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Tax-Credit Bonds: North Dakota Senator Proposes Using QZABs For New School Construction

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by Alison L. McConnell

Municipalities would be authorized to use qualified zone academy **bonds** to finance new school construction under legislation introduced last week by Sen. Kent Conrad, D-N.D.

Conrad's bill, which is almost identical to one he proposed in July 2003, would also open up the program to all types of **tax**-exempt bond investors, allow for **credit**-stripping, and change the way QZAB issuance limits are determined.

QZABs are taxable **tax-credit bonds** that provide holders with federal income **tax** credits in lieu of **tax**-exempt interest payments. The \$400-million-a-year program was created in 1997 and currently allows municipalities to raise funds for repairs and renovations at existing educational facilities, but not for new construction.

Conrad's bill would extend the QZAB program, which technically expired last year, through 2007 and expand it in several ways.

It would first broaden the list of eligible bond purchasers to comprise all taxpayers, including investors such as individuals and mutual funds. Currently only banks, insurance companies, and financial lending institutions are eligible to purchase QZABs.

Under existing law, QZABs can be used to finance repairs and renovations to existing school facilities. Conrad's legislation would add new school construction and land acquisition for schools as approved uses of QZAB proceeds.

The bill would also authorize states to roll their unused QZAB authority over indefinitely - current law allows them to do so only for two years - and allow the **tax** credits to be stripped from QZABs and resold as separate securities, a proposal popular with buy-siders, and alter the way state-by-state QZAB authority is calculated each year.

Currently, the \$400-million authority earmarked for the school **bonds** is divided up based on the percentage of each state's residents that lives below the poverty line. Conrad's bill would instead require that QZAB authority allocations be based on the annual grants states receive from the U.S. Department of Education.

It would also give small states more access to QZABs by requiring a minimum per-state allocation of 1% of the national level - at current program levels, \$4 million each.

"There is certainly a case to be made that the pockets of rural poverty are such that some states would be better served by this formula," said **Laurence Peters**, director of **Cyberlearning.org**, a nonprofit group that helps schools use QZABs.

"It is natural that it should follow the Title 1 formula. I would recommend that the minimum amount of 1% or \$4 million be increased to 2% or \$8

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million since there is very little to attract a state to such a low amount," he said.

Jeremy A. Spector of Blank Rome LLP in Philadelphia said Conrad's changes would improve the utility of the QZAB program.

"The bill would enhance the demand and efficiency of the program by allowing credits to be stripped and by allowing virtually any taxpayer to benefit from owning an entitlement to the **credit**," he said.

Linda Schakel of Ballard Spahr Andrews & Ingersoll LLP here said in the past schools might have been discouraged from undertaking new construction projects, even though they might have been more cost-effective, because they could not use QZABs.

"Hopefully it will save schools some money. I think it will be helpful," she said.

Conrad's bill was introduced March 1 and immediately referred to the Senate Finance Committee, that chamber's **tax**-writing committee. Since the **tax** reconciliation bills awaiting conference on Capitol Hill also contain an extension of the QZAB program through 2007, it is unclear whether a successfully passed law containing that extension would alter Conrad's bill. President Bush has also proposed extending the program through 2007.

"This is a decision that the Senator will make after the conference committee acts," spokesman Sean Neary said yesterday.

QZABs were the first taxable **tax-credit bonds** created by Congress. Since then, lawmakers have crafted clean renewable energy **bonds**, or CREBs - another bond category that works in very similar ways and can be used by nonprofit utilities to finance renewable energy projects.

Ed Oswald of Orrick Herrington & Sutcliffe LLP said Conrad's bill would make QZABs more consistent with CREBs.

"The group of eligible taxpayers who now could receive a **credit** with this legislation is being expanded to any taxpayer, like CREBs," he said. It's "intended to provide for a group of more diverse holders and increased market demand."

Peters said pension fund managers would be "overjoyed" to have QZABs open to them as investment opportunities, and added that the new construction portion of the bill is crucial.

"We know that the need is there," he said, noting estimates that U.S. schools need over \$112 billion in repairs and modernization to comply with federal mandates. (c) 2006 The Bond Buyer and SourceMedia, Inc. All rights reserved. <http://www.bondbuyer.com>
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