

January 19, 1970

Dear Mr. Kingman:

Your letter of December 23, 1969, and the enclosures from Mr. William Rosenberg, Executive Director of the Michigan State Housing Authority is acknowledged.

We have been advised that the Treasury Department has not raised any fiscal policy objections with respect to HUD providing FHA mortgage insurance and mortgage interest subsidies to projects financed by the issuance of tax-exempt bonds. This policy question, therefore, is up to HUD.

This office has previously directed your attention to the Tax Reform Act of 1969 and specifically to section 601 of the Act, which is the arbitrage bond provision. This section defines an arbitrage bond as one in which the yield on the acquired security is "materially" higher than the bond yield. The word "materially" is not defined in the Act, but must be defined by regulations or in the tax ruling process.

It appears to us that HUD should expressly alert the issuer to the arbitrage provision, and if there is any doubt in counsel to the issuer's mind with respect to this provision, HUD should urge that a ruling request be filed. Otherwise, the government could be put in the embarrassing position of the Internal Revenue Service challenging the tax exempt status of bonds in a project in which HUD has actively participated.

We do not mean to imply from this comment that the bonds to be issued by the Michigan authority would or would not be arbitrage bonds. Rather, we feel that you should understand that no determination by Treasury has been made. Thus, until regulations are issued, the tax status of these bonds is uncertain.

If you have any questions about this matter, please call upon us.

Sincerely yours,

Meade Whitaker
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