



RECOVERY ZONE FACILITY BONDS

Recovery Zone Facility Bonds (RZFB) are one of the new public finance tools created by the American Recovery and Reinvestment Act of 2009 (ARRA). (Please refer to our separate summary for information on Recovery Zone Economic Development Bonds.) On June 12, the Internal Revenue Service (IRS) issued written guidelines (Notice 2009-50) on the allocations of issuing authority and the use of these bonds. This summary offers our thoughts on the potential use of RZFB.

Q: What are RZFB?

A: Recovery Zone Facility Bonds are a tool for encouraging private investment in economic development and job growth. RZFB are a new type of qualified private activity bonds (think IDB). RZFB create the ability to use tax-exempt borrowing for a wide range of business development.

RZFB are subject to the general rules that apply to qualified private activity bonds, except: (1) RZFB have a separate allocation (volume cap) of issuing authority and (2) bond proceeds can be used to acquire existing property.

Q: What are the uses of RZFB?

A: The primary criteria is that 95% or more of bond proceeds must be spent on "recovery zone property". The IRS guidelines set three criteria for recovery zone property:

1. The property was constructed, reconstructed, renovated, or acquired by purchase by the taxpayer (the party borrowing and securing the bonds) after designation of the recovery zone.
2. The original use of the property commences with the taxpayer.
3. Substantially all use of the property occurs in the recovery zone and is the active conduct of a qualified business.

The "qualified business" provisions represent a key expansion of the use of private activity bonds. Essentially, the IRS guidelines allow any businesses that are not specifically excluded. The list of businesses that are not qualified businesses includes rental residential, golf courses, country clubs, massage parlors, suntan facilities, racetracks or other facilities used for gambling, or off-sale liquor stores.

Unlike conventional IDB, RZFB can be used to acquire existing property.

RZFB create the opportunity to use tax-exempt financing for commercial uses, owned housing and other private development not allowed under the rules for private activity bonds. RZFB could also be used for tax increment (or other municipal bonds) that would be private activity bonds.

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Q: Can I issue RZFB?

A: The answer to this question lies with both IRS guidelines and state law. The basic requirement under the IRS guidelines is that an issuer must have an allocation of the state volume cap equal to the amount of the bonds. It is important to recognize that RZFB is a federal designation. An issuer must also have statutory authority to issue the bonds. In Minnesota, this authority likely comes from the ability to undertake "projects" and issue bonds pursuant to Minnesota Statutes, Sections 469.152 to 469.165. These powers are given to cities and certain townships (M.S. 368.01). Counties are only authorized to undertake projects in areas outside of cities or these townships. These statutory requirements are particularly important because of the volume cap allocations given to Minnesota counties.

Q: Who has allocation to use RZFB?

A: The June 12 IRS Notice contained a list of allocations to local governments in each state. The Minnesota allocation went to two cities (Minneapolis and Saint Paul) and to 55 counties (see complete list on pages 3 and 4). Minneapolis, Saint Paul and these counties may directly issue and designate bonds as RZFB up to the amount of allocated volume cap. Instead of issuing bonds, these local governments may reallocate or waive all or part of its allocation.

Reallocation may be made to any entity that includes the city/county. Such entities could include the county's HRA/EDA/CDA, a city within the county, or the HRA/EDA/Port Authority of a city within the county. The decision to reallocate can be made "in any reasonable manner".

If the cities/counties decide not to directly issue or reallocate, then the allocated volume cap is waived. All waived volume cap is reallocated by the State. Any criteria for State reallocation have not been determined.

Q: What is a recovery zone?

A: The proceeds of RZFB must be spent to promote development or other activity in a designated "recovery zone". The IRS guidelines do not contain a detailed definition of a recovery zone. Instead, the criteria for a recovery zone must be pieced together from several parts of the guidelines.

- The guidelines specifically list three means of designation. (1) Issuers may designate a recovery zone as any area having "significant poverty, unemployment, rate of home foreclosures, or

general distress". (2) Economic distress caused by the closure or realignment of a military installation pursuant to the Defense Base Closure and Realignment Act of 1990 may be used as the criteria for a recovery area. (3) A recovery zone may be an empowerment zone or renewal community in effect as of February 17, 2009.

- The guidelines do not further define these factors other than to require that designation be "based on certain specified criteria".
- The only guidance on the designation process comes from the provision that any state or local government receiving a volume cap allocation may designate recovery zones "in any reasonable manner as it shall determine in good faith in its discretion".

This lack of specific guidelines means that the designation of recovery zones will be an evolving issue as issuers exercise this authority.

Q: What other factors apply to the use of RZFB?

A: Three factors in particular should be noted:

1. Activities financed with the proceeds of RZFB are not subject to federal prevailing wage rates.
2. Use of RZFB avoids the various caps/limits tied to small issue IDBs.
3. The bonds must be issued before January 1, 2011.

Q: What else do you need to know?

A: Unfortunately, the nature of the IRS guidelines mean that certain aspects of using RZFB will evolve over time. Here are some things to watch:

- How will the County decide to use or reallocate issuing authority?
- Will the State make waived issuing authority available to other local governments?
- How will the initial issues shape future use?

RZFB Allocations - Minnesota

Area	Recovery Zone		
	Residual	Economic Development Bond	Recovery Zone Facility Bond
Minnesota		132,154,000	198,231,000
Minneapolis city, MN		12,993,000	19,490,000
St. Paul city, MN		8,672,000	13,008,000
Aitkin County, MN		50,000	75,000
Anoka County, MN		11,466,000	17,200,000
Becker County, MN		914,000	1,371,000
Beltrami County, MN		0	0
Benton County, MN		457,000	685,000
Big Stone County, MN		0	0
Blue Earth County, MN		2,399,000	3,599,000
Brown County, MN		0	0
Carlton County, MN		675,000	1,013,000
Carver County, MN		3,021,000	4,532,000
Cass County, MN		398,000	597,000
Chippewa County, MN		0	0
Chisago County, MN		1,633,000	2,450,000
Clay County, MN		0	0
Clearwater County, MN		0	0
Cook County, MN		310,000	464,000
Cottonwood County, MN		12,000	18,000
Crow Wing County, MN		926,000	1,388,000
Dakota County, MN		13,966,000	20,949,000
Dodge County, MN		174,000	261,000
Douglas County, MN		189,000	283,000
Faribault County, MN		342,000	513,000
Fillmore County, MN		861,000	1,291,000
Freeborn County, MN		133,000	199,000
Goodhue County, MN		215,000	323,000
Grant County, MN		0	0
Hennepin County, MN	Residual	26,853,000	40,280,000
Houston County, MN		174,000	261,000
Hubbard County, MN		0	0
Isanti County, MN		1,291,000	1,937,000
Itasca County, MN		1,492,000	2,237,000
Jackson County, MN		0	0
Kanabec County, MN		248,000	371,000
Kandiyohi County, MN		522,000	783,000
Kittson County, MN		0	0
Koochiching County, MN		153,000	230,000
Lac qui Parle County, MN		130,000	195,000
Lake County, MN		0	0
Lake of the Woods County, MN		50,000	75,000
Le Sueur County, MN		808,000	1,211,000
Lincoln County, MN		0	0
Lyon County, MN		88,000	133,000
McLeod County, MN		0	0
Mahnomen County, MN		115,000	172,000
Marshall County, MN		0	0
Martin County, MN		0	0
Meeker County, MN		0	0

RZFB Allocations - Minnesota

Area	Recovery Zone	
	Economic Development Residual	Recovery Zone Facility Bond
Mille Lacs County, MN		920,000
Morrison County, MN		0
Mower County, MN		0
Murray County, MN		254,000
Nicollet County, MN		1,276,000
Nobles County, MN		0
Norman County, MN		0
Olmsted County, MN		1,268,000
Otter Tail County, MN		0
Pennington County, MN		0
Pine County, MN		0
Pipestone County, MN		0
Polk County, MN		0
Pope County, MN		0
Ramsey County, MN	Residual	7,770,000
Red Lake County, MN		430,000
Redwood County, MN		613,000
Renville County, MN		0
Rice County, MN		77,000
Rock County, MN		209,000
Roseau County, MN		242,000
St. Louis County, MN		4,059,000
Scott County, MN		4,445,000
Sherburne County, MN		2,933,000
Sibley County, MN		0
Stearns County, MN		1,665,000
Steele County, MN		0
Stevens County, MN		197,000
Swift County, MN		601,000
Todd County, MN		525,000
Traverse County, MN		180,000
Wabasha County, MN		192,000
Wadena County, MN		0
Waseca County, MN		0
Washington County, MN		7,773,000
Watonwan County, MN		483,000
Wilkin County, MN		230,000
Winona County, MN		106,000
Wright County, MN		3,976,000
Yellow Medicine County, MN		0