IRS eases golf course management constraints

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By ANGELO PALERMO

Thanks to a recent Internal Revenue Service ruling relative to golf facilities financed by tax-exempt municipal bonds, marriages between municipal golf courses and golf course management firms are likely to be occurring with much greater frequency in the years ahead. It also enhances the chances of success for those who've already tied the knot.

Issued January 10, the new ruling (Revenue Procedure 97-13) went into effect May 15 of this year. It superseded earlier IRS rulings that had been in effect since 1986. Among other things, the old rulings contained a number of provisions that have fostered short-range thinking and carried constraints that have not allowed many public/private management partnerships to fully take root and blossom.

To the new ruling, for example, the IRS had stipulated that the terms of these agreements could not exceed five years and that municipalities, if they wished to do so, could terminate these contracts without financial penalty after only three years. Conditions like these have discouraged many management companies from undertaking capital improvements and other long-term efforts to improve in the operation of the facilities they're managing.

Under the new ruling, the ceiling on the term of such contracts has been extended up to 15 years. It also softens the "cancelation without compensation" provisions in the old law and liberalizes some of the old formulas that were used to calculate the various ways in which management firms could be compensated.

The new ruling affects current as well as future management agreements. For example, a municipality with a golf course now being operated under a five-year management agreement can extend that agreement for up to another 10 years.

The new compensation formulas will stabilize fees for these longer-term agreements. More specifically, fee payments to those management companies that land 15-year contracts must — under the new ruling — be at least 95 percent "periodic fixed fee." This means that 95 percent of the fee must be a stated dollar amount each month. Under the old ruling, only 50 percent of the management fee had to be predetermined at a fixed rate.

For 10-year agreements, at least 80 percent of the management fee must now be periodic fixed fee. In all cases, automatic increases in these fees may be tied to increases in the Consumer Price Index and other such external factors that are not linked directly to the financial performance of the golf facility.

The impact of these changes will be far reaching for both municipalities and management firms. For example, knowing that they no longer have to renegotiate their management contracts every five years may encourage more municipalities to consider the option of retaining a professional management firm. Management firms also now have a greater opportunity to build their business portfolios and to do so at less financial risk.

The new IRS ruling should also increase municipal bond-buyer confidence because municipalities that choose to retain a management company can now offer bond holders the added degree of certainty that comes with a long-term management agreement.

For more information on the new ruling and/or a copy of Procedure 97-13, contact Lorreta J. Finger in the IRS's Office of Assistant Chief Counsel for Financial Institutions and Products. She can be reached in Washington, D.C., at 202-622-3880.