October 12, 2020

The Honorable Steven Mnuchin
Secretary of the Treasury
Main Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

The Honorable Jerome Powell
Chair of the Board of Governors
The Federal Reserve
20th Street Constitution Avenue, N.W.
Washington, D.C. 20551

Dear Secretary Mnuchin and Chairman Powell,

On behalf of the state and local governments and finance officials that we collectively represent, we acknowledge the actions taken by the Administration, the Federal Reserve and Congress to stabilize our markets through this COVID-19 crisis. On October 5, 2020, the Federal Reserve amended the Municipal Liquidity Facility FAQs to require eligible governments to submit notice of interest to participate in the facility 30 days prior to facility close date. This taken together with an effective termination of future federal stimulus discussions are actions we consider to be excessively punitive in an environment when states and local governments are gauging the stark realities of revenue declines in FY2021 budgets.

States and local governments have been and will continue to serve on the frontlines of this national crisis. As you know, an historic cash event, prolonged paralysis in bond markets, and impending budget shocks stemming from the pandemic have all culminated at once, forcing many businesses and nearly every state and local government into a state of damage control. **Our primary advocacy with our federal legislators based on current fiscal conditions is for additional unencumbered direct funding to plug budget shortfalls and projected losses in revenues resulting from slowed commerce.** Our advocacy extends to support the municipal debt market, where state and local government access to credit and budgets will be further stressed at the most inopportune time, particularly as revenues decline as a result of business closures and rising unemployment.

We wish to see the municipal credit markets normalized now and into 2021. To that extent, we wish to be a resource for you as we enter a new phase of our nation's economic history challenged with significant revenue decline and untenable market conditions. We also wish to provide recommendations to augment the facility already in place that seeks to provide stability in the market accessible to state and local governments.

The Municipal Liquidity Facility

On April 9, 2020, the Federal Reserve announced the "Municipal Liquidity Facility (MLF)," which will provide direct, short-term lending to eligible state and large local governments. The facility was greatly expanded on April 27, to include a larger universe of eligible local issuers and multistate entities. The MLF is a critical, historic and necessary first step in supporting larger issuers access to credit for cash flow needs, particularly as they faced delayed income tax revenues resulting from the IRS's decision to delay tax filing deadlines and the inevitable drop in revenues caused by the nationwide shutdown. We applaud the Federal Reserve's announcements regarding the MLF and appreciate its immediate positive impacts to issuers accessing credit markets over the past few months. We also commend the Federal Reserve's responsiveness and consideration to the issuer community's input as it has built upon and improved various iterations of the facility. However, the FAQ amendment effective October 5, 2020 speeds up the timeline for eligible entities to access the facility at an inopportune time.

We offer the following suggestions to improve the Facility and its responsiveness to issuers of governmental securities provided the current economic realities of providing essential public services.

Extension of the Origination Deadline of December 30, 2020

Forecasts from economists broadly agree that the recession-effects of necessary shutdowns will have a lagging effect that will last well into 2021. An extension of the MLF's origination period into 2021 would very likely mean more access for issuers who need it most. We also request significant lead-time for the termination period considering the newly required 30-day submission requirement for the notice of interest for any entity accessing the MLF.

Provide Access to a Variety of Issuers

This pandemic has different revenue and expenditure effects on different types of issuers and it will continue to have a profound impact on the financial condition of governmental units that will continue to serve on the frontlines of this national crisis. Expanding the facility to include an expansive network of essential public services providers will help to underpin the infrastructure we use keep the country running.

Expand Structure and Use of Proceeds

The MLF's 36-month term should be lengthened and borrowers should have greater flexibility on the use of proceeds. Many states in the US have either constitutional or policy restrictions that limit governmental entities from borrowing for operating capital needs. Most eligible entities would require constitutional amendments or substantial policy changes at the state level to access the MLF. Both options are highly formidable tasks even under non-pandemic conditions. For eligible entities that are able to borrow for operating capital, the short-term maturities of MLF loans risks entities facing insurmountable principal repayments or having to rollover debt into existing markets during a time at which markets will likely remain fragile. Most economists agree that the economic recovery will stretch over several years.

Providing entities with the ability to amortize the repayment of MLF loans over terms greater than 36-months (ideally up to 10 years), and increasing the flexibility on the use of proceeds would ease both of these concerns. Making these changes to the MLF will also help jurisdictions make investments that could provide long-term benefits for communities. The needs and strengths of every community differ; thus, the pandemic and economic crisis will play out differently for each state and local government. The Federal Reserve should allow for a broad use of the proceeds to allow jurisdictions to utilize them in ways that best suit their needs.

Eliminate Punitive Pricing

The Federal Reserve should reconsider the impact of penalty pricing to participate in the MLF. Should market conditions change, as they surely will, the Federal Reserve should carefully consider whether the MLF is continuing to support state and local governments as intended by Congress. Provided this policy objective, we would encourage the Fed to refine its pricing structures in a way that would not penalize an issuer.

Parity in Facilities Offered to the Private and Public Markets

The Federal Reserve should create a facility to provide relief by purchasing municipal securities in the secondary market, similar to the secondary purchasing program in the Secondary Market Corporate Credit facility. The municipal bond market has recently improved, but these conditions are largely tied to the uncertain course of the ongoing pandemic. Issuers' access to credit remains fragile and volatile. Issuers remain concerned that a new wave of COVID-19 cases and ensuing stay-at-home orders could result in a repeat of the gridlocked market conditions seen mid-March and necessitate additional Federal Reserve actions. Developing a special purpose vehicle aimed at purchasing municipal securities and providing relief to the secondary market should be considered. At a minimum, having such a facility developed in advance and at the ready to begin purchasing in the event of a second market selloff would rapidly provide much needed stability to our fragile markets. We believe such a facility is in line with the congressional intent of Title IV of the CARES Act (P.L. 116-136) and note congressional letters supporting the issue.[1, 2]

Relief to Smaller, Less Frequent Issuers

Finally, we recommend exploring additional ways to enhance the ability for smaller issuers to access capital. We believe that targeted easing of capital requirements along with minor changes to the U.S. Tax Code would further strengthen access to bank loans and lines of credits for smaller issuers. Often in smaller communities, the bank relationship between an issuer and the community bank is the primary source of capital. Limitations on the deductibility of carrying costs as well as stressed capital requirements and asset caps placed on banks constrain their ability to meet the credit needs of small issuers. GFOA, USCM, NLC, NACo and ICMA have supported bipartisan legislative efforts like the "Municipal Bond Market Support Act of 2019" (H.R. 3967), which would greatly expand the number of small issuers eligible to issue "bank qualified debt" and provide an additional purchaser in our markets to further diversity sources of credit to state and local governments.

Conclusion

Without timely and strong federal government efforts to support the municipal bond market and compensate for delayed revenues, our state and local governments will be forced to take actions that will exacerbate economic contraction and offset the vital stimulus that Congress, the Federal Reserve, and the Administration have worked to provide. Our consistent and overarching request from our federal legislators is for direct, unencumbered funding to ensure stability in in this environment where revenues are falling drastically short. Our advocacy extends to support the municipal debt market, where state and local government access to credit will be further stressed at the most inopportune time. We urge you to consider using your authority provided in Title IV of the CARES Act and existing powers under Section 13 of the Federal Reserve Act to develop and refine facilities like those outlined above in order to counter the unprecedented impacts of current market uncertainty.

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[1] "Letter from Congressman Steve Stivers, Dutch Ruppersberger et. al. Calling for Support for the Secondary Municipal Bond Market." May 1, 2020. See attached.

[2] "Letter from Senator Robert Menendez, Thom Tillis et. Al. Encouraging the Treasury and the Federal Reserve to Take Further Action to Stabilize the Municipal Bond Market." May 14, 2020. See attached.

Sincerely,

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Cc: Members of the Federal Reserve Board of Governors
Federal Reserve Bank of New York
Members of the United States House of Representatives
Members of the United States Senate