

Commonwealth of Kentucky
Recovery Plan

**State and Local Fiscal Recovery
Funds**
August 31, 2021 Report

Commonwealth of Kentucky Recovery Plan

Executive Summary

In response to the pandemic and the economic recovery, the Commonwealth of Kentucky has taken official actions to devote nearly half of Kentucky's State and Local Fiscal Recovery Fund allocated resources to critical economic recovery and pandemic response activities.

President Biden signed the American Rescue Plan Act on March 11, 2021. Governor Andy Beshear, 19 days later, signed bipartisan legislation enacted by the Kentucky General Assembly that made specific appropriations during its 2021 Regular Session, which adjourned on March 30, 2021, from the State Fiscal Recovery Fund totaling \$1,167,934,200 in state fiscal year 2021-2022.

In response to the pandemic and the economic recovery, the Commonwealth of Kentucky has devoted State and Local Fiscal Recovery Fund resources to the following uses:

Repayment of federal loan to Kentucky's Unemployment Insurance Trust Fund - \$575,000,000 is appropriated and \$505,731,673.91 was expended to fully repay Kentucky's federal loan to its unemployment insurance trust fund. The outcome results in businesses in Kentucky, especially small businesses that were especially hit hard by the pandemic, from incurring significant increases in state unemployment insurance taxes to repay the federal loan which was largely the result of necessary job reductions associated with mitigation efforts to slow the spread of the COVID-19 infection. This action will remove a potential barrier to Kentucky's economic recovery that the pandemic caused.

Water and Sewer infrastructure - \$250,000,000 is devoted to water and sewer infrastructure projects across the Commonwealth. Governor Andy Beshear announced the \$250 million Cleaner Water Program in June, 2021 stating that, "Quality drinking water and well-maintained sewer systems are fundamental to keep Kentuckians safe and to build a better Kentucky. This funding boost will make a real difference in cities and counties across Kentucky while also creating more than 3,800 direct and indirect jobs. This is a chance for us to upgrade our systems without raising costs on Kentuckians. It's a real chance to be transformative." Fast progress for the deployment of these funds has already been made. Project applications from most of Kentucky's 120 counties have been received and are under review. The Commonwealth has used its existing statewide water planning and project management system that is used to carry out the existing clean water and drinking water state revolving fund programs to collaborate with water systems across the state and to expedite the application process. The allocation of the \$250 million incorporates several elements including devoting \$50 million of the funds for grants to utilities to provide drinking water services to unserved, rural customers or to utilities under a federal consent decree.

Broadband infrastructure - \$300,000,000 to expand broadband services to unserved and underserved areas of Kentucky. Governor Andy Beshear in a recent announcement said, "In today's technology-dependent society, access to reliable, high-speed internet can no longer be considered a luxury available only to those who can afford it. In fact, broadband is foundational to our future economic growth, particularly in areas of the state previously deemed unprofitable to serve. Over the last 18 months, we have seen just how critical reliable internet access is for all of us to stay informed, safe and connected to work, school, health care, friends and family. And now, we look to our broadband community to tell us how they would use the funds available to support the construction, development or improvement of broadband access across the commonwealth, with our unserved communities receiving first priority."

The first phase of implementation devotes \$50 million to target Kentucky areas that are unserved by broadband service. A Request for Proposal has been issued to solicit applications from private and

municipal broadband providers. The expected outcomes include the provision of affordable, high-speed broadband service with speed of at least 100 megabits per second to households and businesses that are currently unserved. These funds represent the first statewide public funds available to award grants for the deployment of broadband infrastructure.

COVID-19 prevention and mitigation in vulnerable or congregate settings - \$42,934,200 is appropriated for COVID-19 prevention and mitigation in vulnerable and congregate settings, with \$5,934,200 directed to testing, mitigation and other COVID-19 responses in county jails. The remaining \$37,000,000 is still in the planning stage.

The Commonwealth, through its biennial budget process, expects to deploy the remaining amounts of its \$2,183,237,290.90 allocation to the pandemic and economic recovery. The budget process flows through the 2022 Regular Session of the Kentucky General Session, which ends in April, 2022. Governor Beshear will present a proposal to the Kentucky legislature in late January, 2022.

Uses of Funds

Using the expenditure category typology set forth by the U.S Department of Treasury's reporting requirements, the \$1,167,934,200 appropriated for the State Fiscal Recovery Fund covers the following uses of funds.

Public Health (EC 1)

A total of \$42,934,200 is appropriated for COVID-19 prevention and mitigation in vulnerable and congregate settings, with \$5,934,200 directed to testing, mitigation and other COVID-19 responses in county jails. The remaining \$37,000,000 is still in the planning stage. In Kentucky, a significant number of adjudicated state felons, especially for shorter sentenced felons, are housed in county jails. County jails which are a part of Kentucky's county governments, working with public health guidance, need fiscal assistance to contend with the necessary extra costs to mitigate infection of COVID-19 while carrying out their public safety function of holding pre-trial persons, misdemeanants, and designated state felons.

Negative Economic Impacts (EC 2)

To address one of the most severe negative economic impacts of the pandemic, the unprecedented job losses that took place in the spring of 2020 that was necessary to prevent the spread of infection, \$575,000,000 was appropriated and \$505,731,673.91 was expended to fully repay Kentucky's federal loan to its unemployment insurance trust fund. State unemployment insurance trust funds are financed from employers through taxes and other payments to the trust fund based on their experience with the reduction of employees that was not the fault of the laid-off employees. Kentucky's employers, by law, bear the responsibility of repaying the federal loan and for building back up the trust fund balance. This is a business expense that had nothing to do with market forces; but had everything to do with the pandemic. The devotion of State Fiscal Recovery Funds to repay the federal loan relieves Kentucky employers from the extra expenses of paying for the repayment while most of them are struggling with the pandemic. This is a necessary response to the negative economic impacts of the pandemic. The outcome results in businesses in Kentucky, especially small businesses that were especially hit hard by the pandemic, from incurring significant increases in state unemployment insurance taxes to repay the federal loan that otherwise would take place if not for the use of the State Fiscal Recovery Fund. This action will remove a potential barrier to Kentucky's economic recovery that the pandemic caused.

Water, sewer, and broadband infrastructure (EC 5)

A total of \$250,000,000 is devoted to water and sewer infrastructure projects across the Commonwealth. Governor Andy Beshear announced the \$250 million Cleaner Water Program in June, 2021. The legislation governing the disposition of the funds allocated \$150 million to Kentucky's 120 counties based on their proportion of the state's population. Another \$50 million of the funds is directed to grants to utilities to provide drinking water services to unserved, rural customers or to utilities under a federal consent decree. This component directly targets communities that have not been sufficiently served as well as the major urban areas of the Commonwealth that are contending with federal consent decrees. Quality drinking water and well-maintained sewer systems are fundamental to keep Kentuckians safe and to build a better Kentucky. This funding boost will make a real difference in cities and counties across Kentucky while also creating more than 3,800 direct and indirect jobs. This is a chance to be transformative. Expedited progress in the deployment of these funds has already been made. Project applications from most of Kentucky's 120 counties have been received and are under review. The Commonwealth has used its existing statewide water planning and project management system that is used to carry out the existing clean water and drinking water state revolving fund programs to collaborate with water systems across the state and to expedite the application process.

A total of \$300,000,000 is devoted to expanding broadband services to unserved and underserved areas of Kentucky. The pandemic has highlighted the necessity of having access to affordable high-speed internet service to all households and businesses. It can no longer be considered a luxury available only to those who can afford it. In fact, broadband is foundational to our future economic growth, particularly in areas of the state previously deemed unprofitable to serve. This \$300 million, when combined with at least a 50 percent match, will result in a significant step toward universal broadband coverage. To address those most severely impacted by the pandemic, a priority will be placed on communities that have no access to broadband service, the unserved. The first phase of implementation devotes \$50 million to target Kentucky areas that are unserved by broadband service. A Request for Proposal has been issued to solicit project applications from private and municipal broadband providers. The expected outcomes include the provision of affordable, high-speed broadband service with speed of at least 100 megabits per second to households and businesses that are currently unserved. These funds represent the first statewide public funds available to award grants for the deployment of broadband infrastructure.

Promoting equitable outcomes

The U.S. Department of Treasury incorporated supplemental reporting requirements after the American Rescue Plan Act was passed in developing the administrative requirements of the State Fiscal Recovery Fund program. This included elements around the promotion of equitable outcomes of various types.

Water and Sewer Infrastructure

When Governor Beshear and the Kentucky General Assembly were making decisions in March, 2020, on the allocations of the State Fiscal Recovery Fund, these reporting requirements were not yet known or published. Specific equity goals were not an explicit element of that decision-making in March, 2020, but there will be some results for spending for water, sewer and broadband infrastructure that will address prior inequities. When the Kentucky General Assembly directed \$250 million in funds for water and sewer infrastructure, the state legislative text directed the allocation of funds and established funding caps for each of the 120 Kentucky counties in proportion to their share of the state's population for 60 percent, or \$150 million, of the \$250 million for water and sewer infrastructure. Another \$50 million was directed to be available to those areas of Kentucky that were unserved for drinking water or were under federal consent decrees. This aspect of the water and sewer infrastructure funding will directly bear on promoting equitable outcomes, as delivering clean drinking water service to an area that is unserved clearly addresses an economic equity issue by instituting that necessary service. Also, the four areas of Kentucky

that are under a federal consent decree are comprised of the top three most urban populations in the state. Those areas also include the highest number and highest concentration of minorities in Kentucky.

Broadband Infrastructure

The funding to provide broadband services also included a priority for unserved areas of the Commonwealth. Economic equity concerns will be directly addressed by the approval of projects that bring broadband services to locations that are currently unserved or have internet speeds of less than 10 megabits per second download. There are many rural areas of the state based on existing mapping information that are unserved by broadband. There are also urban areas that are currently unserved. This economic equity will be first in line for use of the funds. The Commonwealth will be able to identify demographic and economic information on these unserved areas once projects have been approved to construct the infrastructure necessary to deliver broadband services.

Unemployment Insurance-Repayment of Federal Loan

The repayment of Kentucky's unemployment insurance federal loan also contains elements of economic equity.

The severe reduction in employment at the onset of the pandemic impacted heavily certain sectors with a heavy impact on small businesses. Nonfarm employment in Kentucky dropped by about 240,000 jobs in the second quarter of 2020. The leisure and hospitality services sector lost 31 percent of these jobs with a concentration in small businesses.

Unemployment insurance (UI) benefits are funded from taxes paid by employer. The COVID-19 pandemic created an unprecedented surge in state unemployment insurance claims, and UI benefits have played an important role in helping individuals who have been negatively impacted by the pandemic and associated economic downturn. However, the impact of the extraordinary demand for UI benefits had a dramatic effect on Kentucky's UI trust fund balances. Kentucky's UI trust fund balance was approximately \$550 million on April 1, 2020. By the end of June 2020, less than 90 days into the COVID-19 pandemic, the UI trust fund was insolvent, and Kentucky began borrowing from the Federal government under Title XII to meet State unemployment insurance benefit payments. The Commonwealth last dealt with Title XII loans during the Great Recession, and the experience of repaying the loans was a long and difficult experience for employers in Kentucky. The ability to utilize the federal State Fiscal Recovery Fund for the repayment of Kentucky's outstanding Title XII loans will save employers in the Commonwealth over \$537.8 million in increased State and Federal UI taxes.

The unemployment insurance program in Kentucky is designed so that the employers that lay off their employees with greater frequency face higher UI taxes than employers that maintain a better record of avoiding layoffs. Each business' layoff history determines that business's experience rating, and the employer's experience rating determines that business's UI tax rate. Kentucky has multiple UI tax rate schedules, depending on the current solvency of the UI trust fund, and each rate schedule has a range of rates, whereby employers with poor experience ratings are subject to the higher tax rates, while employers with better experience ratings pay lower rates. As a result of a declining trust fund balance, all employers will pay a higher UI tax rate regardless of their experience rating. The impact of COVID-19 would have triggered the maximum change possible in the rate schedules in Kentucky, as employers would have moved from Schedule A, with a range of 0.3% to 9.0% of taxable wages, to Schedule E, with a range of 1.0% to 10% of taxable wages. Based on estimates from the University of Kentucky, the average tax rate for employers in the Commonwealth was expected to increase by 60.5%, from 1.62% to 2.60% of taxable wages, representing an increased UI tax burden on Kentucky employers of approximately \$177.8 million.

In addition to the State mechanisms for recovering from insolvency, the Federal Title XII program has a built-in repayment mechanism for repayments of loans for States that have outstanding balances. After a state has a loan balance on January 1st for two consecutive years, the State will be deemed a FUTA credit reduction state. Employers in the state will lose 0.3% of their 5.4% FUTA credit towards Federal UI tax payments for each year the borrowing State has an outstanding loan balance. The FUTA credit reduction of 0.3% is applied to the Federal taxable wage base of \$7,000 and results in a penalty for employers of \$21 per employee. The proceeds from the credit reduction are applied to the outstanding loan balance, and the credit reduction increases by 0.3% each additional year that a State has an outstanding balance. Based on the past experience of Kentucky during the Great Recession, the Commonwealth would have been expected to have faced at least three years of reduced FUTA credits, costing employers in the Commonwealth approximately \$360 million in additional FUTA taxes.

The impact of the potential increases in UI taxes have a greater incidence on smaller businesses, as unemployment taxes represent a greater share of business expenses. In Kentucky, Census data shows that of the approximate 91,000 business establishments, over 88,500 establishments have fewer than 100 employees. As the economy recovers from the impact of COVID-19, these small firms are struggling to regain their economic footing, and providing relief from a dramatic increase in the UI tax rates paid by these firms will help them continue their recovery.

Performance

The repayment of the federal unemployment insurance loan can be best measured by the amount of additional business expenses that will be foregone as a result of the use of the State Fiscal Recovery Funds for that purpose, including the heavy percentage of employers that are small businesses and the structure of unemployment insurance taxes with its cap on the wage base that imposes a higher incidence on small businesses, who were among the hardest hit by the pandemic.

For water and sewer infrastructure, the performance measures that will be used are the same that are used for the Clean Water and Drinking Water State Revolving Fund (SRF) programs, including the number of Kentucky households and businesses that will attain drinking water services and improved water and sewer services, as well as the median household income data for each project's area.

The broadband infrastructure projects will reveal the number of unserved (less than 10 megabits per second download and 1 megabit per second upload) households and businesses that will achieve affordable access to high-speed internet services (a minimum of 100 megabits per second download and upload). The Commonwealth will examine methods of measuring other benefits related to the project areas that are more remote and have less dense populations. These areas best reflect the circumstances in which the broadband service market has failed because households and businesses are in geographic locations that have not been commercially feasible to provide broadband services.

Community Engagement

As mentioned in the Executive Summary, the American Rescue Plan Act was effective on March 11, 2021 and the Kentucky General Assembly was required to adjourn its legislative session by April 1, 2021. There was very little time available to discern all the competing uses of the State Fiscal Recovery Fund and to engage in a broad set of engagement.

The business community, particularly the Kentucky Chamber of Commerce, reached out to the Governor to strongly advocate for the use of federal pandemic relief and recovery funds to relieve Kentucky businesses from having to incur the costs of repaying the federal loan to the unemployment insurance trust fund that was primarily due to the pandemic. At Governor Andy Beshear's recommendation, the legislature appropriated total of \$575,000,000 from the State Fiscal Recovery Fund and \$505,731,673.91 was expended to fully repay Kentucky's federal loan to its unemployment insurance trust fund from the State Fiscal Recovery Fund. Governor Andy Beshear previously allocated \$203.5 million from the federal Coronavirus Relief Fund to Kentucky's unemployment insurance trust fund that kept Kentucky from increasing its federal loan amount. Governor Beshear also devoted over \$76.4 million from the Coronavirus Relief Fund for the state matching portion of the Lost Wages Assistance program, resulting in over \$305 million in pandemic-related unemployment insurance benefits to Kentuckians.

After the approval of \$250 million from the State Fiscal Recovery Fund for water and sewer infrastructure by the Kentucky legislature in March, 2021, an outreach effort began. This outreach effort involved communicating and working with all of the water utilities, both special district and municipal, and county and city governmental officials, to make them aware of the availability of funds and the possible eligible uses. This effort was coordinated by the Kentucky Infrastructure Authority (KIA) and the Kentucky Department of Local Government.

The Commonwealth of Kentucky has a Water Resource Information System (WRIS) that has been in place for more than 20 years. It is the first step in planning for and financing water and wastewater projects, was chosen as the application portal for the Cleaner Water Program grants. KIA coordinated Zoom meetings and phone calls with the Area Development Districts (ADDs), regional government coordinating bodies, letting each Water Management Coordinator and Executive Director know the type of funding available, the criteria for project selection, the eligible project types, the application process and deadlines, and the timeline for funding awards. The information was also shared with legislative committees, Kentucky League of Cities, Kentucky Association of Counties and the Kentucky Water and Wastewater Operators Association members. The Water Management Coordinators at the ADDs conducted meetings with each County Water Management Council for the purpose of reaching a consensus on the split of county allocation funds and explained there were two other types of available funding to the water/wastewater utilities.

The WRIS Portal also serves as the statewide registry for water and wastewater projects in the Commonwealth of Kentucky. Multiple funding sources require applicants to have a completed Project Profile within the WRIS including the Clean Water and Drinking Water State Revolving Fund (SRF), Community Development Block Grants (CDBG), Appalachian Regional Commission (ARC), Delta Regional Authority, State and Federal Line Item Grants, and Coal Severance Grants. The WRIS Project Profile is the project database that populates the e-Clearinghouse portal for review by all state agencies.

For the broadband infrastructure allocations, the Commonwealth of Kentucky is engaging in a Request for Proposal (RFP) process for its initial application phase for the use of \$50 million for the construction of broadband infrastructure to unserved areas of the state. Prior to releasing the RFP and grant application, a Request for Information (RFI) process was undertaken. Many interested parties provided useful information. In addition, there has been numerous appearances before Kentucky's legislative committee system and further outreach to local elected officials at their summer conferences.

Labor Practices

There are no workforce practices outlined in the Annual Recovery Report reporting guidance that are reportable for the appropriated uses of the State Fiscal Recovery Fund. Kentucky is not a "little" Davis-

Bacon state. The procurement of design and construction services for water, sewer and broadband infrastructure will be the responsibility of the utilities and follow the same practices as the state revolving fund programs administered by states through the Environmental Protection Agency.

Use of Evidence

The devotion of Kentucky’s allocation of State Fiscal Recovery Funds to repaying its unemployment insurance federal loan, constructing water, sewer and broadband infrastructure, or reimbursing county jails for COVID-19 mitigation responses are not the type of uses of the fund that strongly relate to the type of social actions that are determinative through evidence-based interventions. There are best practices in terms of the proper design and compliance matters in regard to water, sewer and broadband infrastructure. The social and economic benefits from the availability of clean drinking water, environmentally compliant wastewater systems, and affordable access to high-speed internet are public good benefits that inure to both households, businesses, and Kentucky communities.

Table of Expenses by Expenditure Category

Category		Cumulative expenditures to date (\$)	Amount spent since last Recovery Plan
2.8	Contributions to UI Trust Funds	505,731,673.91	505,731,673.91

Project Inventory

There are no projects applicable to this reporting period.

Ineligible Activities: Tax Offset Provision

This is not applicable to the Commonwealth of Kentucky’s decisions on the use of the State Fiscal Recovery Fund to-date.