THE COMMERCIAL APPEAL
Memphis, Tennessee

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Industry group pushes to protect tax-free status of municipal bonds

By Wayne Risher

Tuesday, November 13, 2012

They're a tax advantage for rich investors and a time-honored way of financing expensive public infrastructure improvements.

But tax-exempt municipal bonds could become the baby that's thrown out with the bath water of fiscal reform, some bond dealers and local government officials fear.

The re-election of President Barack Obama increased the odds that Congress will be asked to rein in tax-exempt bonds. Obama has proposed to take the deduction away from high-income taxpayers who are the most likely individual buyers of the bonds.

The threat is serious enough that a lobbying campaign is gearing up to make the case for preserving the exemption.

Mike Nicholas, CEO of Bond Dealers of America, was in Memphis on Tuesday to meet with member companies and spread the message of Municipal Bonds for America, a coalition of bond issuers and dealers and state and local government officials.

Raymond James/Morgan Keegan, Duncan-Williams, Vining Sparks and Stifel Nicolaus are among member companies with Memphis offices.

Tax-free munis pay investors lower interest rates than corporate bonds but provide a higher net return on investment after the tax savings. Local and state governments are able to obtain lower interest rates that add up to substantial savings over 20- to 30-year payback periods.

Opponents have argued that tax-exempt munis are an inefficient way to finance projects, and that local governments would be better served by an updated version of Build America Bonds. Used to finance projects under the American Recovery and Reinvestment Act, or stimulus program, Build America Bonds involve subsidies from the Treasury to local governments to lower the net cost of borrowing.

But Nicholas said tax-exempt munis, with their 99-year history, have stood the test of time.

"We think that the markets have proven over the past decades and decades that it is an incredibly efficient way to fund roads and bridges and schools and community centers, sewer systems, etc.," he said.

Municipal Bonds for America contends that curtailing deductions for tax-exempt interest will lead to higher borrowing costs for big public projects, or that cities, counties and states will choose to forego vital repairs and improvement of infrastructure.

Marlin Mosby, retired managing director of Memphis consultant Public Financial Management, agreed that tax-exempts are "very efficient. It's because the market is working."

If they go away, "From an economic standpoint, you would think it would mean some projects don't get done, or if they do get done, it will be at a somewhat higher cost. Is it a huge increase? No. But it's significant."

Mosby didn't see a program like Build America Bonds as a suitable replacement. "It was just much more cumbersome."
