Post-Issuance Tax Compliance Webinar IRS Schedule K Workshop

May 18, 2017

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Introduction

- What is Schedule K, and why is it required?
- Who must file?
- What information do you need to prepare the Schedule K reporting?
- How is Schedule K used by the IRS?

Schedule K – Page 1

SCHEDULE K
(Form 990)

Department of the Treasury
Internal Revenue Service

Supplemental Information on Tax-Exempt Bonds

► Complete if the organization answered "Yes" on Form 990, Part IV, line 24a. Provide descriptions, explanations, and any additional information in Part VI.
► Attach to Form 990.
► Information about Schedule K (Form 990) and its instructions is at *www.irs.gov/form990*.

OMB No. 1545-0047
2016
Open to Public Inspection

Name of the organization	Employer identification number

Part I Bond Issues

	(a) Issuer name	(b) Issuer EIN	(c) CUSIP #	(d) Date issued	(e) Issue price	(f) Description of purpose	(g) Defeased		(h) On behalf of issuer		(i) Pooled financing	
							Yes	No	Yes	No	Yes	No
A												
B												
C												
D												

Part II Proceeds

		A	B	C	D
1	Amount of bonds retired				
2	Amount of bonds legally defeased				
3	Total proceeds of issue				
4	Gross proceeds in reserve funds				
5	Capitalized interest from proceeds				
6	Proceeds in refunding escrows				
7	Issuance costs from proceeds				
8	Credit enhancement from proceeds				
9	Working capital expenditures from proceeds				
10	Capital expenditures from proceeds				
11	Other spent proceeds				
12	Other unspent proceeds				
13	Year of substantial completion				

		Yes	No	Yes	No	Yes	No	Yes	No
14	Were the bonds issued as part of a current refunding issue?								
15	Were the bonds issued as part of an advance refunding issue?								
16	Has the final allocation of proceeds been made?								
17	Does the organization maintain adequate books and records to support the final allocation of proceeds?								

Part III Private Business Use

		A		B		C		D	
		Yes	No	Yes	No	Yes	No	Yes	No
1	Was the organization a partner in a partnership, or a member of an LLC, which owned property financed by tax-exempt bonds?								
2	Are there any lease arrangements that may result in private business use of bond-financed property?								

For Paperwork Reduction Act Notice, see the Instructions for Form 990. Cat. No. 50193E **Schedule K (Form 990) 2016**

Part I – Bond Issues

- Purpose: List identifying information about each bond issue that was issued after 12/31/2002 and had $100,000+ outstanding
- Part I information should be copied from the Form 8038 filed in connection with the bond issue
- Common Errors:
  - Listing multiple CUSIPs for the same bond issue. Should list latest maturity only.
  - Multiple series of bonds treated as one issue for tax purposes should be listed as one issue on the Schedule K
  - Issues that have been refunded for tax purposes should use the information for the "reissued" bonds.
- (g): Check "Yes" if there was a partial defeasance. (e.g., partial advance refunding or defeasance escrow for remediation of PBU)
- (h): Should be checked "No"

Part II – Proceeds

- Purpose: Inform the IRS as to how bonds proceeds were used (e.g., new money)
- Common errors:
  - Don’t rely on Form 8038 information anymore! Report on **actual use** of proceeds.
  - Line 4: Gross Proceeds
  - Lines 3, 5-12: Proceeds = Sale Proceeds + investment earnings
  - Line 9: most likely blank
  - Refunding Proceeds: Line 6, then Line 11
  - Line 16: Don’t‘ rush to check “Yes”

Part III – Private Business Use

- Purpose: Inform the IRS of any potential or existing private business use
- Looks at a one-year snapshot

Private Business Use – Overview

- Federal tax law restricts amount of private use to 5% of a bond issue
- "Private Use" is use of bond-financed assets in a trade or business of a nongovernmental and non-501(c)(3) person
  - Nongovernmental entities include conventional for-profit businesses and the federal government.
- Private use limits are average annual limits
- Five percent limit includes any amounts used to pay "Costs of Issuance" – up to 2% of the bond proceeds

Private Business Use - Examples

- Sale or Transfer to a non-501(c)(3) entity
- Use of a facility by a related, for-profit entity
- Leases with Third-Parties
  - Laundry Rooms
  - Bookstores
  - Use of Fitness Centers
  - Cell Tower

Private Business Use – Additional Examples

- Summer Camps & Conferences
  - Fields, classrooms, dorms
- Management Contracts (Rev. Proc. 2017-13)
  - Food Service
- Contracts for Exclusive Pouring Rights & Vending
- Research Agreements (Rev. Proc. 2007-47)

Part III – Private Business Use

- Common Errors:
  - Line 3a: Should check "Yes" if there is any management contract
  - Line 3c: Should check "Yes" if there is any research agreement
  - Line 4: Should list the average percentage for the year only.

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Part III Private Business Use *(Continued)*

		A		B		C		D	
		Yes	No	Yes	No	Yes	No	Yes	No
3a	Are there any management or service contracts that may result in private business use of bond-financed property?								
b	If "Yes" to line 3a, does the organization routinely engage bond counsel or other outside counsel to review any management or service contracts relating to the financed property?								
c	Are there any research agreements that may result in private business use of bond-financed property?								
d	If "Yes" to line 3c, does the organization routinely engage bond counsel or other outside counsel to review any research agreements relating to the financed property?								
4	Enter the percentage of financed property used in a private business use by entities other than a section 501(c)(3) organization or a state or local government . . . . ▶		%		%		%		%
5	Enter the percentage of financed property used in a private business use as a result of unrelated trade or business activity carried on by your organization, another section 501(c)(3) organization, or a state or local government . . . . ▶		%		%		%		%
6	Total of lines 4 and 5		%		%		%		%
7	Does the bond issue meet the private security or payment test?								
8a	Has there been a sale or disposition of any of the bond-financed property to a nongovernmental person other than a 501(c)(3) organization since the bonds were issued?								
b	If "Yes" to line 8a, enter the percentage of bond-financed property sold or disposed of		%		%		%		%
c	If "Yes" to line 8a, was any remedial action taken pursuant to Regulations sections 1.141-12 and 1.145-2?								
9	Has the organization established written procedures to ensure that all nonqualified bonds of the issue are remediated in accordance with the requirements under Regulations sections 1.141-12 and 1.145-2?								

Part IV Arbitrage

		A		B		C		D	
		Yes	No	Yes	No	Yes	No	Yes	No
1	Has the issuer filed Form 8038-T, Arbitrage Rebate, Yield Reduction and Penalty in Lieu of Arbitrage Rebate?								
2	If "No" to line 1, did the following apply?								
a	Rebate not due yet?								
b	Exception to rebate?								
c	No rebate due?								
	If "Yes" to line 2c, provide in Part VI the date the rebate computation was performed								
3	Is the bond issue a variable rate issue?								
4a	Has the organization or the governmental issuer entered into a qualified hedge with respect to the bond issue?								
b	Name of provider								
c	Term of hedge								
d	Was the hedge superintegrated?								
e	Was the hedge terminated?								

Arbitrage – Overview

- Rules are designed to limit the rate of return from investment of proceeds of a tax-exempt bond issue.
- Rules applied in two forms:
  - Yield Restriction (Can you earn it?)
  - Rebate (Can you keep it?)
- General Rule: Rebate payable <u>at least every 5 years</u>.
- CHEFA provides arbitrage rebate services for its borrowers.

Part IV - Arbitrage

- Purpose: Ensure limited rate of return from investment of proceeds of tax-exempt bond issue
- CHEFA can provide information for Lines 2a,b,c
  - If no rebate is due, check “Yes” to Line 2c.
- Common errors:
  - Line 4a should only be checked “Yes” if interest rate swap was identified as a qualified hedge.
  - Line 4d should most likely be checked “No.”

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Part IV **Arbitrage** *(Continued)*

		A		B		C		D	
		Yes	No	Yes	No	Yes	No	Yes	No
5a	Were gross proceeds invested in a guaranteed investment contract (GIC)?								
b	Name of provider								
c	Term of GIC								
d	Was the regulatory safe harbor for establishing the fair market value of the GIC satisfied?								
6	Were any gross proceeds invested beyond an available temporary period?								
7	Has the organization established written procedures to monitor the requirements of section 148?								

Part V **Procedures To Undertake Corrective Action**

	A		B		C		D	
	Yes	No	Yes	No	Yes	No	Yes	No
Has the organization established written procedures to ensure that violations of federal tax requirements are timely identified and corrected through the voluntary closing agreement program if self-remediation isn't available under applicable regulations?								

Part VI **Supplemental Information.** Provide additional information for responses to questions on Schedule K. See instructions

Part V – Procedures to Take Corrective Action

- Only check "Yes" if written procedures specifically require the institution to go to VCAP.
- VCAP: Voluntary Closing Agreement Program
  - Self-reporting an issue to the IRS.

Part VI – Supplemental Information

- Provide additional information on:
  - Purpose of Issue
  - Any private use over 5% (3%)
  - Any post-issuance compliance procedures that don't mandate VCAP
  - Other items as appropriate

Post-Issuance Compliance Procedures: Background

- Not a statutory or regulatory requirement, per se
- In recent years, IRS has strongly encouraged beneficiaries of tax-exempt bond issues to adopt procedures to ensure compliance with federal law requirements for tax-exempt bond financings.
- CHEFA **does require** each borrower to adopt its own procedures.

Post-Issuance Compliance Procedures: Why Should You Care?

- Helps to ensure that interest on your bonds remains tax-exempt
- Helps to ensure that you are in compliance with document covenants
- Enables “checking the box” on the Form 8038 filed in connection with closing
- A “plus factor” in an IRS audit

How to Develop Post-Issuance Compliance Procedures

- Review requirements contained in tax documents executed at closing (e.g., Tax Regulatory Agreement).
- Appoint one or two people to be in charge of the process:
  - Determine who at your institution is involved in review or execution of contracts with third-parties; and
  - Determine who at your institution has been involved in the tax-exempt bond financings.

How to Develop Procedures (cont'd)

- Educate department heads or other appropriate persons to identify arrangements that could result in potential private use.
- Document which facilities have been bond-financed. Should track final allocation of bond proceeds.
- Be mindful of existing exclusivity contracts and the effect they may have on future buildings to be bond-financed.
- Confirm expenditure of bond proceeds (including investment earnings) with Trustee or Bank.

Amending Schedule K

- File a new return, using the version of Form 990 applicable to the year being amended.
- Must provide all information, not just the new or corrected information.
- Check the "Amended return" box on page 1.
- Identify amended items in Schedule O and describe the amendments.
- Be certain to inform CHEFA of any amendments **prior** to filing the return.

Questions or Comments?

Please do not hesitate to contact:

- Michael F. Morris - Managing Director

  (860)761-8424 or mmorris@chefa.com

- Dan Kurowski - Arbitrage Rebate Specialist

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