THE BOND BUYER

IRS private letter ruling a breakthrough for ports, airports

By

Brian Tumulty

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WASHINGTON — Government-owned ports and airports are expected to benefit from a recently released Internal Revenue Service Private Letter Ruling supporting a simplified method of calculating a safe harbor for private leases of tax-exempt bond-financed facilities.

Private leases that go beyond 80% of the useful life of a port or airport jeopardize the public ownership of a port or airport that's required for these tax-exempt facility bonds.

Calculating the remaining useful life of a port or airport facility can be problematic, but the IRS ruling released May 3 supports a simplified method of making this determination using the date of the new agreement as a starting point.

Matthias Edrich, a partner at Kutak Rock in Denver, described that date as a practical starting point.

"It allows for a more current determination of the actual remaining useful life of property rather than relying on useful life determinations that may have been made many years previously when the related bonds were originally issued," Edrich said in an email.

The ruling involved an unidentified port that calculated the remaining useful life of five asset classes of its property: wharves and pilings; yard improvements such as paving, fencing and utilities; buildings; cranes; and land.

An engineer's report was used for each of the five asset classes using the date of the inspection as the starting point. Each asset class was given a weighted average based on the amount of tax-exempt bonds at their date of issue.

Charles Cardall, a partner at Orrick based in San Francisco who chairs his firm's tax department, submitted the PLR request to the IRS on behalf of a client. He said the ruling "removed all the complication of looking at individual improvements. For ports and airports I think it's a big breakthrough."

"I spend a fair amount of time with port and airport clients talking to them about, how do you manage this notion of older assets that you think today really do have a fair amount of life left to them," Cardall said. "You paid for them a long time ago and how do you do that, how do you manage that?"

Ports may have old bond-financed facilities that were built 30 years ago with only 10 years left on the original 40-year useful life estimate, but the improvements made to it over the years have extended that useful life.

"Most people have tried to meet that safe harbor, or be less than 80%," said Cardall. "The problem was, it was very hard to know exactly how you calculated it."

The port represented by Cardall had a terminal operator that consolidated some operations and wanted to make a number of improvements. But before doing that, the terminal operator wanted to extend three existing leases.

Cardall said the port didn't have that many years in the useful life of various assets.

“I said you could redeem a bunch of bonds, but that was going to be really expensive and they said there’s got to be a better way,” he said. “We came up with this analysis and we thought there was enough support for this in the general tax law.”

Although the IRS said the ruling applies only to the particular case it was presented with, Edrich and Cardall said it will be used by other bond attorneys.

“Others will probably look to this ruling for bonds that are of the same type,” Edrich said. “Bonds that are also exempt facility bonds that are also subject to this governmental ownership requirement.”

Cardall said the ruling might also be applied to management contacts involving tax-exempt bond-financed hospitals, student housing, university facilities and parking structures.

“For these guys I was working with, this was an excellent answer and I think it will be a really good answer for a lot of folks,” Cardall said.