



L Street =

Lease Revenue Bond Issuer =

Project =

State =

Year W =

Year X =

Year Y =

Dear :

This letter is in response to your request for a ruling that the Lease Revenue Bonds, as defined herein, will not satisfy the private loan financing test under section 141(c) of the Internal Revenue Code (the "Code"). A second private letter ruling concerning the Assessment Bonds, as defined herein, will be issued on the same date as this letter. To reach a conclusion with respect to the Lease Revenue Bonds, we must examine each element of the Project, including the various contractual arrangements, the parity in value of the consideration to be exchanged under those contracts, the bonds to be issued to finance the New Hall, and the sources of revenue that will pay debt service on those bonds, for evidence of private loan financing.

**Facts and Representations**

You make the following factual representations. The Lease Revenue Bond Issuer is an authority established pursuant to a joint powers agreement between the City and the county in which it is located (the "County"). The Assessment Bond Issuers are two

districts that will be formed by the City pursuant to certain provisions of State law. The Lease Revenue Bond Issuer was formed and the Assessment Bond Issuers will be formed to assist the City and the County with respect to financing and construction of convention and exhibition facilities located within the boundaries of the City. Both issuers are, or will be at the time of the issuance, qualified to issue tax-exempt bonds under section 103 of the Code.

Currently located in the immediate area of the improvements contemplated as part of the Project are the City's existing convention center, existing parking facilities, a stadium, and an entertainment complex. The convention center is owned by the City and consists of three interconnected buildings: Hall A, Hall B, and Hall C. The existing parking facilities are owned by the City and consist of, among others, a parking garage on K Street (the "Old K Street Garage"), a surface lot on L Street (the "L Street Lot"), and a parking garage beneath Hall C (the "Hall C Parking"). The stadium (the "Stadium") is owned by the Company, a private firm in the sports and entertainment business. The Company has leased the land on which the Stadium sits from the City for a nominal annual rent through Year Y (the "Stadium Lease"). The entertainment complex (the "Entertainment Complex") is also owned by the Company and includes theaters, bars, restaurants, a movie theater, and hotels.

In contemplation of the Project, the City and the Company have entered into a non-binding memorandum of understanding (the "MOU") to memorialize preliminary terms and provide a general framework for continued negotiations. The MOU contemplates construction of a new wing of the convention center (the "New Hall") to be owned by the City, construction on the site of Hall C of another stadium (the "Event Center") to be owned and operated by the Company, and replacement of the Old K Street Garage and the L Street Lot with two new parking garages (respectively, the "New K Street Garage" and the "New L Street Garage") to be owned by the Company. In connection with these improvements, the MOU provides that the City intends: (1) to lease to the Company the land on which the Event Center will be built (the "Event Center Lease"); (2) to lease to the Company the land on which the New K Street Garage and the New L Street Garage will be located (the "Parking Lease"); (3) to enter into an agreement that extends the term of the Stadium Lease to be coterminous with the Event Center Lease (the "Stadium Lease Extension Agreement"); and (4) to enter into an agreement that conveys to the Company certain rights to locate signage on the exterior of Hall A and the New Hall (the "Signage Agreement").

To finance construction of the New Hall, the City will cause two types of bonds to be issued. First, the Lease Revenue Bond Issuer will issue bonds with a term of b years in the principal amount of \$c (the "Lease Revenue Bonds"). The Lease Revenue Bonds will be secured by and payable from payments from the City, made from its general fund. Second, the Assessment Bond Issuers will issue bonds with a term of b years in the principal amount of \$d secured by and payable from assessments imposed on certain interests in property held by the Company (the "Assessment Bonds").

These and the other arrangements comprising the Project are set forth in more detail below.

### *Construction of the New Hall*

The City and the Company will enter into an agreement that will obligate the Company to build the New Hall. In exchange, the City will pay the Company an amount equal to the Company's costs in connection with building the New Hall, not to exceed an agreed upon cost ceiling. Through a competitive request-for-proposal process, the Company will select a general contractor that will agree to a guaranteed maximum price contract such that the contractor will bear the costs in connection with building the New Hall to the extent that those costs exceed the cost ceiling, unless the cost ceiling has been increased via a formal change order. The City will finance its payment obligations with the proceeds of the Lease Revenue Bonds and the Assessment Bonds (collectively, the "Bonds"). The proceeds of the Bonds will be spent on the construction of the New Hall which will be solely owned by the City. The Company will have no option to purchase any part of the New Hall at any price.

### *The Event Center Lease*

At its own expense, the Company will construct the Event Center on the site currently occupied by Hall C. The Event Center Lease will provide that the City lease this site to the Company for a term of e years. In exchange for the rights conveyed by the City, the Company will pay the City an annual rent beginning on the earliest of completion of the New Hall, commencement of demolition of Hall C, or a specified date in Year X.<sup>1</sup> The Company will also pay the cost of demolishing Hall C and the cost of defeasing bonds originally issued to finance the development of Hall C (the "Hall C Bonds").<sup>2</sup>

### *The Parking Lease*

To address the need for additional parking and to replace the Hall C Parking that will be eliminated when Hall C is demolished, the Company will, at its own expense, construct the New K Street Garage and the New L Street Garage on the sites currently occupied by the Old K Street Garage and L Street Lot, respectively. The Parking Lease will provide that the City lease these sites to the Company for a term of e years. In exchange for the rights conveyed by the City, the Company will bear certain costs of preparing the site for construction, such as the cost of demolishing the Old K Street

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<sup>1</sup> In addition, the Event Center Lease will also provide that, in connection with the largest events hosted at the convention center, the Company will permit the City to use the Event Center in exchange for a fee that will not exceed the fee imposed by the City on the event producer.

<sup>2</sup> Such amounts are treated as rent under the Event Center Lease for purposes of the "equivalence of value exchanged" discussion below. As further described in the discussion of the Lease Revenue Bonds below, the costs of defeasing the Hall C Bonds may be offset by an abatement of sales tax to the extent that the sales tax generated by the construction contemplated in the MOU exceeds the amount of sales tax needed to pay the debt service on the Lease Revenue Bonds.

Garage and L Street Lot, and will pay the City an annual rent beginning on the earliest of completion of the New K Street Garage and the New L Street Garage, demolition of Hall C, or a specified date in Year X. In addition, the City will have certain limited rights to use the New L Street Garage.<sup>3</sup> If the sum of projected additional parking revenue and projected additional parking tax (described below) to the City attributable to Event Center events will be less than the current net income to the City from the Hall C Parking, then the Company will give the City a one-time “make whole” payment to compensate for the shortfall (the “Parking Make Whole Provision”).

### *The Lease Revenue Bonds*

To partially fund construction of the New Hall, the Lease Revenue Bond Issuer will issue the Lease Revenue Bonds in approximately Year W. Under the terms of the Lease Revenue Bonds, the City will lease the site on which the New Hall will be built to the Lease Revenue Bond Issuer, and the Lease Revenue Bond Issuer will sublease the site and improvements back to the City. Under the terms of this sublease, the City will agree to make payments from its general fund sufficient to pay debt service on the Lease Revenue Bonds.

The City expects to derive new revenues attributable entirely to the Project that will be sufficient to pay the debt service on the Lease Revenue Bonds. It expects these new revenues to come from the following four sources: the Company’s rent payments under the Event Center Lease, the City’s share of the possessory interest taxes that will be levied pursuant to State law on the Company’s leasehold interests under the Event Center Lease and the Parking Lease, the parking tax currently levied on all fee-based parking in the City that will be generated by parking during events at the Event Center, and the City’s share of the sales tax generated by construction of the Project. You represent that the sales tax, parking tax, and possessory interest tax are generally applicable taxes. You also represent that you reasonably expect that new revenue from these four sources will equal or exceed the debt service on the Lease Revenue Bonds.

However, to the extent that new revenue received by the City from the possessory interest taxes, the parking taxes, and the sales taxes falls short of the debt service on the Lease Revenue Bonds reduced by the Company’s rent under the Event Center Lease, the Company will agree to reimburse the City for that shortfall (the “Gap Funding Agreement”). In determining whether such a shortfall exists in a year, the City will pay the debt service on the Lease Revenue Bonds first from the possessory interest taxes, then from the parking taxes, and last from the sales taxes. If new revenues received by the City from sales taxes owed by the Company in connection with the construction activities of the Project are not needed to pay debt service on the Lease Revenue

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<sup>3</sup> The Company will permit the City to use exclusively and to operate, retaining all revenue and paying all operating costs, the New L Street Garage during any convention center events that do not conflict with events at the Event Center or the Stadium. The Company will also permit the City to use the first floor of the New L Street Garage to stage trucks for convention center events.

Bonds, those sales taxes will be abated, but only to the extent that the Company paid the costs of defeasing the Hall C Bonds.

*The Assessment Bonds, Signage Agreement, and Stadium Lease Extension Agreement*

Under a State law (the "Assessment Bond Act"), the City is authorized to establish a district and, with the approval of those in the district, to levy a special tax on the property within the district for the purpose of issuing bonds secured by and payable from the revenue from the special tax. To partially finance construction of the New Hall, the Assessment Bond Issuers will, in approximately Year W, issue the Assessment Bonds pursuant to the Assessment Bond Act. The City will establish two districts to be the Assessment Bond Issuers. In one of these districts, consisting of the Stadium and at least part of the convention center, the special tax will be levied on the Company's leasehold interest in the land on which the Stadium is located. The City will levy this special tax beginning approximately two years after Year W and ending in the last year of the term of the Assessment Bonds. In the other district, consisting of the Entertainment Complex and at least part of the convention center, the special tax will be levied on the Company's ownership interest in the Entertainment Complex. The City will levy this special tax beginning approximately 12 years after Year W and ending in the last year of the term of the Assessment Bonds. The Assessment Bonds will be secured by and payable from these special taxes. In each district, the Company is the only entity that will be subject to the special tax.

The Signage Agreement will provide that, beginning two years after Year W and ending with the term of the Assessment Bonds, the City grant to the Company the right to locate certain advertising signage on the exterior of Hall A and the New Hall. The Stadium Lease Extension Agreement will provide that the City extend the term of the Stadium Lease to be coterminous with the Event Center Lease. In exchange for the signage rights and the extension of the Stadium Lease, the Company will approve and pay the special taxes to be levied pursuant to the Assessment Bond Act on its leasehold interest in the site of the Stadium and its ownership interest in the Entertainment Complex. The term of the Signage Agreement is not more than  $f$  percent of the reasonably expected economic life of the New Hall. As more fully described below, the amount of the special taxes is intended to correspond to and to be in lieu of the fair market value payments that the Company would otherwise make in exchange for the signage rights and lease extension.

At least in part, the Company will not make payments of the special tax contemporaneously with its receipt of rights under the Signage Agreement and the Stadium Lease Extension Agreement. During the period in which it is paying the special tax attributable to only one district, the amount of special tax paid by the Company will be less than the fair market value of the rights it will receive under the Signage Agreement; but during the period in which it is paying special taxes attributable to both districts, the amount of special tax paid by the Company will exceed the fair market value of the rights it will receive under the Signage Agreement. Because the extended

Stadium Lease will end in approximately e years after Year W, several years after the end of the term of the Assessment Bonds, the Company will fully pay for the rights it will receive under the Stadium Lease Extension Agreement in advance of receiving those rights.

#### *Equivalence of Value Exchanged*

You represent that, in the aggregate, the present value of the amounts paid by the Company under the Event Center Lease and the Parking Lease and as special taxes under the Assessment Bond Act (as contemplated under the Signage Agreement and the Stadium Lease Extension Agreement) will not exceed the present value of the rights received by the Company under the Event Center Lease, the Parking Lease, the Signage Agreement, and the Stadium Lease Extension Agreement. You represent that this relationship holds using a discount rate of a% and that, based on the facts and circumstances of this case, that rate is reasonable.

#### *Letters of Credit*

The Company will provide the City with one or more irrevocable standby letters of credit to secure the Company's obligations under the Gap Funding Agreement and the other agreements entered into in connection with the Project and to serve as part of a reasonably required reserve fund for each issue of the Bonds. The amount of these letters of credit will decrease over three defined periods ending with the full payment of the Assessment Bonds. You represent that you do not expect any draws to be made under the letters of credit.

#### *Private Business Tests*

The portion of the Signage Agreement that relates to the New Hall will be treated as private business use of the New Hall. Nevertheless, you represent that each issue of the Bonds issued to finance the New Hall will not satisfy the private business tests under section 141(b) of the Code.

#### **Law**

Section 103(a) of the Code provides that, except as provided in section 103(b), gross income does not include interest on any state or local bond. Section 103(b) provides that section 103(a) shall not apply to any private activity bond which is not a qualified bond (within the meaning of section 141). Section 141(a) provides that the term "private activity bond" means any bond issued as part of an issue which meets the private business tests of section 141(b) or the private loan financing test of section 141(c).

Section 141(c)(1) provides that an issue meets the private loan financing test if the amount of the proceeds of the issue which are to be used (directly or indirectly) to make

or finance loans (other than tax assessment loans and other loans described in section 141(c)(2)) to persons other than governmental units exceeds the lesser of 5 percent of such proceeds or \$5,000,000. Section 1.141-5(b) of the Income Tax Regulations provides that, in determining whether the private loan financing test is met, the amount actually loaned to a nongovernmental person is not discounted to reflect the present value of the loan repayments.

Section 1.141-5(c)(1) provides that any transaction that is generally characterized as a loan for federal income tax purposes is a loan for purposes of section 1.141-5. Section 1.141-5(c)(1) further provides that a loan may arise from the direct lending of bond proceeds or may arise from transactions in which indirect benefits that are the economic equivalent of a loan are conveyed. Thus, the determination of whether a loan is made depends on the substance of a transaction rather than its form. For example, a lease or other contractual arrangement (such as a management contract or an output contract) may in substance constitute a loan if the arrangement transfers tax ownership of the facility to a nongovernmental person. Similarly, an output contract or a management contract with respect to a financed facility generally is not treated as a loan of proceeds unless the agreement in substance shifts significant burdens and benefits of ownership to the nongovernmental purchaser or manager of the facility.

### **Analysis**

The issue to be decided for purposes of this private letter ruling is whether the Lease Revenue Bonds satisfy the private loan financing test of section 141(c). Having considered all of the facts and circumstances, we conclude that the Lease Revenue Bond Issuer has neither directly loaned proceeds of the Lease Revenue Bonds to the Company nor conveyed to the Company benefits that are the economic equivalent of a loan of such proceeds. The Lease Revenue Bonds do not, therefore, satisfy the private loan financing test. Our conclusion is based on an examination of each element of the Project, including the various contractual arrangements, the parity in value of the consideration to be exchanged under those contracts, the Bonds to be issued to finance the New Hall, and the sources of revenue that will pay debt service on the Bonds.

As the Company's right to install signage under the Signage Agreement is private business use of the New Hall, so are these signage rights private business use of the proceeds of the Bonds. Nevertheless, this use will not result in a loan of such proceeds. Even though the debt service on the Assessment Bonds will generally correspond to the value of the Company's rights under the Signage Agreement and the Stadium Lease Extension Agreement, several factors weigh against the conclusion that there is a loan of the proceeds and in favor of the conclusion that the Signage Agreement is a lease. The City will be the sole owner of the New Hall. The Company will have no option to purchase any part of the New Hall at any price and no other facts suggest that the Company will have any direct or indirect ownership interest in the New Hall at any time in the future. The Company's private business use of the New Hall for signage will end with the term of the Bonds, yet the useful life of the New Hall is expected to be



significantly longer than the term of the Bonds. Additionally, the Company's signage rights on the New Hall will be part of broader, uniform signage rights that include Hall A, and the signage rights with respect to Hall A will not give rise to a loan of the proceeds of the Bonds.

Furthermore, the facts do not support a conclusion that the Lease Revenue Bond Issuer, the Assessment Bond Issuers or the City will advance proceeds of the Bonds to the Company. Outside of the exchanges expected to occur under the Event Center Lease, the Parking Lease, the Signage Agreement, and the Stadium Lease Extension Agreement, the City will not directly convey any value or benefit to the Company. The Company alone will bear the cost of construction of all buildings other than the New Hall. The City will use the proceeds of the Bonds to pay the construction costs of the New Hall. With respect to the agreement that the Company will build the New Hall at an agreed upon cost ceiling, the Company will not receive any proceeds of the Bonds for its own benefit because it is expected that the Company will pass all of the City's payments through to the general contractor and others who will perform the work pursuant to a guaranteed maximum price contract. Because of the guaranteed maximum price contract with the contractor, the Company is expected to have no obligation to bear the costs of constructing the New Hall. The Company will not own any portion of the New Hall, and the City will not transfer tax ownership of the New Hall to the Company through a contractual arrangement such as a management contract or output contract.

This conclusion that the Lease Revenue Bond Issuer and the Assessment Bond Issuers have advanced no proceeds of the Bonds to the Company is supported by the fact that the Company's payments to the City in connection with the Project cannot be repayment of any such advance. Specifically, the Company's direct and indirect payments to the City under the Event Center Lease and Parking Lease, including rent and demolition expenses, and the special taxes contemplated in the Signage Agreement and the Stadium Lease Extension Agreement will be made in exchange for rights and benefits of equal or greater value. The Company's payment of the possessory interest tax on the Company's leasehold interests under the Event Center Lease and the Parking Lease and sales tax on certain of its construction expenditures for the Project are generally applicable taxes of which the City only receives a share and the creation of which is unrelated to the Project, and thus cannot be repayment of a loan of proceeds of the Bonds. The Company's obligations under the Gap Funding Agreement and the letters of credit are remote and unlikely to be triggered. Finally, the Parking Make Whole Provision of the Parking Lease is merely compensation for lost Hall C Parking revenue.

### **Conclusion**

Accordingly, we conclude, based strictly on the information submitted and representations made and considering all the facts and circumstances, that the Lease Revenue Bond Issuer will not loan the Company, directly or indirectly, any of the

proceeds of the Lease Revenue Bonds. The Lease Revenue Bonds will not, therefore, satisfy the private loan financing test of section 141(c).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Associate Chief Counsel  
(Financial Institutions and Products)

By: \_\_\_\_\_ /S/  
Timothy L. Jones  
Senior Counsel  
(Financial Institutions and Products)