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MEMORANDUM

Executive Summary of the American Recovery and Reinvestment Act of 2009

In the face of the nation's economic crisis, the Federal government enacted the most expansive economic stimulus legislation in generations. The American Recovery and Reinvestment Act of 2009 ("ARRA") quickly injects federal spending and tax incentives into many areas of the economy. In addition, several fundamental priorities of the Obama Administration are reflected in the spending and tax incentives in ARRA.

Overall, ARRA generally does three things: massive appropriations, with most funds flowing through state governments; innovations directed specifically at unlocking credit in public finance and in the renewable energy sector; and changes in tax law that affect 95% of individual taxpayers. This memorandum addresses ARRA actions in the following arenas:

- Energy;
- Infrastructure;
- Public Finance;
- Health;
- Education;
- State & Local Aid;
- Unemployment Assistance;
- Low-Income Community Investment;
- Tax Relief; and
- Transparency

I. ENERGY

In the energy sector of the economy, ARRA's focus is on funding and stimulating investment in the "clean energy" sector of renewable energy technologies and energy efficiency, including electric transmission facilities that can support bringing renewable energy to market and "smart grid" systems that can enhance efficiency of electricity use.

For context, this background may be helpful: the renewable energy industry has been entirely dependent for many years on an interconnected web of federal and state incentive programs, particularly federal tax credits and accelerated depreciation rules. However, the market for tax-driven equity investors was virtually frozen by late 2008, meaning that passive investors who could utilize tax credits generated by renewable energy projects had pulled out of that market. (Example: Lehman Brothers.)

In response, ARRA takes multiple energy-related initiatives, including:

- Devotes more than \$40 billion of ARRA funding (not counting loan guarantees and certain grants) to direct funding of clean energy programs.

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- Restructures an existing though stalled DOE loan guarantee program, allowing for \$60 billion in commercial loan guarantees to renewable energy and transmission projects.
- Creates a grant program administered by the Treasury Department (recognizing that many investors have insufficient taxable income to offset with tax credits), whereby project owners can waive their right to claim an investment tax credit (ITC) and instead, receive a cash payment equal to 30% of project capital cost. The appropriation for these grants is unlimited.
- Creates innovative bonding authority, as mentioned below in the discussion of public finance. In relation to energy, the most important provision is the elimination of the prohibition on multiple governmental subsidies being applied to a single project; as a result, a single project can claim the ITC, or convert ITC benefits to a Treasury cash grant, and at the same time be structured to incorporate subsidized bond finance mechanisms. This is especially significant for “public/private” projects with county or city sponsorship or involvement.
- Creates investment tax credits for manufacturing investments in renewable energy technologies.
- Funds two DOE matching-grant programs for investment in smart grid technologies and equipment, and supports investment in transmission facilities that can bring output from remote renewable energy projects to the grid.
- Appropriates massive funds for state and local governments, which will re-grant the funds for private renewable energy and energy efficiency projects, as well as use the funds to install renewable energy facilities at government buildings. For example, ARRA directs over \$12 billion in federal spending to promote energy efficiency, via both direct grants and block grants to states and local governments.

II. INFRASTRUCTURE

Under ARRA, four non-energy areas of American infrastructure receive an injection of Federal spending: (i) transportation, (ii) broadband, (iii) water, and (iv) housing. All modes of transportation, including highway, transit, rail, aviation, and ports, receive in the aggregate approximately \$45.8 billion in formula funding and discretionary grants. With this money, public agencies can improve infrastructure and equipment. Projects receiving these transportation funds must be shovel-ready.

The development of broadband across the nation is a feature of ARRA. The legislation charges the Federal Communications Commission to develop a National Broadband Plan to improve access to, and use of, broadband service in all areas of the United States. \$4.7 billion is available through the U.S. Department of Commerce’s Broadband Technology Opportunities Program and another \$2.5 billion is available through the U.S. Department of Agriculture’s Distance Learning, Telemedicine, and Broadband Program. The latter program targets broadband development in rural areas that do not otherwise receive funds from the Broadband Technology Opportunities Program.

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Programs with the Environmental Protection Agency and the U.S. Department of Agriculture inject over \$7 billion to improve the nation's drinking water and sewage infrastructure. The Environmental Protection Agency's Clean Water State Revolving Fund and Drinking Water State Revolving Fund provide \$6 billion in capitalization grants that can be used for new projects or debt refinancing.

For the housing component of ARRA, there is \$13 billion for the U.S. Department of Housing and Urban Development to improve access to affordable housing in urban areas and to address neighborhood destabilization created by foreclosed-upon homes and residential properties. This includes a \$4 billion capital fund for public housing agencies, of which \$1 billion remains available on a competitive application process.

III. PUBLIC FINANCE

ARRA makes various changes to the rules governing the financing of public sector bonds, and expands the scope of bonding authority by state, county, and city governments. These changes had two unified objectives -- to unlock frozen credit markets, and to facilitate the funding of public sector projects that would have an employment impact. Key features include:

- Expanded authorization for tax credit bonds ("TCBs") issued in 2009 or 2010. TCBs are bonds bearing taxable interest with Federal tax credits or payments as a subsidy in lieu of tax-exemption. The effect is to allow the issuer the benefit of borrowing money at a reduced overall cost that is generally equal to tax-exempt interest rates or in some cases significantly lower. TCBs are intended to be sold into the taxable markets, which are broader than the tax-exempt market. Any public purpose bond can be issued as a TCB under the provisions for "Build America Bonds," and deeper subsidy credits are allowable for TCBs that qualify under rules for school construction, renewable energy, and "recovery zone" development.
- Exemption from alternative minimum tax on tax-exempt private activity bonds issued in 2009 or 2010. Purchasers of tax-exempt private activity bonds such as bonds for airports, solid waste disposal facilities, and single-family and multi-family housing are exposed to alternative minimum tax ("AMT") depending on their individual circumstances. AMT exposure has traditionally added approximately 0.25% to the market interest rates for tax-exempt private activity bonds. ARRA exempts these bonds from AMT on either "new money" bonds or certain kinds of refundings, meaning that outstanding "AMT bonds" can be refunded into the non-AMT market at a potential rate savings of 0.25%.
- Increase in authorization for "bank qualified" bonds ("BQs") for 2009 or 2010. BQs are bonds that can be purchased by a bank without being subject to the general rule that a bank will lose its ability to take a tax deduction for interest that it pays on its indebtedness to investors or depositors, to the extent that it holds tax-exempt bonds. Pre-ARRA, an issuer could sell up to \$10,000,000 of governmental bonds or bonds issued for 501(c)(3) organizations to any bank without a corresponding loss of the bank's interest deduction, provided that the issuer did not issue more than \$10,000,000 of tax-exempt bonds in the calendar year. ARRA raised the \$10,000,000 limit to \$30,000,000 and allowed a separate \$30,000,000 for bonds issued for a 501(c)(3) borrower. ARRA also

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allows banks to purchase tax-exempt bonds in 2009 and 2010 up to 2% of their balance sheet assets, without regard to the \$30,000,000 per-issuer limit.

IV. HEALTH

Acting on the belief that more effective digitalization of health care information will create jobs, cut costs, and save lives, ARRA includes provisions that invest significant amounts to improve Health information technology. ARRA invests approximately \$20 billion and amends Medicare and Medicaid to promote and advance the use of health information technology by developing the nationwide electronic exchange and use of health information and infrastructure and tools for promotion of telemedicine, including coordination among federal agencies in the promotion of telemedicine.

ARRA also aims to preserve the public health by investing in community health centers, low-income children and families, and immunization. Community health centers that serve medically underserved populations are eligible for \$2.5 billion dollars under ARRA, of which \$1.5 billion is for construction, renovation, and equipment for health centers that serve medically underserved populations. The remainder of the available funding would support the center's operations. Existing programs for low-income children and families, such as Child Care and Development Block grants, Head Start grants, Early Head Start grants, and Community Services Block grants, receive an additional \$5.1 billion. Lastly, ARRA invests \$1 billion in a Prevention and Wellness Fund that will finance a discretionary immunization program and the Preventive Health and Health Services Block Grant program.

V. EDUCATION

ARRA markedly increases the amount of federal funding available in existing federal education programs such as Title I and IDEA. Combined, there is more than \$25 billion for these two funding programs, which provide money through statutory formulas to local educational agencies that serve the disadvantaged or children requiring special education.

The new State Fiscal Stabilization Fund helps states to maintain governmental support for education despite the budget crises that all states are facing to various degrees. There is approximately \$45 billion available for states to restore state support, allow implementation of increases to support elementary schools and secondary schools for FY 2010 and FY 2011, and to modernize school facilities. This fund also includes two incentive grant programs that reward states, local educational agencies, and schools that make significant progress towards certain educational achievements.

VI. STATE & LOCAL AID

States and local governments are facing budget shortfalls, layoffs, and an inability to maintain all the government services that their residents require, particularly during this recession. Services receiving federal support in ARRA include public safety, Medicaid and unemployment. Almost \$9 billion is available in ARRA for states to fill budget shortfalls in any state-supported public safety governmental activity. In addition, there is almost \$4 billion for U.S. Department of Justice programs that support local law enforcement.

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The recession increases the demand on state, Medicare, Medicaid and unemployment programs and decreases each state's ability to meet those demands. ARRA provides fiscal relief by increasing the federal support for each program. Specifically, there is a temporary increase to the Federal Medical Assistance Percentages ("FMAP"), which reduces each state's financial obligations to its own Medicaid programs, provided that states do not restrict the eligibility for their Medicaid program. ARRA also halts various Medicare payment reductions scheduled for Fiscal Year 2009 for disproportionate share hospitals, hospice providers, and teaching hospitals. Lastly, ARRA relieves states from paying some of the interest on the funds that states have borrowed from the Federal government to pay unemployment insurance and temporarily expands the Extended Benefits Program so that it is 100 percent federally funded.

VII. UNEMPLOYMENT ASSISTANCE

ARRA also provides two new federally funded unemployment programs. These programs provide financial incentives for states to maintain or even expand their unemployment insurance programs despite the decreasing financial stability of state accounts in the Unemployment Trust Fund. ARRA establishes a \$25 per week supplemental payment to individuals otherwise eligible for unemployment compensation, provided that states do not reduce their average weekly benefit. In addition, ARRA appropriated \$7 billion for a new incentive grant program that encourages states to expand their eligibility standards for unemployment insurance.

ARRA makes health coverage more affordable for employees who lose their jobs by lowering the cost of COBRA coverage for many individuals. Any qualifying individual whose employment is involuntarily terminated between September 1, 2008, and December 31, 2009, and who is eligible for continuation coverage under COBRA because of the termination will be able to continue health coverage at only 35 percent of the ordinary COBRA premium for up to nine months. Employers (and, in certain cases, insurers) will subsidize the remaining 65 percent, but have the right to recover the subsidy amount from the federal government through a credit on their payroll tax deposits.

There is also about \$4 billion for job re-training and employment services. This funding is available from the U.S. Department of Labor for institutions of higher education and other eligible training providers, provided that any grant must facilitate the training of multiple individuals in high-demand occupations.

VIII. LOW-INCOME COMMUNITY INVESTMENT

ARRA also contains tax incentives for businesses to invest in low-income communities and to stimulate the economy. It increases the new markets tax credit allocation cap by \$1.5 billion and permits state housing credit agencies to trade in tax credits for federal grants. In addition, business may now claim a work opportunity tax credit equal to 40 percent of the first \$6,000 of wages paid to employees in certain targeted groups.

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IX. TAX RELIEF

In addition to the tax-related incentive provisions mentioned in the sections above, ARRA also includes two types of tax-relief provisions: for middle class individual taxpayers, and for certain types of transactions and for business, including a particular focus on small businesses.

By way of a few important examples, ARRA highlights include:

- Allowing taxpayers to elect to defer recognition of cancellation of indebtedness income (“COD”) occurring in 2009 and 2010 and then, after the deferral period, to spread out the recognition of the COD over five years (COD Deferral and Spread).
- Permitting certain small corporations to elect to carry back net operating losses from taxable years beginning or ending in 2008 (but not both years) to the third, fourth, or fifth taxable year preceding the loss year.
- Nullification, prospectively, of the effect of an IRS Notice issued by the Bush Administration (IRS Notice 2008-83) that permitted acquired banking corporations to utilize losses realized from bad loans in post-acquisition transactions without regard to the change of ownership limitations imposed under Section 382 of the Code.
- Finally, significant components of ARRA were directed at relief for individual taxpayers, for example, 95% of taxpayers will benefit from the “Making Work Pay Tax Cut.” It is a refundable tax credit of up to \$400 per taxpayer (\$800 per couple filing jointly). It phases out at \$200,000 for couples filing jointly and \$100,000 for individuals.

X. TRANSPARENCY

Every recipient of recovery funds from a Federal agency, including states, state agencies, and political subdivisions, must submit detailed quarterly reports to the Federal agency that include a description of the activities the recovery funds are supporting, an estimate of the number of jobs retained by the project or activity, and detailed information on subcontracts and subgrants. All of the reports by recipients, and review reports by Federal agencies, must be available on www.recovery.gov, where they are subject to scrutiny from the public and a newly established Recovery Accountability and Transparency Board.