

Recovery Zone Bonds: A Useful Financing Tool

The Recovery Zone Bond program was designed to provide tax incentives for economic development in the form of lower borrowing costs. Costs are lowered either through federal tax exemption for the interest on bonds issued or through “direct payments” of interest subsidies to the bond issuer. There are two types of Recovery Zone bonds: Economic Development and Facility Bonds.

Recovery Zone Economic Development Bonds (Public Financing)

Recovery Zone Economic Development Bonds (RZEDBs) is the ability to use the bonds for public infrastructure such as water, sewer, storm water, and street improvements. RZEDBs can also finance the construction of public facilities such as water or wastewater treatment plants and other public buildings.

Qualified Economic Development Purposes:

1. Capital expenditures paid or incurred with respect to property located in the Recovery Zone.
2. Expenditures for public infrastructure and construction of public facilities.
3. Job training and educational programs as they related to public utilities.

RZEDBs may not be issued to refinance expenditures in “refunding issues.” Generally, RZEDBs target capital expenditures and working capital expenditures to promote development or other economic activity.

The bond issuer receives an interest subsidy in the form of payments from the Internal Revenue Service (IRS).

The subsidy rate is 45 percent of the interest payments.

Recovery Zone Facility Bonds (Commercial Financing)

Recovery Zone Facility Bonds (RZFBs) create opportunity for private business to develop or expand through accessing lower cost financing. RZFBs are tax-exempt bonds and may be used to finance private activity projects within a designated Recovery Zone.

Qualified Economic Development Purposes:

1. Retail
2. Commercial
3. Office
4. Manufacturing
5. Entertainment
6. Warehouse Facilities
7. Mixed-use Properties

RZFB can be utilized to purchase existing property (building) but it must be substantially rehabilitated. RZFBs may also be used to purchase new construction, renovate existing facilities, or purchase new equipment.

Use of Funds:

Facility Bonds can be used for depreciable assets.

Terms:

Terms would be similar to standard banking terms including 5 to 10 years for equipment and up to 25 years for buildings.

Size of Bonds:

Utilizing bond financing makes sense when the project is able to recoup the fees associated with the bond issuance. Typically, bond financing is preferable on projects greater than \$250,000.

Benefits:

Private industry has access to tax-exempt financing. Typically, the interest rate on a tax-exempt issuance is 70 percent of a taxable issuance. For example:

Taxable Rate	8.0%
Non Taxable Rate	5.6%

The Bondholder (typically a bank) receives the benefit of the tax-exempt interest income. The Issuer (business) receives the benefit of lower interest rate while still deducting the interest expenses.

Dates to Note:

Recovery Zone Bonds must be allocated before January 1, 2011. There is pending federal legislation (HR 4849), however, that could extend the Recovery Zone deadline to January 1, 2012, as well as provide additional allocations.

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