

## Treasury/IRS Provide Early Holiday Present: Final “Issue Price” Regulations Released

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After two sets of proposed regulations, Treasury and IRS have now released final regulations on the definition of “issue price” for purposes of arbitrage investment restrictions that apply to tax-advantaged bonds (the “Final Regulations”) and it appears that the third time’s the charm. Practitioners are particularly praising the addition of a special rule for determining issue price for competitive sales and clarification on determining issue price for private placements. The Final Regulations were published in the Federal Register on December 9, 2016.

Several years ago, tax regulators became concerned that the longstanding practice of allowing an issue price to be calculated based on reasonable expectations could lead to abuse in that “reasonably expected” issue prices for bonds sometimes differed from the prices at which bonds were actually being sold to retail investors. A determination by the IRS that the “issue price” has been erroneously calculated can have ramifications for the calculation of arbitrage yield that could ultimately cause loss of tax-advantaged status. A clear and predictable definition of issue price is therefore essential for the tax-advantaged bond community.

After the first set of proposed regulations, published in the Federal Register on September 16, 2013, caused an uproar in the bond counsel community as being largely unworkable, they were withdrawn and re-proposed on June 24, 2015 (the “2015 Proposed Regulations”). The 2015 Proposed

Regulations were subject to a comment period followed by a public hearing. These Final Regulations build on the 2015 Proposed Regulations with certain changes in response to the public comments.

The Final Regulations look to actual facts as the general rule for determining issue price. Generally, the issue price of bonds is the first price at which a substantial amount (at least 10%) of the bonds is sold to the public. For bonds issued in a private placement to a single buyer, the Final Regulations clarify that the issue price of the bonds is the price paid by that buyer.

In recognition of the need in the tax-advantaged bond community for certainty as of the sale date (particularly in the case of advance refundings), the Final Regulations offer a special rule in the event a substantial amount of bonds has not been sold to the public as of the sale date. The special rule allows reliance on the initial offering price to the public if certain conditions are satisfied including evidence that the bonds were actually offered at the initial offering price and the written agreement of each underwriter that it will not offer or sell the bonds to any person at a price higher than the initial offering price during the period starting on the sale date and ending on the earlier of (i) the close of the 5<sup>th</sup> business day after the sale date, or (ii) the date on which the underwriters have sold at least 10% of the bonds to the public at a price that is no higher than the initial offering price.

Procedures for satisfying the conditions for use of this special rule will have to be developed but it is reasonable to expect that changes will need to be made to bond purchase agreements and underwriter selling agreements to comply with these requirements.



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The special rule for competitive sales provides that in a competitive sale meeting certain requirements, an issuer may treat the reasonably expected initial offering price to the public as of the sale date as the issue price if the winning bidder certifies that its winning bid was based on this reasonably expected initial offering price as of the sale date. This special issue price rule for competitive sales has been repeatedly requested by practitioners and is a welcome improvement over the prior proposed regulations which treated both negotiated sales and competitive sales in the same manner.

The Final Regulations will be effective for obligations that are sold on or after June 7, 2017 and there is no option to rely upon the Final Regulations with respect to obligations that are sold prior to that date. This delayed effective date should allow bond counsel and underwriters time to develop effective and hopefully uniform procedures and documentation to implement the new regulations.

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