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Services

[Public Finance Tax](#)

Proposed Regulations Affect Arbitrage Rules for Tax-Exempt Bonds

On March 12, 2026, the United States Treasury Department and the Internal Revenue Service published proposed regulations (the “Proposed Regulations”) affecting the arbitrage bond provisions of Section 148 of the Internal Revenue Code of 1986 (the “Code”) and the Treasury Regulations thereunder (the “Regulations”). The Proposed Regulations are available under [REG-117298-21](#) in the Federal Register. We are evaluating the potential impacts of the Proposed Regulations on existing and future tax-exempt bond issuances and will provide updates to clients as warranted. Members of our [national public finance tax group](#) will work closely with industry associations to provide comments to the Treasury Department regarding the Proposed Regulations.

The caption of the Proposed Regulations suggests the Proposed Regulations address “Guidance on Tax-Exempt Refunding Bonds.” However, the refunding guidance in the Proposed Regulations is modest, as most of the Proposed Regulations address matters other than refundings. The following is a summary of certain provisions contained in the Proposed Regulations.

1. [Restricting Certain Allocations of Proceeds to Expenditures](#)

The Proposed Regulations would limit allocations of bond proceeds in transactions involving multiple funding sources unless such other sources are on hand at the time an expenditure is paid. For issuers and participants in housing transactions or transactions where bonds represent only a portion of the funding mix, the Proposed Regulations may complicate the allocation of proceeds to expenditures that are appropriate under the Code. The scope of the Proposed Regulations is limited to Section 148 of the Code, suggesting that this change in law may not be intended to apply to certain other provisions affecting tax-exempt bonds. We will continue to review the impact of this proposed change on issuers and believe particularly issuers of housing bonds and those involved in structuring housing transactions should take note of the potential change to the allocation rules.

2. [Existing Positive Guidance Incorporated in Regulations](#)

The Proposed Regulations would cement the helpful guidance in Notice 2024-32 which provides that bonds issued to refinance existing loans and cross-calling bonds with loan repayments in student loan and single-family financings will not result in refunding treatment. See our [client alert regarding Notice 2024-32](#) for a discussion of these provisions. The Proposed Regulations do not make any changes to the guidance already provided in such notice, and we do not believe the Proposed Regulations will impact existing structuring approaches.

3. [Additional Time for Recovering Overpayments of Rebate](#)

The Proposed Regulations would extend the deadline for filing a request for the refund of rebate overpayments to up to the later of two years after (1) 60 days after the final computation date of the issue to which the payment relates, or (2) the date the payment was made to the

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federal government with respect to the portion of an overpayment paid more than 60 days after the final computation date. This is a helpful change that should prove useful to issuers requesting refunds of rebate overpayments.

4. Clarification on Valuing Investments in Refundings

The Proposed Regulations note that questions have arisen as to the meaning of the phrase “arbitrage restrictions” when valuing investments for transferred proceeds in refundings, and whether such phrase is limited to the yield restriction rules and not the rebate requirements of Section 148 of the Code. The Proposed Regulations would clarify that the phrase is intended to refer to all requirements of Section 148 of the Code. This is a particularly technical clarification with perhaps little practical use or impact to many clients.

5. Relief for Demand Deposit SLGS

Section 1.150-1(b) of the Regulations treats the investment of gross proceeds in Demand Deposit State and Local Government Series investments (Demand Deposit SLGS) as an investment in “tax-exempt bonds.” This means that, for certain purposes of the arbitrage rules, the investment in Demand Deposit SLGS is not subject to yield restriction and may satisfy certain safe harbor provisions such as the safe harbor for longer-term working capital financings. Under existing rules, the Treasury Department may convert such Demand Deposit SLGS into special 90-day certificates of indebtedness if the Treasury Department deems this necessary to address considerations relating to the federal statutory debt limit. The Proposed Regulations would confirm that, even if Demand Deposit SLGS are converted into such 90-day certificates, the certificates continue to qualify as “tax-exempt bonds.” This change represents a helpful confirmation of what many practitioners have already believed the rule should be.

This client alert was prepared by Kutak Rock’s [national public finance tax group](#). Please reach out to any member of the group listed if you have questions about the Proposed Regulations and their impact on tax exempt bond financings. You may also visit us at www.kutakrock.com.

