exempt bonds permit small and large communities alike to provide everything from sidewalks to sewers, roads to drinking water, and hospitals to classrooms for our citizens. We believe that efforts to constrain our ability to issue tax-exempt bonds or reduce their value to investors should be avoided by Congress, and that Congress should work to alleviate many constraints hindering the ability to issue bonds in an administratively and fiscally efficient manner.

If the proposals contained in the report were to become effective, governments would face significantly higher borrowing costs for infrastructure and capital improvements during a time of revenue shortfalls and strict budgetary constraints that already limit their ability to adequately meet pressing needs. To protect the viability of tax-exempt bonds as sound, long-term financing vehicles, we ask that you consider the negative effect these proposals would have on local and state governmental entities and the municipal marketplace. We also ask that you provide needed and long-sought relief to assist communities across America.

Below, we have highlighted our concerns with several of the proposals set forth in the report.

1. Eliminate Advance Refunding of Governmental Bonds and 501(c)(3) Bonds.

Substantial restrictions limiting the ability to issue and manage debt already exist. Taking away a tax-exempt issuer's sole advance refunding opportunity would be a severe blow to local and state governments that are struggling to provide essential services to their citizens in the face of ever increasing non-discretionary costs, such as Medicaid, pension costs and debt service.

Since 1986, local and state governments have only been allowed to advance refund their debt once during the lifetime of the bonds – usually 30 years. This restriction has handcuffed local and state governments ability to capitalize on favorable interest rates, and refinance their debt to lower their costs. Lowering debt service payments allows governmental entities to save money on their debt, and have more funds available to pay for essential government services. Especially throughout the past 4-5 years, we have heard an outcry from local and state governments that had already used their single advance refunding opportunities in the 1990s and were thus unable to take advantage of the even lower interest rates that were prevalent in 2001-2003. We have been calling on Congress to provide governmental entities with an additional advance refunding (108th Congress, S. 271) and believe this would greatly assist communities across the nation.

An example of the savings available to local and state governments through advance refundings, is the recent Liberty Zone legislation that afforded New York City the ability to have an additional advance refunding of its outstanding debt. To date, approximately \$4.3 Billion has been refunded, saving New York City \$345 Million.

2. Amend Information Reporting Requirements to Include Tax-Exempt Debt. Requiring local and state governments to track and issue reports to those businesses and individuals who invest in tax-exempt bonds will be onerous, time-consuming, and very costly to local and state governments. In many instances, it would not be possible. Local and state governmental entities do not have the internal structures in place to implement such a system, or the data to administer such a program. Unlike the private sector, many governmental entities do not have a specific debt management/investor relations office. Especially for local governments, the finance office, which handles all finance issues for an entity, is responsible for the debt management of the entity in addition to other responsibilities, including budgeting, cash management, accounting, and pension fund administration. Placing this additional burden on governmental entities should not be pursued, as it produces no cost savings for the federal government, while imposing a tremendous cost and administrative burden on local and state governmental entities. Additionally, this provision does not help with enforcement concerns because the IRS rarely goes after bondholders and can already retrieve bondholder information by using a John Doe Summons.

As the AMT is mentioned in the proposal under this section, we would also ask that Congress address the global problems associated with the AMT. As noted in the report, current law indirectly makes tax-exempt bonds taxable for certain individuals and corporations. We believe that this erodes the very essence of tax-exempt bonds, will increase interest rates, and limits state and local governments ability to meeting their congressionally-established purposes.

3. Disallow Deduction for Interest on Indebtedness Allocable to Tax-Exempt Obligations and Disallow Deduction for Interest on Debt Allocable to Tax-Exempt Income of Insurance Companies. We strongly oppose extending the pro rata disallowance of tax-exempt interest expense to all corporations and insurance companies. This provision would significantly decrease demand for tax-exempt bonds and increase state and local borrowing and lease financing costs for equipment, infrastructure and other capital facilities. According to data from the Federal Reserve Board, approximately one-third of bondholders would be impacted by this provision.

Already, corporations, banking institutions and insurance companies have a number of limitations placed on them that impair the attractiveness of purchasing tax-exempt bonds. This includes the application of AMT to tax-exempt interest, denying bank interest deduction for most municipal securities, and a reduction in deductible loss reserves for P&C insurers that purchase municipal securities. These provisions already reduce demand and drive up interest rates. To place additional restrictions on the municipal securities marketplace would cause those entities that purchase tax-exempt bonds to seek other investment products, which would ultimately increase the costs of issuing bonds, and negatively impact the budgets of governmental entities across the country.

We also believe that Congress should not implement other proposals included in the JCT report that would disrupt tax-exempt bond financing programs, including those that would impact legitimate pooled bond financings and the provision that would make it more difficult for state and local governments to meet their housing needs for low-income families by altering the mortgage revenue bonds program.

We would appreciate discussing these issues with you further. Additionally, we would like to present to you and your staff other proposals pertaining to tax-exempt bonds that should be included in any tax simplification and tax reform measures.

Sincerely,

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