IRS Identifies Proposed Tax-Exempt Political Subdivision Regulations as Overly Burdensome

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07/11/2017

The Internal Revenue Service has identified the proposed regulations on the definition of political subdivisions as one of eight regulations that (i) impose an undue financial burden on U.S. taxpayers; (ii) add undue complexity to the Federal tax laws; or (iii) exceed the statutory authority of the IRS.

The IRS issued Notice 2017-38responding to an Executive Order signed by President Trump calling on the Treasury Department to identify regulations that meet at least one of these criteria. The analysis of the Treasury identified eight such regulations, including the political subdivision regulations proposed by the Treasury Department on February 23, 2016. The proposed regulations define a “political subdivision” for purposes of Section 103 of the Internal Revenue Code, and would impose restrictions regarding the eligibility of certain entities to issue tax-exempt bonds for governmental purposes.

In its Notice issued on July 7, 2017, the IRS notes that commenters have stated that the proposed regulations’ extension of the “sovereign powers” standard defining government entities is already well-settled law and was endorsed by congress, which makes additional limitations unnecessary. Furthermore, commenters also stated that this new regulation would disrupt the current status of many existing entities and that it would be burdensome and costly for issuers to revise their organizational structures in order to comply with the proposed regulation.

The IRS has requested comments on whether this proposed regulation, along with the others identified by the Treasury, should be rescinded or modified. The public comment period ends on August 7, 2017 and the Treasury must submit a report to the President by September 18, 2017, which will recommend the specific actions necessary to mitigate the tax burdens identified. Here is the the full text of the proposed regulation.