



**LFN 2020-24**

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# Local Finance Notice

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## COVID-19 Operating Deficits and Extraordinary Expenditures: Implementation of P.L. 2020, c.74

[P.L. 2020, c.74](#), enacted on August 31, 2020, empowers local governments to alleviate fiscal impacts related to the COVID-19 emergency through the measured use of existing budgetary and debt structures that have been reshaped to meet local units' emerging needs during the COVID-19 emergency. The approach contained in the new law combines budgetary relief, checks to ensure fiscal responsibility, and borrowing relief into a package that maintains the financial integrity of New Jersey local units. This is especially important for local unit budgets with narrower reserves or that are more reliant on non-property tax revenue tied to general economic activity such as the hotel/motel tax.

These measures will help assure immediate, practical, and comprehensive budgetary and tax relief for New Jersey's local units. Municipalities and counties facing substantial budget shortfalls tied to the COVID-19 pandemic now have the flexibility to spread an otherwise unsustainable single-year impact over several years. In doing so, governing bodies can minimize taxpayer hardship, continue needed capital improvement projects, and preserve the essential services that are especially critical during this time. The tools contained in the new law offer a crucial lifeline to those municipalities facing significant economic fallout due to COVID-19.

## Standards for Anticipating COVID-19 Affected Revenues

Section 1 of P.L. 2020, c.74 amended N.J.S.A 40A:4-26 to authorize the Director of the Division of Local Government Services ("Division") to promulgate new standards for the anticipation of COVID-19 affected revenues in the FY2021 budget, and, if necessary, in future years. For FY2021, the Director authorizes use of a three-year average for calculation of affected revenues, which shall be calculated in a manner consistent with the Reserve for Uncollected Taxes (RUT) calculation used for anomalous years.

### **COVID-19 Special Emergencies – Certain Related Costs**

New subsection l. of N.J.S.A. 40A:4-53 allows a municipality or county to authorize special emergency appropriations for “[t]he immediate preparation, response, recovery, and restoration of public services” during the COVID-19 related public health emergency. Qualifying costs include, but are not limited to, signage, physical reconfiguration of workspace, personal protective equipment (PPE) and sanitizing measures. As with other statutorily permitted special emergency appropriations, a special emergency for extraordinary COVID-19 expenses can be financed by special emergency notes issued pursuant to N.J.S.A. 40A:4-55.

### **COVID-19 Special Emergencies – Operating Deficits**

N.J.S.A 40A:4-53 is amended to qualify local units’ COVID-19 related operating deficits as a special emergency that can be certified through the Division and then spread over several subsequent budgets as a deferred charge, rather than budgeted fully in the current or next year. Qualifying operating deficits include documented COVID-19 affected revenue loss or additional expenditures. Local units need only demonstrate the operational gap and are not required to deplete surplus to qualify. This applies to the general fund as well as to deficits in utility budgets.

#### Documenting and Certifying COVID-19 Related Revenue Loss and/or Additional Expenditures

Any municipality or county seeking to appropriate a COVID-19 related deficit experienced in 2020 or 2021 (or FY2020 or FY2021 for State Fiscal Year municipalities) must make written application to the Division Director in the [prescribed form](#), available on the Division’s website. Using the form specified by the Director and available on the Division’s website, the chief financial officer (“CFO”) shall certify that the deficit is directly attributable to COVID-19 and submit the form to [dlgs@dca.nj.gov](mailto:dlgs@dca.nj.gov) with “COVID-19 Special Emergency” as the subject heading. The CFO must include the following information on the certification accompanying the written application:

- A detailed listing of each revenue and appropriation by its corresponding FCOA code, including identification of specific revenues experiencing reductions due to COVID-19 and COVID-19 related expenditures by category or commodity;
- Anticipated and realized amounts for the current budget year and the three previous budget years and, for those specific revenues having experienced reductions due to COVID-19, an average of the amount collected by the last day of each of the three preceding fiscal years;
- A list of any applications to programs of the federal government, the State, and other sources for purposes of offsetting any qualifying deficit; and
- Fiscal and operational measures being implemented to avoid a structural deficit in future budget years.

The Chief Financial officer shall submit the certification for approval by a majority of the full governing body. A municipality or county seeking approval for a special emergency under this provision shall apply for any financial assistance that may be available from the federal government, the State, and other sources to offset any qualifying deficit directly attributable to COVID-19. Any such financial assistance obtained by the local unit shall be used to offset any deficit.

A municipality or county shall make application to the Director during the year in which the revenue deficits or additional expenses occurred by no later than December 1. The certification must be based on the best available revenue and expenditure estimates. The Director shall have the discretion to grant a written request for extension of the December 1 deadline. Approval of the certification of the special emergency and resulting deferred charge in advance of the close of the budget year eliminates the deficit in operations on the AFS. Please reference the "Accounting Considerations" subsection below for treatment of deficits certified before the end of the current year.

The Director shall approve or disapprove any complete application within 45 days, or the next business day if the 45th day falls on a Saturday, Sunday, or holiday. If a written decision is not rendered within this time period, the application shall be deemed to be approved and the municipality or county may proceed to adopt the special emergency. A disapproved application may be resubmitted with such changes as the municipality or county deems appropriate, with submission and review subject to the same requirements.

Municipalities obtaining Director approval to adopt a special emergency for a COVID-19 related revenue deficit or additional expenses shall not be eligible for local budget exam pursuant to subsection b. of N.J.S.A. 40A:4-78 until the fiscal year after the final appropriation is made.

#### Funding the Special Emergency

Once approved by the Director, the special emergency may be raised in the budget over a five-year period with no appropriation for the deferred charge required in the first year. For example, a deferred charge resulting from a special emergency in 2020 need not be budgeted in 2021 but rather 1/5 of the amount would be budgeted in the 2022 through 2026 annual budgets, thus is raised in the budget over a six year period.

A municipality or county that would experience substantial financial hardship by appropriating for the deferred charge over the automatic six-year emergency period may seek Local Finance Board approval to make the appropriations over up to 10 years. The Division will soon issue a Board application specific to this circumstance to be incorporated into the certification process. If approved, the extended period shall be in accordance with a schedule determined by the Board, which shall be no later than the end of the 11th year after declaration of the special emergency. Substantial financial hardship includes, but is not limited to, when appropriation of the special emergency over five of the next six years would directly cause a tax levy increase of greater than 2% or an increase of greater than \$50 per average assessed home for each year deferred charges appear in the local unit's budget, or in the case of a utility, an at least five percent (5%) increase in user fees or charges.

This special emergency process affords a municipality or county significant time to compensate for lost revenues and achieve recovery, effectively authorizing a no-interest loan within the entity's own budget to absorb revenue losses, potentially mitigating the need to borrow to fill these gaps.

Local units are not required to use fund balance to offset this deferred charge. Any offsetting receipts from the federal government, the State, and other source directly related to COVID-19 shall be directly applied to funding the special emergency.

A special emergency passed for any purpose must be appropriated as a deferred charge and is excluded from caps.

#### Issuance of Special Emergency Notes

If the special emergency for a COVID-19 related operating deficit is approved by the Director, a municipality or county may issue a special emergency note to address the cash flow and appropriations needs related to the deferred charge. Any associated borrowing has a maximum maturity date tied to the duration of the approved deferred charge spread. A municipality or county seeking approval to extend the deferred charge spread must obtain Board approval to issue special emergency notes pursuant to an extended maturity schedule. Because the deferred charge accounts for the up-front need, this borrowing would likely be cash-flow related; however, cash management needs may arise during the recovery period. Municipalities and counties may not borrow moneys duplicative of financial assistance received to cover costs or replace lost revenues related to COVID-19.

A municipality or county may issue COVID-19-related special emergency notes through a county improvement authority pool, and notes issued by a municipality may also carry a county guarantee. Participation in pooled issuances may improve market access and ratings, particularly for comparatively smaller municipalities or those municipalities with lower credit ratings.

#### Accounting Considerations for Revenue Deficits

If a municipality or county receives Division approval to declare a COVID-19 related special emergency in advance of the close of the fiscal year, the emergency can be funded in advance, thereby cancelling the certified anticipated deficit by recording the deferred charge as a revenue. If the actual deficit experienced was less than the amount originally certified, the difference shall be canceled by resolution, thereby reducing the amount of the deferred charge. If revenue recorded pursuant to the above paragraph is related to the collection of delinquent taxes, all tax revenues collected in the subsequent year, and those that are collected in excess of a three year average as "Receipts for Delinquent Taxes" shall be directly applied to fund the Special Emergency. See the Appendix to this Notice for relevant examples.

#### **Refunding Bond Issuances for Certain COVID-19 Related Costs: Local Authorities & Boards of Education**

Sections 6 and 7 of P.L. 2020, c.74 permit authorities and boards of education to seek approval from the Local Finance Board to issue refunding bonds for the cost of COVID-19 expenditures incurred for the immediate preparation, response, recovery, and restoration of public services. The refunding bond issuance shall not exceed five years.

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Approved: Melanie R. Walter, Director

Document	Internet Address
P.L. 2020, c.74	<a href="https://www.njleg.state.nj.us/2020/Bills/PL20/74_..PDF">https://www.njleg.state.nj.us/2020/Bills/PL20/74_..PDF</a>
COVID-19 Special Emerg. Certification	<a href="https://www.nj.gov/dca/divisions/dlgs/programs/mc_bud_docs/Certification%20for%20COVID-19%20Special%20Emergency.xlsx">https://www.nj.gov/dca/divisions/dlgs/programs/mc_bud_docs/Certification%20for%20COVID-19%20Special%20Emergency.xlsx</a>

## Appendix

### Sample COVID-19 Related Special Emergency Accounting Journal Entries:

#### Scenario 1

A Municipality or County anticipates \$2,000,000 in parking revenue, but now anticipates a deficit of \$1,000,000 due to COVID-19. The municipality certifies the anticipated loss before the close of the budget year.

1. Authorize a "Special Emergency COVID-19" and submit the application and certification to the Division by December 1.

Debit: Deferred Charge "Special Emergency COVID-19"

Credit: Operations

2. Issue "Special Emergency Notes" for \$1,000,000.

Debit: Cash

Credit: Emergency Notes Payable\*\*

\*\*If at the close of the budget year, the realized emergency was less than the \$1,000,000 certified in advance by, for example, \$200,000, then an additional entry to reduce the emergency to \$800,000 must be made:

Debit: Reserve for Notes Payable for the difference

Cancel by resolution \$200,000 of the special emergency. Reflect only \$800,000 on Sheet 29 of the Annual Financial Statement.

Debit: Operations

Credit: Deferred Charge "Special Emergency COVID-19"

3. Insert a Budget Appropriation for the appropriate Deferred Charge amount beginning in 2022, and each year for the next 5 proceeding years until paid, or for the extended period otherwise authorized by the Local Finance Board.

Debit: Current Appropriations

Credit: Deferred Charge "Special Emergency COVID-19"

4. When Special Emergency Notes are Paid:

Debit: Special Emergency Notes Payable (Balance Sheet)

Debit: Interest on Notes (Appropriation required on AFS Sheet 32)

Credit: Cash

Note: When issuing a special emergency note, cash surplus on sheet 21 is not restricted by the outstanding deferred charge because the cash has been received.

Scenario 2

A Municipality or County anticipates \$500,000 in court revenue, but due to closure only realizes actual revenue of \$300,000 and a deficit of \$200,000. The municipality certifies the anticipated loss before the close of the budget year. (See journal entries in Scenario 1).

Scenario 3

Anticipating Receipts for Delinquent Taxes in the subsequent budget year when loss of revenue from tax collections is part of the Special Emergency COVID-19:

A tax collection revenue shortfall of \$5,000,000 was certified in the local unit's Special Emergency Covid-19

Collections in the three prior years were:

Year 1 - 1,100,000

Year 2 - 1,200,000

Year 3 - 1,300,000

Average - 1,200,000

Collection in Subsequent Year - 6,100,000

Collection to be applied to fund Special Emergency- 4,900,000. (6,100,000 – 1,200,000)

The Levy Cap exclusion for the Deferred Charge Special Emergency COVID-19 would be entered net of the offsetting revenue on the Levy Cap workbook.

Scenario 4

The municipality has experienced unanticipated increases in expenses for police, fire, emergency management services and incurred costs for plexiglass, wall barriers, floor markings, and remote work-related IT, totaling \$2,500,000 that are directly attributable to COVID-19, and incurred Structural changes for plexiglass, wall barriers, floor markings, additional signage and information technology improvements necessary to allow remote work in the amount of \$2,500,000.

1. Authorize a "Special Emergency COVID-19" in the amount of \$2,500,000.

Debit: Deferred Charge "Special Emergency COVID-19"

Credit: Current Appropriations

2. Issue "Special Emergency Note" for \$2,500,000.

Debit: Cash

Credit: Emergency Notes Payable

3. Insert a Budget Appropriation for the appropriate Deferred Charge beginning in 2022, and each year for the next five consecutive years until paid, or for the extended period otherwise authorized by the Local Finance Board.

Debit: Current Appropriations

Credit: Deferred Charge "Special Emergency COVID-19"

4. When Special Emergency Notes are Paid

Debit: Special Emergency Notes Payable (Balance Sheet)

Debit: Interest on Notes (Appropriation required on AFS Sheet 32)

Credit: Cash

Note: When issuing a special emergency note, cash surplus on sheet 21 is not restricted by the outstanding deferred charge because the cash has been received.