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Qualified Energy Conservation Bonds: An Overview

Introduction and History

This memorandum addresses Qualified Energy Conservation Bonds ("QECBs"), a type of qualified tax credit bond that state and local governments may use to finance various energy projects, including particularly those that promote energy efficiency and renewable source technologies. QECBs were originally authorized under the federal Energy Improvement and Extension Act of 2008, enacted in October 2008, as further amended and expanded by the federal American Recovery and Reinvestment Act of 2009, enacted in February 2009, under Sections 54A and 54D of the Internal Revenue Code of 1986, as amended (the "Code"). Initially, QECBs only provided a credit to a taxpayer bondholder against the bondholder's tax liability for the year; however, following the enactment of H.R. 2847 in March 2010, issuers now also have the option of electing to receive a direct subsidy from the U.S. Department of Treasury (the "Treasury") in an amount equivalent to the non-refundable tax credit that would otherwise accrue to the bondholder.

This memorandum will explain the relevant provisions of the Code and additional requirements under federal law relating to the issuance of QECBs and subsequent receipt of payments from the Treasury, and will describe what types of energy-related projects will be eligible. This memorandum also will discuss the rules and procedures promulgated by the Georgia Environmental Facilities Authority ("GEFA"), which set forth prerequisites to receiving QECB allocation that are specific to Georgia municipalities and other local governments.

Basic Federal Requirements

For bonds to qualify as QECBs, they must be part of an issue for which:

1. 100 percent of the available project proceeds are to be used for one or more "qualified conservation purposes";

2. a state or local government is the issuer; and

3. the issuer has designated such bonds as QECBs for purposes of Section 54D of the Code.

Treasury Notice 2009-29 sets forth the maximum face amount of QECBs that may be issued by each state and large local government (defined as having a population of 100,000 or more) in order to comply with the national QECB volume cap of $3.2 billion.

For Georgia, the total combined state and local QECB allocation is limited to $100,484,000. Within the statewide and each large local governmental sub-allocation, at least 70 percent of the amount must be dedicated to public purpose projects, while the remaining 30 percent may be applied to private activity bonds.

Pursuant to and in accordance with the authorization of the Treasury and the Georgia State Financing and Investment Commission ("GSFIC"), GEFA has disseminated additional policies and procedures relating to the allocation and reallocation of QECB volume cap, which are set forth in this memorandum below. Once QECBs are issued, the issuer also must comply with Davis-Bacon wage and benefit requirements, as well as with various arbitrage, reporting, and other tax laws under the Code.

Eligible Projects

As noted above, one of the basic requirements of a QECB is that 100 percent of the available project proceeds will be used for one or more "qualified conservation purposes." Pursuant to Section 54D(f) of the Code, qualified conservation purposes can include (but are not limited to) the following:

- Reducing energy consumption in public buildings by at least 20 percent;
- Implementing green community programs;
- Supporting research facilities or research grants relating to energy reduction and efficiency technologies and production of nonfossil fuels;
- Supporting mass commuting facilities and pollution reduction expenditures;
- Promoting commercialization of green building technology, waste-to-fuel conversion, and various other technologies through demonstration projects; and
- Conduction public education campaigns to promote energy efficiency

The foregoing list is not meant to be exhaustive, and additional types of energy projects may qualify. For private activity bonds that are QECBs, qualified conservation purposes are limited to capital expenditures.

Treasury Subsidy

The issuer of a QECB bond issuance has two options relating to how the QECB subsidy will be applied: either the issuer may issue the QECBs as traditional tax credit bonds (whereby the bondholder will receive a quarterly tax credit offsetting the bondholder's tax liability in lieu of receiving interest payments by the issuer) or, alternatively, the issuer may irrevocably elect to receive direct payments from the Treasury in an amount equal to the credit amount that the bondholder otherwise would have received. In either scenario, the QECB issuer will benefit from a lower effective interest rate.

The annual credit amount is determined by multiplying the "applicable credit rate" by the outstanding face amount of the QECB bond. For QECBs, the applicable credit rate is 70 percent of the rate that the Treasury determines will permit the issuance of qualified tax credit bonds with a specific maturity or redemption date without discount and without interest cost to the issuer. The Treasury sets this rate daily.

Georgia Sub-Allocations

The State of Georgia received an aggregate allocation of $100,484,000 under the QECB program, of which $37,047,531 was allocated directly to the state and the remainder sub-allocated amongst various large governmental units therein. Provided that a sub-allocation designee properly notified GEFA of its intent to use its QECB allocation before the applicable deadline (as further described below), the following chart sets forth the respective share of QECB allocation allotted to various major cities and counties across Georgia:

Allocation Designee (Large Governmental Unit)	**Share of State Allocation**
City of Atlanta	$ 5,465,388
Bibb County	1,628,726
Clayton County	2,865,811
Cobb County	7,284,149
DeKalb County	7,367,023
Fulton County	5,372,355
Gwinnett County	8,173,474
City of Savannah	1,372,082

GEFA Requirements

As noted above, certain large local governmental units in Georgia received QECB volume cap sub-allocations separately from the allocation amount issued to the State. However, GEFA's written procedures required that the 19 counties, two consolidated governments, and three cities that did receive such sub-allocation each notify GEFA no later than November 2, 2009, of their intent to use such sub-allocation, or else it would be deemed waived back to the state. Accordingly, any Georgia local government that either did not receive an initial sub-allocation or did not notify GEFA of its direct allocation acceptance by the deadline, but that now desires to issue QECBs, must file an "application for notice of re-allocation" in accordance with GEFA's procedures in order to receive a specified amount of Georgia's state allocation.

In addition to the GEFA application form, the potential issuer filing for QECB re-allocation amounts should submit to GEFA the following items:

- An issuer's certificate, certifying that the issuer has a project eligible for QECB financing;
- A written opinion of legal counsel addressed to GEFA, to the effect that the issuer is authorized under Georgia law to issue bonds for the proposed project, citing constitutional or statutory authority;
- A written opinion of legal counsel addressed to GEFA, to the effect that the proposed bonds will qualify as QECBs when issued;
- A written letter of intent from an underwriter, lender, or other purchaser, addressed to GEFA, to purchase the bonds upon delivery; and
- Any additional items or information that may be specified in GEFA's procedures or otherwise reasonably required by GEFA.

At the discretion of GEFA, the requirement of a written letter of intent may be waived if an officer of the issuer certifies that the proposed QECBs will be issued on a competitive bid basis. Applications must be in even amounts of $1,000. Applicants may also include a letter of support for the proposed project from a state economic or community development agency or a state agency promoting energy or environmental activities. Upon reviewing applications, special consideration will be given to projects that, among other criteria, (1) expand economic opportunities, particularly in areas of distress, (2) meet critical energy needs or statewide conservation goals, (3) promote the general welfare of the state, or (4) demonstrate feasibility and readiness.

Notwithstanding the extension under federal law of the QECB program past January 1, 2011, GEFA is not required to accept any application for notice of re-allocation after December 31, 2010. A notice of re-allocation pursuant to a GSFIC resolution upon the recommendation of GEFA constitutes the only means by which any of Georgia's QECB volume cap can be re-allocated by the state to a specific issuer for a specific issue of bonds. Any notice of re-allocation will expire on the one hundredth day (or first business day thereafter) after the notice of re-allocation has been given, provided, however, upon good cause shown that GEFA has the discretion (but not the obligation) to extend such expiration date for one additional period not longer than 30 days.

Hunton & Williams can assist municipal governments, development authorities and other potential issuers interested in the QECB program with determining whether a potential project is eligible; preparing the GEFA application for notice of re-allocation and necessary governmental resolutions authorizing QECB issuance; acting as bond counsel and counsel to the issuer; and complying with the federal and state regulations and requirements prior and subsequent to the issuance of the bonds. Please feel free to contact Doug Selby at (404) 888-4207 or Kristen Nugent at (404) 888-4168 if you have any questions.