NLC DELIVERS

May 21, 2021

Coronavirus Local Fiscal Recovery Funds Guidance:

Prohibited Expenditures

On May 10, the U.S. Treasury released an Interim Final Rule to provide guidance on cities, states and tribal governments can spend funds allocated to them by the American Rescue Plan Act ("ARPA"). The guidance is effective immediately and summarizes the prohibited uses of the funds.

In Sections 602(c)(1) and 603(c)(1) of ARPA, Congress provided four eligible uses of funds:

a) To respond to the public health emergency or its negative economic impacts, including assistance to households, small businesses, and nonprofits, or aid to impacted industries such as tourism, travel, and hospitality;

b) To respond to workers performing essential work during the COVID-19 public health emergency by providing premium pay to eligible workers;

c) For the provision of government services to the extent of the reduction in revenue due to the COVID–19 public health emergency relative to revenues collected in the most recent full fiscal year prior to the emergency; and

d) To make necessary investments in water, sewer, or broadband infrastructure.[1]

In general, any use of ARPA funds outside of these categories is prohibited. ARPA also includes explicit prohibitions on how the funds can be used. The prohibitions include:

a) Depositing funds into any pension fund.
b) Using funds to directly or indirectly offset a reduction in the net tax revenue of [the] State or territory resulting from a change in law, regulation, or administrative interpretation.

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[1] Interim Final Rule: Coronavirus State and Local Fiscal Recovery Funds, U.S. Department of Treasury (hereinafter "Treasury Guidance"), 7.

The Treasury Guidance provides additional clarifications on these prohibitions as summarized below. Despite these prohibitions, a City still has significant flexibility with how it spends the ARPA funds. The Treasury Guidance provides flexibility to use funds for programs and projects that are not expressly described in the Guidance, provided that it responds to the negative economic impacts of the COVID-19 public health emergency, and/or is designed to address an economic harm resulting from or exacerbated by the public health emergency.[2]

Spending on Projects Outside ARPA Timelines

The Guidance sets parameters on when funds can be used. The funds may be used for any allowed purpose starting on March 3, 2021, and must be encumbered by December 31, 2024. Funds that were encumbered during this period must be spent by December 31, 2026.[3] Use of funds for projets outside of these dates is prohibited. Funds not spent by the end of 2026 must be returned to the federal government.[4]

Pensions

Sections 602(c)(2)(B) and 603(c)(2) prohibit any recipient, including cities, non-entitlement units of government, and counties, from using Fiscal Recovery Funds for deposit into any pension fund. The prohibition is aimed at preventing cities from using the ARPA funds to make up deficits in their public employee pension funds that may be unrelated to the Pandemic.

Treasury interprets “deposit” to mean an “extraordinary payment into a pension fund for the purpose of reducing an accrued, unfunded liability.”[5] The Rule sets forth two criteria which preclude a payment as eligible assistance. A payment is not allowed into a pension fund if:

1. the payment reduces a liability incurred prior to the start of the COVID-19 public health emergency, and

2. the payment occurs outside the recipient’s regular timing for making such payments.

“Deposit” and “payroll contribution” are separate payments. A “payroll contribution” is when an employer makes “payments into pension funds on regular intervals, with contribution amounts based on a pre-determined percentage of employees’ wages and salaries.”[6] Payroll contributions are not prohibited, and are anticipated if they are made as part of an employee’s premium pay otherwise authorized under ARPA.[7]

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[2] Treasury Guidance 11.
[3] Treasury Guidance 122.
[4] Treasury Guidance 122.
[5] Treasury Guidance 71.
[6] *Ibid*.
[7] *Ibid*..

Infrastructure that does not meet ARPA Criteria

Not all eligible infrastructure projects are within the scope of the infrastructure investment category. Funding for infrastructure projects may be related to water, sewer, broadband or respond to a "specific pandemic public health need."[8]

Water and sewer projects are allowed if they would otherwise qualify for funding under the Clean Water Act and Safe Drinking Water Act state revolving fund programs.[9] These programs are broad and will capture a variety of different types of drinking water and water quality projects. However, the Treasury Guidance provides more specific criteria for broadband projects. For example, the Guidance states that broadband projects must target underserved areas.[10] Cities will need to make sure that their broadband projects meet the requirements in the Guidance or risk losing funding.

Rainy Day Funds, Financial Reserves, and Outstanding Debt

Funds may not be used for rainy day funds, financial reserves, or funds of a similar nature. Treasury deemed these funds to be ineligible because contributions "would not address these needs or respond to the COVID-19 public health emergency but would rather constitute savings for future spending needs."[11]

Funds cannot be used for the payment of interest or principal on outstanding debt instruments. This includes short-term revenue or tax anticipation notes, or other debt service costs.[12]

Settlements, Judgements, Consent Decrees

Payments required from a settlement agreement, judgment, consent decree, or judicially confirmed debt restructuring plan in a judicial, administrative, or regulatory proceeding are not considered eligible uses of the funds. The exception to this is if "the judgment or settlement requires the provision of services that would respond to the COVID-19 public health emergency. That is, satisfaction of a settlement or judgment would not itself respond to COVID-19 with respect to the public health emergency or its negative economic impacts, unless the settlement requires the provision of services or aid that did directly respond to [those] needs."[13]

Non-essential Workers

ARPA allows cities to give Premium Pay to their essential workers. A worker is not considered to be engaged in essential work if the employee performed telework from a residence, which would exclude them from premium pay.[14] Payments to workers who do not meet these criteria are not authorized under ARPA (but of course can be made with a City's other funds).

[8] Treasury Guidance 37.
[9] Treasury Guidance 56.
[10] Treasury Guidance 67.
[11] Treasury Guidance 38.
[12] Treasury Guidance 54.
[13] Treasury Guidance 38.
[14] Treasury Guidance 42.

Limits to Revenue Losses

Treasury is using the Census Bureau's definition of "general revenue from own sources" As the method of measuring whether a city had lost revenue.[15] The Guidance does not allow a city to use refunds and other correcting transactions, proceeds from issuance of debt or the sale of investments, and agency or private trust transactions are excluded from the eligible use of funds. Revenue generated by utilities and insurance trusts is also excluded.

Federal Matching Requirements

Funding from the Fiscal Recovery Funds may not be used as a non-Federal match for other Federal programs whose statute or regulations bar the use of Federal funds to meet matching requirements.[16]

Note: This summary has been prepared by Best, Best & Krieger LLP

If you have general questions about the Coronavirus State and Local Fiscal Recovery Funds, please email the U.S. Department of Treasury at SLFRP@treasury.gov or call 844-529-9527.

[15] Treasury Guidance 49.
[16] Treasury Guidance 86.