

LAW OFFICES
ORRICK, HERRINGTON & SUTCLIFFE
599 LEXINGTON AVENUE
NEW YORK, NEW YORK 10022
TELEPHONE (212) 326-8800
TELECOPIER (212) 326-8900

SAN FRANCISCO, CALIFORNIA 94111
400 SANSOME STREET
TELEPHONE (415) 392-1122

SACRAMENTO, CALIFORNIA 95814
555 CAPITOL MALL
TELEPHONE (916) 447-9200

LOS ANGELES, CALIFORNIA 90071
333 SOUTH HOPE STREET
TELEPHONE (213) 680-7000

January 28, 1991

Lynette Kelly, Esq.
The Municipal Assistance Corporation
For the City of New York
One World Trade Center
Room 8901
New York, New York 10048

Dear Lynette:

As we have discussed, the Corporation will be required to commence the payment of arbitrage rebate toward the end of 1991 with respect to bonds issued after the enactment of the Tax Reform Act of 1986.

The Corporation has retained Orrick, Herrington to provide rebate calculations on an annual basis with respect to each of the series of bonds which are affected. In addition, the Accounting Memorandum attached to the Arbitrage and Use of Proceeds Certificate for each of the relevant series of bonds contemplates that a calculation will be performed on an annual basis. To date we have only been provided with investment information regarding the Series 66 Bonds and have completed the rebate calculations.

Please review this situation and advise me how you intend to proceed and what work we should anticipate performing pursuant to our engagement.

We have also discussed that for purposes of the Arbitrage and Use of Proceeds Certificates and the rebate calculations performed to date, the Corporation has adopted a conservative procedure for allocating portions of the Second Capital Reserve Fund to refunding bonds. This procedure has been developed as a consequence of the lack of specific guidance in current arbitrage and rebate rulings and

ORRICK, HERRINGTON & SUTCLIFFE

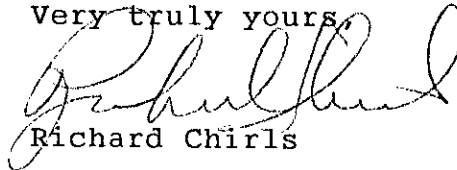
regulations promulgated by the U.S. Treasury Department and to reflect certain underlying principles of the earlier private letter rulings issued by the Internal Revenue Service to the Corporation regarding the Second Capital Reserve Fund.

We believe that it is worthwhile to carefully analyze the method of allocation and to determine whether a more favorable method could be utilized consistent with federal tax law requirements. The potential to reduce the Corporation's rebate liability is significant.

Accordingly, you have authorized us to proceed with this work. It is possible that it may be necessary to obtain a ruling from the IRS prior to approving a method of allocation. We will, of course, confer with you prior to undertaking such an effort. This work regarding the allocation of the Second Capital Reserve Fund investment is not within the scope of our engagement to provide rebate calculation services. Accordingly, we will bill the Corporation on the basis of our normal hourly billing rate procedures.

Please call me regarding the annual rebate calculation with respect to other affected series of bonds or if you have any questions regarding the Second Capital Reserve Fund allocation analysis.

Very truly yours,



Richard Chirls

ap

cc: D. Robinson
G. Majors

MEMORANDUM

Date: 27 April 1990
To: Audit Committee
From: Quentin Spector
Re: Federal Rebate Requirement

MUNICIPAL
ASSISTANCE
CORPORATION
FOR THE CITY
OF NEW YORK

This memorandum summarizes the principal federal arbitrage rebate requirements as they pertain to the Corporation.

The term "arbitrage" has a variety of applications in finance, but with respect to tax exempt finance it applies to the ability of tax exempt issuers to borrow at tax exempt rates and to invest the proceeds at higher taxable rates. In an effort to stem the loss of federal tax revenues arising from abusive issuances driven more by the quest for arbitrage profit than valid public purposes, the federal government has been progressively limiting both the opportunities and incentives for arbitrage for a number of years.

Until the 1986 Tax Reform Act (TEFRA) the major impacts of these limitations on the Corporation's finances were requirements to spend proceeds of issuances within three years, during which time all investment earnings on unexpended proceeds, even if invested at yields higher than the yield on the bond issue, could be kept. Other regulations or special letter rulings from the Internal Revenue Service limited the size or holding period of the capital reserve and the debt service funds, but otherwise all investment earnings could also be retained. With TEFRA, the federal government radically reduced opportunities and incentives for arbitrage in a number of ways. TEFRA also expanded the concept of arbitrage rebate from its previous application to industrial development bonds to all tax exempt issues. The aim of arbitrage rebate is to remove incentive for abusive issuances by requiring the issuer to rebate all arbitrage profits to the federal government.

As such, capital reserve and debt service funds attributable to bonds issued before August 1986 (i.e. up to and including Series 59) are still permitted unrestricted earnings. The capital reserves attributable to issuances since then are subject to the rebate requirement. Accordingly, accumulated earnings on each series' capital reserves in excess of the yield on that series (the bond yield) must be paid to the federal government every five years. This requirement is complicated for a refunding issue in that the amount of capital reserves subject to rebate is related to the redemptions of the bonds refunded by the issue. The attached table projects the amounts of the Corporation's capital reserve funds subject to rebate as of the beginning of each fiscal year when refunded principal is redeemed.

*Municipal Assistance Corporation
For The City of New York*

27 April 1990

Page 2

Unfortunately, the rebate requirement for the capital reserves will continue to grow because the amount of invested funds subject to rebate will continue to grow and it seems likely these funds will be invested at yields higher than the bond yields. It is not possible to predict the growth of the rebate liability on the capital reserve funds precisely, but the attached table projects the annual change based on consistent 8% yields. It also projects the incremental change for each $\frac{1}{2}\%$ of returns realized above the $7\frac{1}{2}\%$ level. Between 6.8% and $7\frac{1}{2}\%$ yields total rebate grows but not as fast. Below 6.8% the rebate is reduced.

When TEFRA was enacted all debt service funds for issues starting with Series 60 were subject to rebate, but the 1988 Tax Act eliminated the debt service fund rebate requirement entirely for bonds issued after November 11, 1988 (to date benefitting only Series 68). For bonds issued between the effective date of TEFRA and November 11, 1988 (i.e. Series 60-67), the 1988 Act provides issuers a choice. One alternative is to cap the rebate liability accrued through November 11, 1988. The other alternative is to continue to subject these funds to a potential rebate liability with the concomitant ability to use any investment earnings below the bond yield to offset arbitrage profits from prior periods. Although the formal election is not required until payment must be made, the financial statements for the three and nine month periods ended March 31, 1990, reflect a decision to cap the liability. However to be conservative until a more definitive calculation is made, the statements reflect the estimated liability as of December 31, 1989 rather than the lower one as of November 11, 1988.

It is not difficult to conclude that it is preferable to cap the rebate liability as of 17 months ago because it has continued to grow since then and it is unlikely that it will ever fall below that level. It has continued to grow because debt service funds have almost always been invested at rates higher than the yields at which the bonds were issued. The bond yields, shown in the attached table, range from 6.80% to 7.50%, while treasury yields have not fallen below these levels for sustained periods of time, as the attached graph demonstrates. The only reason it would make financial sense to continue to pay rebate liability would be to expect that treasury yields will fall to levels below the bond yields, and remain at those levels for the remaining life of the bonds. Only in such a sustained occurrence could the rebate liability be reduced below the requirement as of November 11, 1988. Such an occurrence seems highly unlikely.

Attachments (2)

vsj#314

MUNICIPAL ASSISTANCE CORPORATION
FOR THE CITY OF NEW YORK
ANALYSIS OF CAPITAL RESERVE REBATE
REQUIREMENTS

(\$ 000's)

FISCAL YEAR	SERIES 60	SERIES 61	SERIES 62	SERIES 63	SERIES 64	SERIES 65	SERIES 66	SERIES 67	SERIES 68	TOTAL SUBJECT TO REBATE	TREASURY YIELDS @ 8.00	CHANGE IN REBATE PER 0.5% YLD. VAR.
90	1,493	5,955		921	7,446	7,359	6,824	7,425	7,007	252,308	2,581	1,262
91	2,488	8,678		4,813	9,950	7,055	135,094	36,983	64,808	269,868	2,698	1,349
92	3,484	10,673		4,873	9,950	7,055	135,094	36,983	64,808	272,919	2,733	1,365
93	3,981	12,204		4,934	9,950	7,055	135,094	36,983	64,808	275,009	2,757	1,375
94	19,326	21,634	1,027	5,855	9,950	7,055	135,094	36,983	64,808	301,731	3,049	1,509
95	20,156	35,997	19,382	5,855	9,950	7,055	135,094	36,983	64,808	335,280	3,447	1,676
96	29,860	45,271	34,117	5,855	9,950	7,055	135,094	36,983	64,808	368,993	3,837	1,845
97	29,860	45,271	44,805	5,855	9,950	7,055	135,094	36,983	64,808	379,681	3,965	1,898

-----><-----PROJECTED REBATE-->

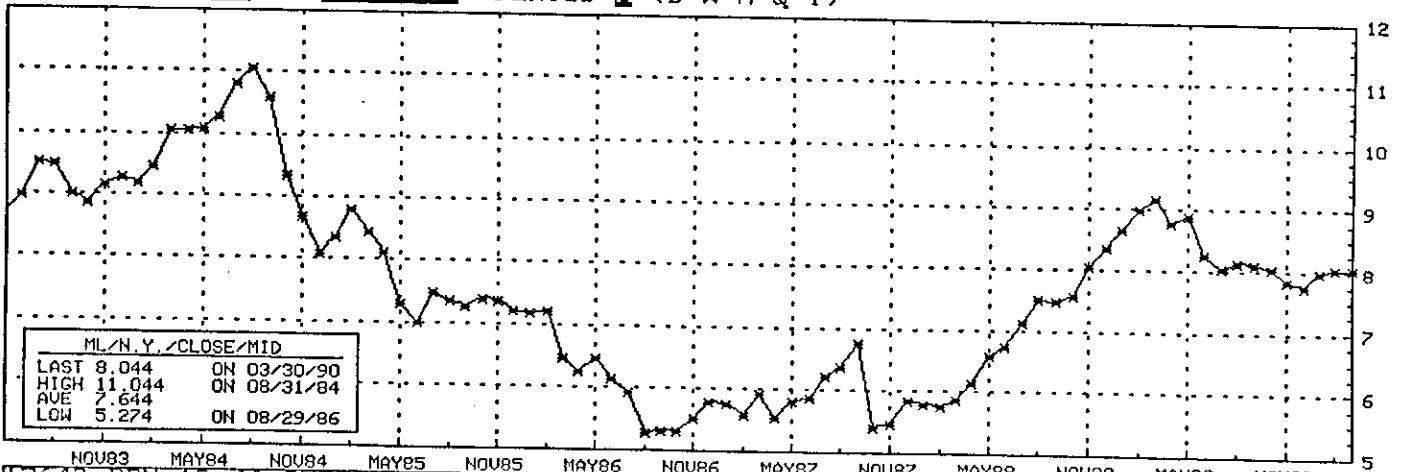
010

Screen printed.

Govt GY

YIELD CHART for GENERIC 3MO BILL

RANGE ~~15/31/88~~ TO ~~15/30/90~~ PERIOD 1 (D-W-M-Q-Y)



Time	Code	Time	Code	Code	Code	Code	Code	Code	Code	Code	Code	Code
NOV83	MAY84	NOV84	MAY85	NOV85	MAY86	NOV86	MAY87	NOV87	MAY88	NOV88	MAY89	NOV89
17643	PRN	13:46	SWEETS & TREATS	FOUNDER	LISTENS	TO	CUSTOMERS	FOR	RECIPES			
17642	APU	13:46	AP	Advisory								
17635	PRN	13:45	NEWLY	DISCOVERED	BACTERIA	REDUCE	ORGANIC	CONTAMINANTS	AND	METHA		
17623	APU	13:43	Telescope	Aperture	Door	Opened						
17622	APU	13:42	Dow	Jones	Averages	At	1:30					

THE BLOOMBERG

The information herein was obtained from sources which Bloomberg L.P. and its suppliers believe reliable, but they do not guarantee its accuracy. Neither the information, nor any opinion expressed, constitutes a solicitation of the purchase or sale of any securities or commodities.

(C) Copyright 1983, Bloomberg L.P. The BLOOMBERG, Bloomberg L.P., and Bloomberg Financial Markets are trademarks, trade names, and service marks of Bloomberg L.P.

Bloomberg L.P. New York: 212-980-7000 London: 71-256-9010 Sydney: 2-238-2191 Tokyo: 3-578-1625

41169-1
C.

LAW OFFICES
ORRICK, HERRINGTON & SUTCLIFFE
599 LEXINGTON AVENUE
NEW YORK, NEW YORK 10022
TELEPHONE (212) 326-8800
TELECOPIER (212) 326-8900

SAN FRANCISCO, CALIFORNIA 94111
400 SANSOME STREET
TELEPHONE (415) 392-1122

SACRAMENTO, CALIFORNIA 95814
555 CAPITOL MALL
TELEPHONE (916) 447-9200

LOS ANGELES, CALIFORNIA 90011
333 SOUTH HOPE STREET
TELEPHONE (213) 680-7000

January 30, 1990

Maxine Gillman, Esq.
Municipal Assistance Corporation
for The City of New York
Suite 8901
One World Trade Center
New York, New York 10048

Dear Maxine:

You have requested that I advise you regarding whether federal arbitrage rebate requirements apply to the earnings on investments attributable to amounts deposited to the Bond Service Fund established with respect to the bonds issued by the Municipal Assistance Corporation for The City of New York (the "Corporation").

As you are aware, the rebate requirements of Section 148(f) of the Internal Revenue Code of 1986 (the "Code") apply generally to bonds of the Corporation issued after August 15, 1986. However, Section 148(f)(4) of the Code, as originally enacted by the Tax Reform Act of 1986, provided that, unless the issuer otherwise elected, any amount earned on a bona fide debt service fund shall not be taken into account in determining the issuer's rebate requirement if the gross earnings on such fund for the bond year is less than \$100,000. This exception is applicable to investments in the Bond Service Fund securing the Corporation's bonds, which Fund constitutes a bona fide debt service fund, to the extent the gross earnings in such Fund are less than \$100,000 for the applicable bond year. The Corporation did not elect to not apply this rule.

Section 148(f)(4) of the Code was amended pursuant to Section 6181 of the Technical and Miscellaneous Revenue Act of 1988 ("TAMRA") to provide that, with respect to bonds issued after November 11, 1988, the rebate exception for a bona fide debt service fund shall apply without regard to the \$100,000

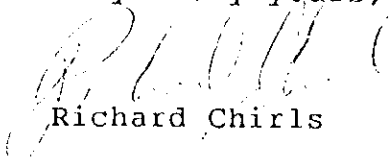
ORRICK, HERRINGTON & SUTCLIFFE

gross earnings limitation and without any opportunity for the issuer to elect otherwise with respect to any bond which is not a private activity bond if the average maturity of the issue is at least 5 years and the bond does not provide for a variable rate of interest. Accordingly, the Corporation's Series 68 Bonds are subject to this amended rebate rule. Therefore, the Corporation will not take into account any investment earnings on amounts deposited to the Bond Service Fund attributable to the Series 68 Bonds in determining the rebate liability. This rebate exception is applicable regardless of whether the gross earnings on such amounts exceed \$100,000 in any bond year.

Section 6181(c)(2) of TAMRA provides further that with respect to bonds (other than private activity bonds) outstanding as of November 11, 1988, the issuer may make a one-time election to apply the amendments to Section 148(f)(4) to amounts deposited after such date in bona fide debt service funds of such bonds. Accordingly, the Corporation may wish to make an election to exclude from the rebate calculation any deposits to the Bond Service Fund made after November 11, 1988 attributable to the Corporation's Series 60 Bonds through Series 67 Bonds regardless of whether the gross earnings on such amounts exceed \$100,000 in any bond year. It appears that such election need not be made until the first rebate payment is made to the federal government with respect to any such Series of Bonds.

Please call me if you have any further questions regarding this matter.

Very truly yours,



Richard Chirls

cc: D. Robinson
K. McDonough