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Bail Out the States?

Any more federal aid should come with very strict conditions.



President Donald Trump and Vice President Mike Pence watch a video of New York Gov. Andrew Cuomo speaking during a coronavirus task force briefing at the White House, April 19.

PHOTO: PATRICK SEMANSKY/ASSOCIATED PRESS

Congress is passing its fourth coronavirus relief bill this week, and already Democrats are teeing up the fifth. The main goal this time will be to bail out state governments, especially those run by Democrats and their allies in public unions. The question to ask is why taxpayers in Appleton and Sarasota should rescue politicians and unions in Albany and Springfield?

“You know the state governments are broke, to use a very blunt term. You know the state governments are now responsible for the reopening and the governors are going to do the reopening, and they have no funds to do it,” New York Gov. Andrew Cuomo said Tuesday after making his case to President Trump for more federal cash.

The Governor blames the pandemic and recession, but states like New York were already in trouble from their own mismanagement. Mr. Cuomo warned for months about a \$6 billion state deficit thanks to runaway Medicaid costs and taxpayers leaving his high-tax state. He signed a \$177 billion business-as-usual budget on April 3 that allows him to borrow \$11 billion if spending exceeds revenues. The coronavirus was already a clear and present danger.

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Or take Illinois, where Gov. J.B. Pritzker in February proposed a \$40.8 billion budget that included \$9 billion for public pensions. Mr. Pritzker raised taxes in 2019 and wants to make the state's current flat tax progressive if voters approve a constitutional change this fall. Yet he and the unions who own the state house have blocked pension or spending reforms.

They've long bet on a federal bailout, and they see Covid-19 as their main chance. Illinois Senate President Don Harmon last week sent a plea for a \$41.6 billion federal bailout to his state's Democratic Congressional caucus. He wants \$15 billion in no-strings-attached cash; \$6 billion for the state's unemployment trust fund; \$10 billion for pensions; and \$9.6 billion in unrestricted aid for cities including Chicago and its unreformed pensions. Oh, and he also want the federal government to pick up 65% of the state's Medicaid costs though Congress's second relief bill already increased the rate to 56% from half.

Mr. Pritzker is now projecting a \$7 billion deficit, which the state could staunch by furloughing nonessential employees or adjusting employee benefits to the level of private workers. Illinois's unfunded pension liability increased 60% between 2010 and last year to \$137 billion even as the stock market more than doubled. Public retirees in the state still get annual compounded pension cost-of-living raises of 3%.

Keep in mind that Congress's \$2.2 trillion Cares Act last month included a \$150 billion blank check to states plus \$90 billion for schools, public transit and Medicaid. To put these numbers in perspective: *All* state tax revenues during the last [three months of 2019](#) totalled \$254 billion. So Washington's last state infusion is roughly equal to three months of tax collections.

Dan Clifton of Strategas Research Partners points out that New York received \$5.22 billion in direct aid from the Cares Act, or 6.8% of its \$77 billion in annual general-fund tax revenue. That doesn't include \$3.8 billion in the Cares Act for the New York subways, and billions more for health care and schools. Illinois received \$3.52 billion, or 8.8% of its general-fund revenue, while Michigan also made it big with \$3.1 billion, or 27%.

The economic shutdowns will cause budget pain in states and cities. But states with healthy finances going into the pandemic should be able to endure revenue declines for a few months thanks to the Cares Act.

The Federal Reserve has also set up a \$500 billion facility to buy short-term (two years or less) debt from states and large municipalities, which will help cover operating costs with little disruption as citizens delay income-tax payments and spend less. This federal taxpayer backstop is also keeping borrowing costs low. California last week issued \$1.4 billion in bonds yielding 1.4% to refinance existing debt and save \$334 million in interest costs.

But the Fed shouldn't rescue states and cities by buying longer-dated securities such as bonds that Illinois floated during the last two recessions to backfill its pensions. This would encourage bad governance.

President Trump has signaled he's open to a state bailout because, well, he's open to anything these days. But Senate Majority Leader Mitch McConnell caused a stir Wednesday when he said states should consider bankruptcy rather than get a bailout. He cited the Chapter 9 workouts of cities like Detroit.

But some doubt that state bankruptcy is constitutional under the Contracts Clause, and any Chapter 9 filing would be challenged in court. Mr. McConnell's larger point is that states shouldn't get more no-strings cash. Private companies that borrow from the Fed and Treasury have to meet stiff conditions, including limits on compensation, and the same should apply to state governments.

Bailout conditions should include cuts in nonessential spending, immediate and permanent reductions in public pension benefits, and other reforms to put states on a path to fiscal recovery. Lawmakers will protest, but they are the ones asking Americans for help. If states want more money, they need to show it won't merely go to sustain unaccountable, one-party political machines.