# Bond Case Briefs

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## Treasury Rescue Won't Bail Out Chicago, New Jersey From Debt.

**• American Rescue Plan funds can't pay debt service: Treasury**
**• Illinois, Chicago and New Jersey pitched paying down debt**

The U.S. Treasury Department is sending a message to states and cities that the billions in aid from the American Rescue Plan should provide relief to residents, not their governments' debt burdens.

The department on Monday released guidance on how state and local governments can use $350 billion in funding from President Joe Biden's $1.9 trillion rescue package. The funds are intended to help states and local governments make up for lost revenue, curb the pandemic, bolster economic recoveries, and support industries hit by Covid-19 restrictions. In a surprise to some, these funds can't be used for debt payments, a potential complication for fiscally stressed governments that had already etched out plans to pay off loans.

"It does mean some state and local governments will have to rethink," Eric Kim, an analyst for Fitch Ratings, said in an interview on Tuesday. While "$350 billion is a lot of money," some of the restrictions "were maybe not anticipated."

Biden's rescue package seeks to shore up the finances of states and municipalities that have been on the front lines of the government response to the outbreak. While municipal tax collections initially plunged at the start of the pandemic, the majority of U.S. states have seen revenue recover to pre-pandemic levels. That's left governors and mayors grappling with how to best spend the aid. Several officials, including leaders in Illinois, Chicago and New Jersey, had considered using the funds to pay back loans, but this week's guidance muddles those plans.

"Expenses related to financing, including servicing or redeeming notes, would not address the needs of pandemic response or its negative economic impacts," according to a document from the Treasury. "Such expenses would also not be considered provision of government services, as these financing expenses do not directly provide services or aid to citizens."

Illinois Governor J.B. Pritzker had suggested using some of the state's $8.1 billion in aid to repay the outstanding $3.2 billion in debt from the Federal Reserve's emergency lending facility and to reduce unpaid bills. Illinois was the only state to borrow from the Fed last year, tapping it twice. On Tuesday, Jordan Abudayyeh, a Pritzker spokesperson, said the administration is "seeking clarification" from the Treasury on whether Illinois can use the aid to pay back the loan from the Fed.

"We need to act responsibly with these dollars," Pritzker said during a press conference Tuesday. "I believe this is an important step toward putting our state's fiscal house in order."

Before the release of the guidance, Chicago Chief Financial Officer Jennie Huang Bennett had proposed using some of the city's nearly $1.9 billion from the rescue package to pay off debt taken to close its 2020 deficit. The "guidance represents interim rules that have been put out for comment," and the city plans to seek clarification and offer comment, according to an emailed statement from the city's budget office.

"These regulations, if not a surprise, certainly make it more difficult for the state of Illinois and city of Chicago to pay down the borrowing," said Laurence Msall, president of the Civic Federation, a local watchdog group.

The rule could also affect New Jersey, which sold nearly $3.7 billion of bonds last year to cover its shortfall during the pandemic. Assembly Republican Leader Jon Bramnick, a Republican, in April had called for Governor Phil Murphy, a Democrat, to use some of the federal aid to pay down the state's debt.

"The guidance is interim and not yet final, and we will continue to evaluate the allowable uses of ARP funds in conjunction with State needs," said Melinda Caliendo, a spokesperson for the state treasury.

The Treasury rules also restrict using the aid to replenish reserves or rainy day funds. Industry groups are taking a close look and planning to give feedback to the Treasury on its guidance and the department is asking for comments on its 151-page document on the interim rules for the funds.

"It's a living, breathing document," said Irma Esparza Diggs, director of federal advocacy at the National League of Cities, who said the group is looking at those restrictions and will be talking to its members throughout the coming weeks.

For states such as Illinois that want to use the money for debt repayment, the large amount of federal aid still gives them "ample" opportunity to do what investors want to improve creditworthiness, said Ty Schoback, a senior municipal research analyst for Columbia Threadneedle Investments.

"We know that within state and local budgets, sources and uses are fairly fungible," Schoback said. Relieving budget pressure in one area with federal aid can open up resources for other items while remaining fully compliant for the intended use, he said. "I don't think they will have any trouble."

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