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# **Urban Land Institute Infrastructure Summit 2009**

## **Recovery Zone Bonds – An Overview**

**May 29, 2009**



**RBC Capital Markets®**

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# Recovery Zone Bonds – An Overview

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- **The Act temporarily amended the IRS Code permitting State and local governments to issue:**
  - **Recovery Zone Economic Development Bonds:** a new category of taxable obligation, to finance qualified economic development purposes. Issuers will receive a direct subsidy from Treasury equal to 45% of the interest on the bonds
  - **Recovery Zone Facility Bonds:** a new tax-exempt private activity bonds, to finance certain depreciable property, including new or used equipment located in a designated recovery zone. General rules on private activity bonds still apply. Investors receive a tax credit in addition of interest on the bonds
- The Issuer must first designate the chosen area for the project as a Recovery Zone
- Federal Davis-Bacon prevailing wage rules will apply on the project
- **A “Recovery Zone” is defined as:**
  - Any area designated by the issuer as having significant poverty, unemployment, rate of home foreclosures, or general economic distress;
  - Any area designated by the issuer as economically distressed by reason of closure or realignment of a military installation pursuant to the Defence Base Closure and Realignment Act of 1990, and
  - Any area for which a designation as an empowerment zone or renewal community is in effect

**The time frame for issuance of Recovery Zone bonds is through January 1, 2011**

# Recovery Zone Bonds

## Structuring Requirements

	Recovery Zone Economic Development Bonds	Recovery Zone Facility Bonds
<b>Volume Cap</b>	\$10 billion	\$15 billion
<b>Eligible Expenditures</b>	<ul style="list-style-type: none"> <li>Public purpose governmental projects</li> <li>New money capital expenditures</li> <li>Public infrastructure promoting economic development in recovery zone</li> <li>Expenditures for job training and educational programs included</li> </ul>	<ul style="list-style-type: none"> <li>Privately activity projects which promote economic development in recovery zone (exempt facility bonds)</li> <li>Projects must be constructed, renovated or acquired after the area is designated a recovery zone</li> <li>Project must be for a depreciable property (e.g. buildings and equipment)</li> </ul>
<b>Bond Structure</b>	<ul style="list-style-type: none"> <li>Bonds are issued with a “taxable” rate.</li> <li>Issuer then receives a direct federal subsidy equal to 45% of the interest on the bonds</li> </ul>	<ul style="list-style-type: none"> <li>Bonds are issued with a “tax-exempt” type market rate</li> <li>Investors receives a tax credit equal to 45% of the interest on the bonds</li> <li>This tax credit can be stripped and sold as needed</li> </ul>
<b>Use of Proceeds Requirement</b>	<ul style="list-style-type: none"> <li>100% of project proceeds must be used for qualified economic development purpose in recovery zone</li> </ul>	<ul style="list-style-type: none"> <li>95% of project proceeds must be used for qualified economic development purposes in recovery zone</li> </ul>

# Recovery Zone Bonds – The Allocation Process

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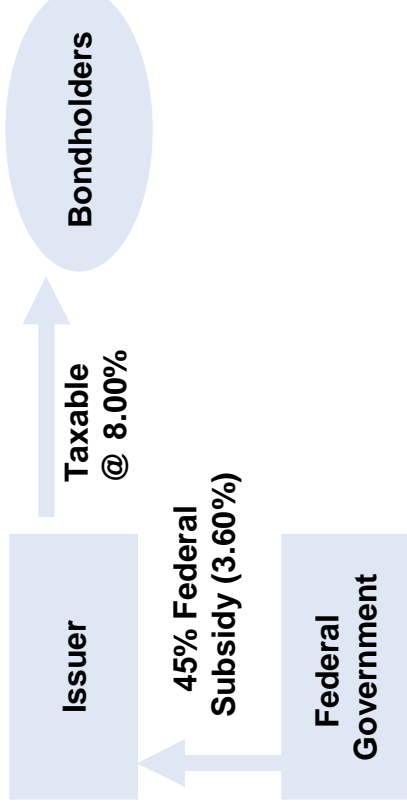
## The Treasury Secretary allocates Recovery Zone Bond issuance authority (volume cap) among States based on the proportion of the State's 2008 employment decline:

- December 2007 employment levels are compared to December 2008 employment levels for each State
- “2008 State Employment Decline” means the decline in the number of individuals employed in the State from December 2007 to December 2008
- Each State is required to reallocate its allocation among the counties and large municipalities (population of more than 100,000) in proportion to each county's or municipality's 2008 employment decline
  - When calculating county employment decline, the decline in any large municipality located in that county is ignored
- Allocation will be adjusted annually to ensure that no State receives less than 0.9% of the national limitation
- Once a sub-allocation is received from the State, the local government issuer would designate one or more areas as recovery zones, prior to the issuance of the recovery zone bonds

# Recovery Zone Economic Development Bonds

## Federal Subsidy Option

- Tax-Exempt Purposes
- New capital expenditures which promote economic development in the recovery zone
- Reserve Fund
- 2% limit on Cost of Issuance
- Bonds must be priced at par or de minimis amount of premium



## Federal Subsidy Option

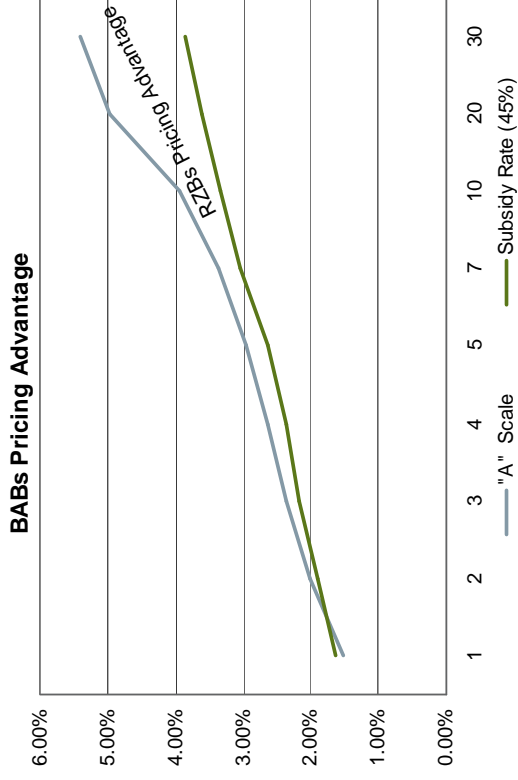
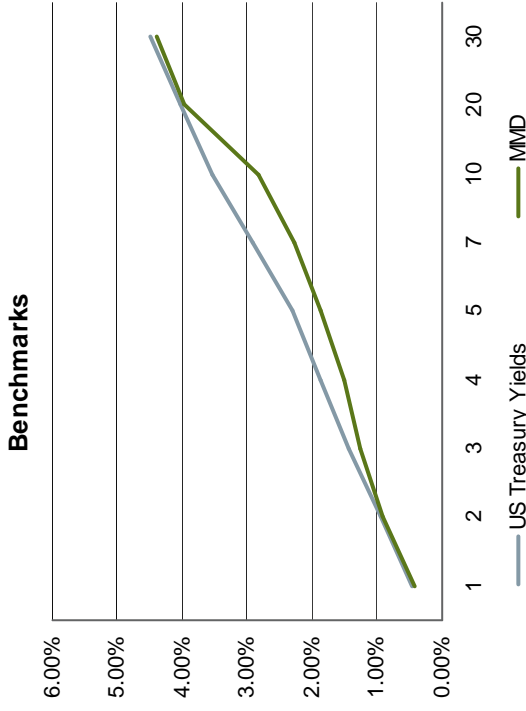
Tax Rate 8.00%

Federal Subsidy (3.60%)

**Effective Cost of Funds 4.40%**

# Recovery Zone Bonds – The Rate Advantage

- Taxable RZBs would be issued as non-callable or with a “make whole” call
- The taxable market also prefers bullet maturity structure in 5, 10, 20 and 30 year maturities
- In evaluating the cost advantage of the RZBs structure, you should compare it against non-callable tax-exempt bonds

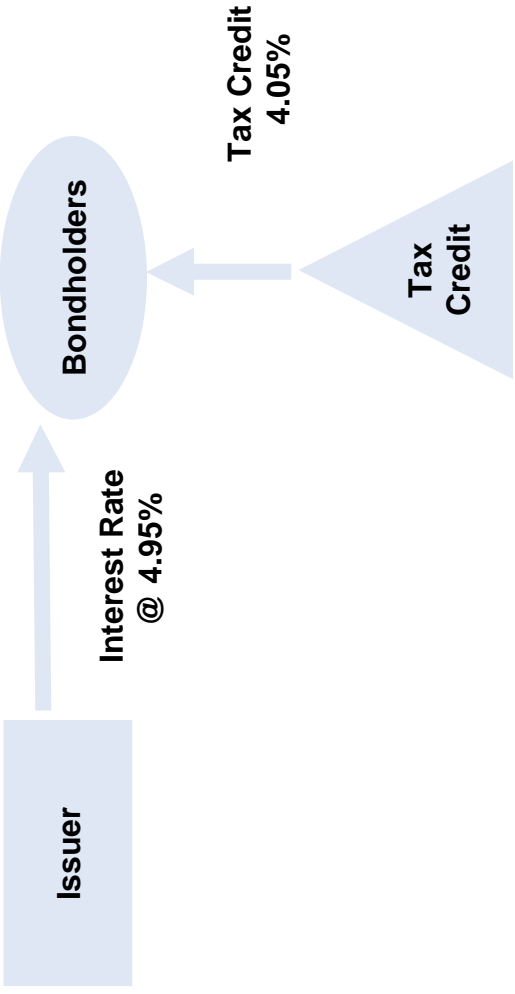


Year	Benchmarks		Tax-Exempt Rates Non-Callable		Taxable Rates Non-Callable		Federal Subsidy Rates	
	Treasury Yield	MMD	"A" Scale	Spread to MMD	Taxable Rates	Spread to Treasury	Subsidy Rate (45%)	Advantage
1	0.46%	0.42%	1.52%	1.10%	2.95%	2.00%	1.62%	-0.10%
2	0.95%	0.92%	2.02%	1.10%	3.45%	2.50%	1.90%	0.12%
3	1.46%	1.27%	2.37%	1.10%	3.96%	2.50%	2.18%	0.19%
4	1.88%	1.52%	2.62%	1.10%	4.30%	2.00%	2.37%	0.26%
5	2.30%	1.87%	2.97%	1.10%	4.80%	2.50%	2.64%	0.33%
7	2.93%	2.28%	3.38%	1.10%	5.55%	2.00%	3.05%	0.33%
10	3.55%	2.84%	3.94%	1.10%	6.05%	2.50%	3.33%	0.61%
20	4.02%	3.98%	4.98%	1.00%	6.55%	3.00%	3.60%	1.38%
30	4.49%	4.41%	5.41%	1.00%	6.99%	2.50%	3.84%	1.57%

Rates as of May 26, 2009

# Recovery Zone Facility Bonds

## Tax Credit Structure



- Private Activity purposes
- New Capital Expenditures Only
- Reserve Fund
- 2% limit on Cost of Issuance
- Bonds must be priced at par or de minimis amount of premium
- Tax credit received is equal to 45% of effective rate received
- Total effective rate received is subject to federal taxation
- Higher effective rate will reflect uncertainty around value of tax credit and secondary market for stripped tax credits

Tax Credit Structure	
Interest Rate	4.95%
Tax Credit Received	4.05%
<b>Effective Rate Received</b>	<b>9.00%</b>



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