

Recovery Zone Facility Bonds

March 19, 2010

Recovery Zone Facility Bonds (“RZFBs,” for short) are a new category of tax exempt bonds created by Congress in the American Recovery and Reinvestment Act of 2009 (“ARRA”). Essentially, RZFBs expand the use of traditional tax exempt private activity bonds (also known as “industrial revenue” or “industrial development” bonds) to “recovery zone property,” which is defined as depreciable property first used in a designated “recovery zone” by the borrower, in the active conduct of a “qualified business,” and which constructed, reconstructed, renovated or acquired by the taxpayer after the date on which the recovery zone was designated. Heretofore, the use of tax exempt private activity bonds has generally been limited to manufacturing and certain kinds of energy facilities, and 501(c)(3) entities. The highlights of RZFBs are as follows:

- A “recovery zone” is an area characterized by significant poverty, unemployment, rate of home foreclosures or general distress, OR which is economically distressed because of military base foreclosure or realignment.
- A “qualified business” means any business other than residential rental property, commercial golf courses, country clubs, massage parlors, hot tub, suntan, racetrack, gambling facilities, or a business that sells drinks off premises.
- ARRA allocates issuing authority on a state by state basis. Maine’s allocation is \$135 million. ARRA further directs each state to sub-allocate its allocation to counties and municipalities with a population of 100,000 or more, of which Maine has none. Accordingly, Maine’s \$135 million was allocated by ARRA to the counties. Cumberland County’s allocation is \$39,174,000; York’s is \$20,855,000, and Androscoggin’s is \$22,305,000.
- Any county may waive its allocation. Waived allocations revert to the State, which may “reallocate the waived volume cap in any reasonable manner as it shall determine in good faith in its discretion.”
- RZFBs must be issued in 2010, unless Congress extends the program. Thus, Maine’s \$135 million allocation should be viewed as “use it or lose it.”

Although RZFBs have already received widespread use in other states, none have yet been issued in Maine, in large part because of uncertainties about the allocation system. In an effort to clarify the situation, the Finance Authority of Maine (“FAME”) and the Governor’s Office sought emergency legislation in the form of LD 1530, “An Act to Facilitate Recovery Zone Facility Bonds, Recovery Zone Economic Development Bonds and Qualified Energy Conservation Bonds,” which immediately reallocates Maine’s \$135 million to FAME, which is in turn required to reserve half of the allocation originally designated for the counties for projects identified prior to June 1, 2010, provided that county allocations not reserved for projects by that date shall be subject to reallocation by FAME. We are pleased to report that the Governor signed LD 1530 on Wednesday, March 17, 2010, and as an emergency bill the legislation is effective immediately. Among other things, the bill designates the entire State of Maine as a “recovery zone,” so projects anywhere in the State are eligible.

As with other tax exempt private activity bonds, RZFBs are conduit bonds, issued by either FAME or a county for the benefit of a private user. The bonds may be either variable or fixed rate, and even taking into account credit enhancement and other transaction costs, are a potentially attractive financing vehicle, particularly for substantial projects. The bonds may either be sold through an underwriter into a public market, or purchased directly by a lender in a private placement. One important caveat applies with respect to the direct purchase of RZFBs by financial institutions (e.g., in a private placement scenario): a financial institution may deduct 80% of the cost of purchasing and carrying

tax exempt bonds, but only to the extent that its tax exempt holdings do not exceed 2% of its assets.

If you wish to know more about RZFBs or any other bonds created by ARRA, please contact Paul Frinsko, Shana Cook Mueller or Phil Gleason in Bernstein Shur's Portland office at 207 774-1200.