****

**FY 2013 Federal Budget Proposal: Potential Impact on Bonds, Issuers, and Investors**

President Obama released his FY2013 federal budget this morning. It proposes $3.8 trillion in federal spending with a budget deficit of $901 billion. The budget estimates that debt held by the public will increase in FY 2012 (the fiscal year we are in) by $1.45 trillion and in FY 2013 by $1.06 trillion. Congress will begin holding hearings on the budget proposal next week, but legislative action to enact any or all of the budget proposals may take time.

Following is a breakdown of proposals in the budget proposal that impact bonds, issuers, and investors:

**Proposals Impacting Tax Treatment of Bonds**

* Limits the value of itemized deductions—including tax-exempt interest—to 28 percent. For single taxpayers with annual income over $200,000 and married taxpayers with annual incomes over $250,000 the Administration’s proposal would limit the tax rate at which high-income taxpayers can reduce their tax liability to a maximum of 28 percent. This limit would apply to most deductions (including itemized deductions, tax-exempt interest, foreign excluded income, employer-provided health insurance, retirement contributions, and selected above-the-line deductions). It would also include tax-exempt interest.
* Build America Bonds. The Administration again proposes reinstating BABs at 30 percent for 2013 and 28 percent thereafter and allow BABs to be used for purposes other than capital financing.
* Current Refundings. The budget proposes allowing current refundings of all bonds if the principal amount of the current refunding bonds is no greater than the outstanding principal amount of the refunded bonds and the weighted average maturity of the current refunding bonds is no longer than the remaining weighted average maturity of the refunded bonds.
* Arbitrage. First, the Administration proposes to unify the arbitrage restrictions to rely primarily on the rebate requirement and to repeal yield restriction in most circumstances. Second, recognizing that limited arbitrage potential exists if issuers spend bond proceeds fairly promptly, the Administration proposes a streamlined broad three-year prompt spending exception to the arbitrage rebate requirement on tax-exempt bonds. Finally, recognizing the particular compliance burdens for small issuers, the Administration proposes to increase the small issuer exception to the arbitrage rebate requirement from $5 million to $10 million, index the size limit for inflation, and remove the general taxing power constraint on small issuer eligibility.
* Mortgage Bond Targeting. The Administration proposes to simplify the targeting requirements for tax-exempt qualified mortgage bonds by repealing the purchase price limitation and the refinancing limitation.
* Unrelated or Disproportionate Use Limit. The Administration proposes to streamline the private business limits on governmental bonds by repealing the 5 percent unrelated or disproportionate private business limit.
* Repeals Bush Tax Cuts for Income over $200,000. The FY 2013 budget proposal repeals the 2001 and 2003 tax cuts for single taxpayers with annual income over $200,000 and married couples with incomes over $250,000.
* Uses the “Buffett Rule” as a substitute for the AMT. The Administration proposes that households with over $1 million in annual income pay no less than 30 percent of their income in taxes. The budget documents do not define whether “income” includes tax exempt income, but earlier reports indicated that it does not. This so-called “Buffett Rule” will replace the Alternative Minimum Tax. The proposal notes that accommodations will be made for households making large charitable contributions.

**Proposals Impacting Federal Spending Relating to Bonds**

Infrastructure Bank. The budget proposes a National Infrastructure Bank, financed by $10 Billion in federal funding in FY 2012. Funding would be awarded for large-scale ($100 Million minimum) transportation, water, and energy infrastructure projects that provide a public benefit and are self-sustaining through a dedicated revenue stream. Loans issued by the Bank could be up to 35 years in length and would represent a partnership between the federal government, private investors and state and local governments. The Bank would fund up to 50 percent of any project. This proposal is identical to earlier proposals made by the Administration.

**SEC Budget**

The President proposes increasing the SEC budget by $245 million to $1.566 billion. Among the stated uses of the funds is that the Division of Trading and Markets plans to enhance its oversight of market structure and operations, analysis of real-time market data, and economic analysis of proposed SRO rules to determine potential burdens on competition of proposed rule changes.

BDA will be closely monitoring congressional hearings on the budget proposal as well as counter-proposals offered in Congress. While we expect legislative progress on these proposals to be slow and drawn-out these proposals remain active ideas for the White House and Congress to pursue in the context of budget negotiations or elsewhere in the legislative process.

We hope this information is helpful. If you have any questions or need additional information, please contact Bill Daly at wdaly@bdamerica.org or 202-204-7902.