NATIONAL ASSOCIATION OF STATE TREASURERS

April 10, 2020

VIA Electronic Mail

The Honorable Mitch McConnell
Majority Leader
U.S. Senate
317 Russell Senate Office Building
Washington, D.C. 20510

The Honorable Nancy Pelosi
Speaker
U.S. House of Representatives
1236 Longworth House Office Building
Washington, D.C. 20515

The Honorable Chuck Schumer
Minority Leader
U.S. Senate
322 Hart Senate Office Building
Washington, D.C. 20510

The Honorable Kevin McCarthy
Minority Leader
U.S. House of Representatives
2486 Rayburn House Office Building
Washington, D.C. 20515

RE: State Finances and COVID-19 Response

Dear Majority Leader McConnell, Speaker Pelosi, Minority Leader Schumer, and Minority Leader McCarthy,

On behalf of the State Treasurers and state financial officials we represent, we applaud your efforts to respond to the COVID-19 public health and economic emergency. We appreciate your tireless efforts and acknowledgement of the role states play in combating this pandemic — both in terms of public health and economic stability. We now write to you urging the passage of additional measures to provide targeted and temporary relief to states and local governments as they continue to serve on the front lines of our national response to this outbreak.

The National Association of State Treasurers (NAST) and our members continue to focus on five areas of economic impact, which stem from the COVID-19 emergency disaster declaration. We have organized this letter, as well as our continuing advocacy and member education efforts, into these five categories:

- **Decreased revenues** resulting from stay-at-home orders and general decline in economic activity, both of which are exacerbated by the lack of certainty on the duration and scope of this public health crisis;

- **Delayed revenues** resulting from the Internal Revenue Service's (IRS's) three-month extension of the filing deadline for federal income taxes, along with concomitant three-month extensions of state filing deadlines;
- **General and widespread market volatility and dislocation** resulting from an unprecedented cash crunch and selloff;
- **Increased COVID-19-related expenditures** resulting from state response efforts; and
- **Need for general economic stimulus** to sustain the American economy and ensure it emerges with stability and strength once the crisis and emergency declaration subside.

State Treasurers depend on the efficient municipal bond market that has historically served as the critical backbone of state and local finance, but which has recently encountered turbulence resulting from this unprecedented crisis. Above all else, State Treasurers want to see our existing capital markets quickly normalized. As the crisis continues, the challenges facing states will likely evolve and additional considerations may be needed.

Decreased Revenues

To date, forty-five states are under some degree of stay-at-home orders and millions of businesses have temporarily closed or reduced operations. Decreased revenues resulting from stay-at-home orders and general economic malaise continue to pose one of the largest threats to the business community, as well as to state and local governments. The revenue compositions of states vary greatly across the nation, but on aggregate elastic sources that face greater exposure to economic downturns made up more than an estimated 36 percent of state general tax revenues in the second quarter of 2019.[1] For some states, this portion is significantly higher.

Unlike inelastic revenues such as income tax that are merely delayed, relatively elastic revenues such as sales and excise tax receipts as well as fares, fees and tolls have and will continue to face immediate declines as a result of business shutdowns and declining commerce. As the crisis continues, revenue sources such as income taxes will also begin to fall as receipts begin to reflect furloughs and rising unemployment rates. The situation is particularly challenging for states as the duration of the declining state of activity is unknown, and states will likely need to retain certain of their reserves for a potential recession that may continue well beyond the end of the emergency declaration.

Easing the financial burden of these lost revenues would free up states to maintain critical levels of employment and better focus on their primary responsibility — combatting the spread of COVID-19. The CARES Act generously provided states and local governments with $150 billion in aid, but these funds are restricted to increased and unbudgeted expenses resulting from

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[1] Including state taxes nationally levied on sales and gross receipts, alcohol, tobacco, motor vehicles, and fuel. Analysis of data found in the "Quarterly Summary of State and Local Government Tax Revenue for Second Quarter 2019." *U.S. Census Bureau.* Web access: https://www.census.gov/content/dam/Census/library/publications/2019/econ/g19-qtax2.pdf

their efforts to combat the pandemic. While these funds are both appreciated and vital, they do not address the equally if not greater fiscal threats posed by declining revenues. As such, Congress and the Administration should consider the following:

- **Provide appropriations for direct and less restrictive aid to states** for the purpose of covering revenues anticipated to be lost as a result of COVID-19. Longer term solutions may be needed depending on the duration of the crisis, but an immediate infusion would greatly alleviate the financial pressures of extending stay-at-home orders and carrying out other Centers for Disease Control (CDC) guidance.

- **Remove matching requirements** for state and local governments receiving federal grants from existing programs.

- **Ease Internal Revenue Code (IRC) and Internal Revenue Service (IRS) restrictions** on the use of tax-exempt borrowing proceeds for cash flow and create a federal guarantee program to ensure market access for issuers.

- **Temporarily permit tax-exempt borrowing for working capital** for bonds and notes issued to cover lost revenues and extend these provisions to all issuers, including instrumentalities and tolling/fare-charging facilities.

While some degree of budget cuts will likely be necessary, without compensating for the current volume of projected lost revenues many states may contemplate larger layoffs and furloughs to comply with balanced budget requirements during a time where unemployment is already historically high.

Delayed Revenues

On March 21, the IRS postponed the filing date for 2020 income taxes from April 15 to July 15.[2] For a number of statutory and political reasons, the IRS's action triggers concomitant postponements for state and local filings as well. State and local governments want to support the Federal Government's efforts to increase liquidity in the markets and put cash into the hands of American households. Many state and local governments continue to contemplate plans to postpone filing and payment deadlines for other sources of revenues, including those for state and local property taxes. Unlike the federal government, many state and local governments have fiscal years that end on June 30, which means postponing revenue receipts beyond that deadline will have additional consequences for our budgets.

We continue to work with the Federal Reserve and U.S. Department of Treasury on implementing section 4003(b)(4) of the CARES Act. We were pleased by the Federal Reserve's recent announcement to create the Municipal Liquidity Facility.[3] Many details remain, but we hope the facility will provide sufficient liquidity to meet potentially abnormal volumes of state-

[2] IRS Notice 2020-18. March 21, 2020. Web access: www.irs.gov/pub/irs-drop/n-20-18.pdf
[3] Board of Governors of the Federal Reserve System. April 9, 2020. Web access: https://www.federalreserve.gov/newsevents/pressreleases/monetary20200409a.htm

issued tax and revenue anticipation notes (TRANs) that might be issued as a result of the extension to the IRS tax filing deadline. We look forward to working with the Federal Reserve as it endeavors to implement this and other potential facilities to support the fiscal health of our state and local governments as they continue to serve on the frontlines of responding to this crisis.

General and widespread market volatility and dislocation

The secondary municipal market has remained volatile since mid-March. Outflows from municipal funds have slowed but continue to distort the market. Meanwhile, many primary issues have come to a standstill with some small volume of issues advancing on a day-to-day calendar basis. Immediately following the passage of the CARES Act, the municipal markets generally rallied on the anticipation that the Federal Reserve would create a program directed at alleviating pressures throughout the secondary market. Since then, the market has remained icy and incremental progress is largely attributed to market expectations that such Federal Reserve action will come.

Among our recommendations to Treasury and the Federal Reserve was to create such a temporary purchasing program to buy a diverse array of municipal bonds in the secondary market to alleviate pressures and stabilize market conditions to a point where demand for essential primary issues is normalized.[4] We remain concerned that failing to meet market expectations could risk additional dislocation. For these reasons, we continue to advocate that Section 4003 of the CARES Act provides sufficient authority and indicates congressional intent for the Federal Reserve to create such a facility. Such action remains necessary to normalize our vital markets.

Increased COVID-19-Related Expenditures

As mentioned, we especially appreciate the provision of $150 billion to state and local governments for COVID-19-related expenses under Section 5001 of the CARES Act. These funds are helpful, and much appreciated by State Treasurers. NAST continues to await guidance from the U.S. Treasury on a number of questions relating to these funds, including: how section 5001 funds will be allocated and distributed to states, what are eligible COVID-19 related expenses, and how funds can be managed. More funding for emergency response may be needed depending on the duration and extent of the crisis. Given the complexity of both the public health and financial challenges facing states, we recommend the widest degree of latitude in the definition of COVID-19 related expenses.

Need for general economic stimulus

The magnitude and duration of this crisis remain uncertain, but we acknowledge a degree of economic stimulus outside of direct COVID-19 response efforts will be needed to ensure the

[4] https://nast.org/wp-content/uploads/NAST-4003-Facilities-Letter-FINAL.pdf

economy can effectively "restart" once the crisis has subsided. Market uncertainty and economic contraction will likely persist beyond the end of the emergency declaration, so we feel it is critical now to urge consideration of additional stimulus measures. As such, Congress and the Administration should consider the following:

- **Facilitate the return of matured unredeemed federal savings bond proceeds to their rightful owners,** by equipping states with the tools, records and proceeds needed to match holders of federal savings bonds with their rightfully owed funds (approximately $26 billion) at a time when it is most needed. *See Unclaimed Savings Bond Act (S. 2417 / H.R. 5269*).

- **Provide relief to states via the Unemployment Trust Fund** by temporarily waiving interest payments for states that borrow from the fund, similar to provisions included in Section 2004 of the American Recovery and Reinvestment Act. *See P.L. 111-5*.

- **Restore tax-exempt advance refunding bonds** to equip states to better weather rapidly changing interest rate environments and enhance access to much-needed capital for critical infrastructure projects.

- **Raise (at least temporarily) the bank qualified debt threshold from $10 million to $100 million,** which would greatly aid small, local issuers by making their securities more attractive to community and regional investors who cannot otherwise deduct the cost of carrying such issues.

- **Reclassify qualifying 2B municipal bonds as level 2A high quality liquid assets (HQLA)** to further open up the market for municipal securities to large institutional investors who may otherwise be reaching asset caps.

- **Restore direct subsidy bonds and remove sequestration on both future and existing issues (Build America Bonds)** to provide a broader purchasing base for municipal bonds issued to finance critical infrastructure.

- **Eliminate the cap on Private Activity Bonds (PABs) for single- and multifamily housing** that ensure financing for affordable housing in the post-crisis era is readily available.

- **Pause all federal rulemaking and the implementation of new rules not related to COVID-19** until the National Emergency Declaration has ended and extend the same provision to self-regulated organizations (SROs) (such as the Municipal Securities Rulemaking Board (MSRB)), and encourage other entities and 501c3s (such as the Governmental Accounting Standards Board (GASB)), which create rules and accepted standards, to voluntarily pause nonessential rulemaking and standards setting processes.

We appreciate your attention and consideration on these matters of critical importance to state finance. Please consider NAST and our membership as a resource as you continue to work on efforts to stabilize the economy and support state and local government. I have asked our Policy Director, Brian Egan (brian@statetreasurers.org | 202-630-1880) to answer any questions you may have relating to this letter or otherwise. Thank you again and please stay well during these challenging times.

Sincerely,

Shaun Snyder
Executive Director
National Association of State Treasurers

CC:

- Members of the United States 116th Congress
- The Honorable Steven Mnuchin, Secretary of the U.S. Department of Treasury
- The Honorable Jerome Powell, Chairman, Board of Governors of the Federal Reserve System
- Members of the Federal Reserve Board of Governors