Fairfax County Economic Development Authority v. Commissioner, 77 T. C. 546 (1981)

Industrial development bonds financing federal facilities are not tax-exempt unless they meet specific statutory exceptions.

Summary

Fairfax County Economic Development Authority proposed to issue industrial development bonds (IDBs) to finance a facility for the U. S. Government Printing Office. The issue before the court was whether these bonds qualified for tax-exempt status under section 103 of the Internal Revenue Code. The court ruled that the bonds did not qualify for exemption because the federal government is not considered an "exempt person" under section 103(b)(3), and the bonds did not meet the small issue exemption criteria due to the aggregation of federal capital expenditures exceeding the $10 million limit. The decision emphasized the legislative intent to apply a modified "real obligor" theory to IDBs, focusing on the use and user of bond proceeds rather than just the issuer.

Facts

Fairfax County Economic Development Authority, a governmental entity, sought to issue bonds to finance a facility for the U. S. Government Printing Office (GPO). The bonds were to be repaid solely from the revenues derived from leasing the facility to GPO. Springbelt Associates Limited Partnership constructed the facility and was to repurchase it from the Authority using an installment sales contract. The bonds were structured with a 6-year call provision linked to the GPO's lease termination rights.

Procedural History

The case was brought before the U. S. Tax Court as a declaratory judgment action pursuant to section 7478 of the Internal Revenue Code. The court reviewed the administrative record and stipulations of fact under Rule 122. The key issue was whether the proposed bonds qualified as tax-exempt industrial development bonds.

Issue(s)

1. Whether the proposed bonds would be obligations of the United States?
2. Whether the Federal Government or the U. S. Government Printing Office (GPO) is an "exempt person" within the meaning of section 103(b)(3)(A)?
3. For purposes of the $10 million small issue exemption of section 103(b)(6)(D), whether the capital expenditures in Fairfax County of the GPO, the legislative branch, or the entire U. S. Government should be aggregated with those of the project involved?

Holding

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1. No, because Congress preempted the “real obligor” theory in determining the tax-exempt status of industrial development bonds when it enacted section 103(b), thereby encompassing IDBs whose proceeds are to be used to finance facilities for the Federal Government.
2. No, because the U. S. Government and its agencies and instrumentalities are not “exempt persons” within the meaning of section 103(b)(3)(A), as upheld by section 1. 103-7(b)(2) of the Income Tax Regulations.
3. No, because for purposes of the $10 million small issue exemption, the capital expenditures in Fairfax County of the entire U. S. Government should be aggregated with those of the GPO facility, exceeding the exemption limit.

Court’s Reasoning

The court rejected the Commissioner’s argument that the bonds were obligations of the United States based on the “real obligor” theory, stating that Congress had specifically addressed this issue in section 103(b) by focusing on the use and user of the bond proceeds. The court found that the Federal Government is not an “exempt person” under section 103(b)(3)(A), as clarified by the applicable regulations, and thus the bonds could not avoid IDB status on this ground. For the small issue exemption, the court held that the capital expenditures of the entire U. S. Government must be aggregated, preventing the bonds from qualifying under the exemption. The court emphasized that the legislative history and purpose behind section 103(b) supported these conclusions, aiming to prevent large business ventures or federal facilities from benefiting from tax-exempt financing without meeting specified exceptions.

Practical Implications

This decision clarifies that industrial development bonds used to finance federal facilities are generally not tax-exempt unless they fall within specific statutory exceptions. Practitioners must carefully consider the use and user of bond proceeds when structuring IDBs, especially when federal entities are involved. The ruling reinforces the need to aggregate all federal expenditures in a jurisdiction when assessing eligibility for the small issue exemption, which can significantly impact the feasibility of using IDBs for projects involving federal agencies. This case has influenced subsequent rulings and regulations regarding the tax treatment of IDBs, emphasizing the importance of adhering to the statutory framework established by Congress.

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