Center on Budget and Policy Priorities

1275 First Street NE, Suite 1200
Washington, DC 20002

Tel: 202-408-1080
Fax: 202-408-1056

center@cbpp.org
www.cbpp.org

To: Interested parties
Re: Treasury's Interim Final Rule for the Rescue Plan's Fiscal Recovery Funds
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Under the American Rescue Plan Act, states, cities, counties, U.S. territories, and tribal nations will receive a total of $350 billion in Fiscal Recovery Funds. Under the Act, the U.S. Department of the Treasury will disburse and oversee the use of these funds. On May 10, 2021, Treasury issued an Interim Final Rule providing guidance to recipient governments explaining how Treasury will interpret the language in the Act and administer the Fiscal Recovery Funds.

While Treasury seeks feedback from recipient governments and the public on its Interim Final Rule and poses numerous questions in the document aimed at encouraging this feedback, the guidance is effective immediately and Treasury is not *required* to change the rule based on public input. The comment period is open until 60 days after the Interim Final Rule is posted in the Federal Register, which is expected within a few days.

The Interim Final Rule and other information about the Fiscal Recovery Funds is available at this website: https://home.treasury.gov/policy-issues/coronavirus/assistance-for-state-local-and-tribal-governments/state-and-local-fiscal-recovery-funds#main-content.

The IFR gives states and other recipients a lot of flexibility to use the Fiscal Recovery Funds to help the many people struggling in today's pandemic economy, as well as to begin to undo longstanding structural inequities the pandemic further exposed. This flexible approach appears to largely clear the way for states and other recipients to pursue CBPP's recommendations for using the Fiscal Recovery Funds, which readers can find here: https://www.cbpp.org/research/state-budget-and-tax/priorities-for-spending-the-american-rescue-plans-state-and-local. The IFR also offers several excellent ideas for making the most of the funds and encourages states and other governments to adopt them. We've included several of those ideas in our summary of the IFR below.

Summary of the Interim Final Rule's Key Features

More than half the states will receive their funds in two tranches, with half coming next year
(See pp. 102-105)

- Those states whose unemployment rate is more than 2 percentage points higher than it was in Feb 2020 will receive all of the funds in one tranche, which Treasury will disburse after it receives a certification letter from the state indicating that the state needs the money and will

follow the rules. Based on the latest unemployment rates (for March 2021), here's how that breaks out:
  - ✓ The states that will receive the funds in one tranche are: CA, CT, CO, DC, DE, HI, IL, LA, MA, MD, ND, NJ, NM, NV, NY, OR, PA, RI, SC, TX, and VA.
  - ✓ The remaining states will receive the funds in two tranches, half once the certification letter is received and the other half a year later.
  - ✓ Puerto Rico and other territories, as well as tribal nations, will receive the funds in one tranche.
- All cities and counties will receive half the funds this month and the other half a year later. No certification letter is required.

Treasury encourages states and other recipients to address public health disparities, target funds to people and areas with low incomes, and seek long-term benefits
(See pp. 10-45)

- States and other governments can use the funds to fight COVID, to provide medical care for people affected, and to "address disparities in public health that have been exacerbated by the pandemic." Treasury includes several examples of the sorts of services that would address these disparities including:
  - ✓ New and expanded mental health, substance use, and behavioral health services, and crisis intervention services.
  - ✓ Conducting outreach and helping people access services. Robust outreach operations will be especially important, especially in assuring that hard-to-reach communities such as certain immigrants are able to access support that is available to them. States, localities, and other governments can use the funds to launch a public awareness campaign and to fund and train organizations rooted in the communities most affected by the pandemic and groups that already help people access public services.
  - ✓ Services that improve health outcomes such as housing services, lead paint remediation, and violence intervention programs.
- The funds may also be used to cover salary and benefits for public health and safety workers focused on fighting COVID, and to improve the design and execution of health and public health programs.
- States and other governments also have broad latitude when considering how to address COVID's economic impacts. They "may presume that a household or population that experienced unemployment or increased food or housing insecurity or is low- or moderate-income experienced negative economic impacts resulting from the pandemic." Assistance to these households or populations can include, for example, help buying food, paying rent, paying utility bills, or paying for internet access. It can also include cash assistance, legal aid to prevent eviction, and job training, among other uses. And it can be used to help small businesses and industries affected by the pandemic (i.e. tourism, travel, and hospitality).
- Treasury will assume certain services are eligible uses if they're provided in a Qualified Census Tract (a definition used by HUD to identify areas where people have low incomes on average) or to people who live in one of these census tracts. These services include, for example, spending to make housing more affordable, reduce educational disparities, and/or promote healthy childhood environments.
- Treasury "encourages recipients to provide assistance to those households, businesses, and non-profits in communities most disproportionately impacted by the pandemic" and

"encourages recipients to consider funding uses that foster a strong, inclusive, and equitable recovery, especially uses with long-term benefits for health and economic outcomes."

Revenue loss is defined in a way that accounts for the fact that revenues would've likely grown if not for the pandemic.
(See pp. 51-61)

- States and other governments may use the funds to provide public services up to the amount of revenue loss due to the pandemic.
- To calculate revenue loss due to the pandemic, states and other governments start with their fiscal 2019 "general revenue from own sources" as defined on the Census Bureau's Annual Survey of State and local Government Finances. This amount establishes their baseline revenue amount. Then they assume that these revenues would have grown by 4.1 percent each fiscal year if the pandemic had not hit. (If a state's actual average revenue growth over the 3 years prior to the pandemic was greater than 4.1 percent, they can use that figure.) By comparing resulting counterfactual amounts to their actual revenues in each fiscal year, states and other governments determine how much of the Fiscal Recovery Funds they can use to cover 'revenue losses due to the pandemic.'
- States have "broad latitude" in how to spend the funds that fall under this provision. They must be used to provide government services, which Treasury defines (on p. 60) to include a wide range of services and investments such as spending to provide education and health care, as well as the maintenance or pay-as-you-go funding of infrastructure projects, modernizing cybersecurity systems, and environmental remediation.

Premium pay rules encourage states and other governments to provide premium pay primarily to lower paid workers. ***(see pp. 45-51)***

- States and other governments may use the Fiscal Recovery Funds to provide "premium" pay – on top of regular pay – of up to $13 per hour and up to $25,000 per worker.
- Treasury defines essential work eligible for premium pay as "work involving regular in-person interactions or regular physical handling of items that were also handled by others."
- Treasury also seeks to prioritize workers who likely would have difficulty covering health costs associated with getting sick. To this end, the guidance requires that states and other governments provide written justification if they want to provide premium pay to any worker whose average pay is more than 150% of the state or county's average wage (whichever is higher).
- Treasury encourages the funds to be used to provide retrospective premium pay for essential work performed since the beginning of the pandemic, but the funds may also be used for prospective work performed during the health emergency.
- For examples of states that implemented premium pay programs last year, and further discussion see: https://www.brookings.edu/blog/the-avenue/2021/04/06/with-federal-aid-on-the-way-its-time-for-state-and-local-governments-to-boost-pay-for-frontline-essential-workers/.

Rules around water, sewer, and broadband infrastructure investments
(See pp. 62-78)

- Recipients may use the funds for water, sewer, and broadband infrastructure projects.
- They have broad latitude about what water and sewer projects they can fund. Any project is eligible if they can receive assistance through existing EPA revolving funds for it. Treasury "encourages recipients to consider projects to replace lead service lines" and "encourages recipients to consider green infrastructure investments and projects to improve resilience to the effects of climate change."
- Broadband infrastructure investments must be targeted to unserved and underserved households and businesses, as defined in the guidance. Treasury encourages broadband projects associated with local governments, non-profits, and co-operatives. As noted above, recipients can use the funds to help low-income people afford internet access.
- Treasury encourages recipients to "use strong labor standards, including project labor agreements and community benefits agreements that offer wages at or above the prevailing rate and include local hire provisions."

Other allowable, not allowable, and limits on certain uses

- States <u>can</u> use the funds to replenish UI trust funds up to the amount that was in the fund on January 27, 2020 and to repay loans taken from the federal government to pay UI benefits between January 27, 2020 and the date on which the Interim Final Rule is published in the Federal Register, which is expected in a matter of days. *(See p. 32 and p. 140.)* Note: we do not consider this use a priority; its primary effect would be to reduce future employer taxes when funds are needed now to help people and to reduce racial and class inequities.

- States <u>cannot</u> use the funds for: *(see pp. 42-43)*
  - ✓ Deposits into a rainy day fund or other reserves, or into a pension fund
  - ✓ To pay off debt or settle legal disputes
  - ✓ For general infrastructure investments (beyond broadband, water and sewer infrastructure). States can use the Fiscal Recovery Funds for infrastructure projects that respond to a specific public health need (e.g. facilities for distributing vaccines or lead abatement projects in low-income areas) or address a specific negative economic impact of COVID (e.g. affordable housing development). They also can use the funds for other, more general infrastructure, by using the portion of their funding allowed to cover lost revenue in the pandemic. They cannot spend on general infrastructure beyond that.

The rules governing the net tax cut provision likely will allow most state tax cuts except for ones that produce large revenue losses without equivalent spending cuts
(See pp. 81-96)

- Baseline is fiscal 2019 state tax revenues adjusted for inflation each year. The definition for "tax revenues" is based on the Census Bureau's definition (see p. 88 and p. 135).
- If a state or territory's tax revenues in subsequent fiscal years are above this baseline, then state/territory is assumed to have seen no net tax reduction. Since tax revenues generally outpace inflation and have grown much more quickly than inflation over the last year, this method likely means that states that wish to cut taxes will have significant room to do so without running afoul of the rule.

- If a state or territory's tax revenues in subsequent fiscal years are below the baseline, they may still not run afoul of the provision if they show that they cut spending by an equivalent amount or if they raised other revenues to make up for the tax cut.
- If the cost of tax cuts enacted in a given fiscal year totals to less than a de minimis amount (defined as 1% of the baseline tax revenue amount), the state does not run afoul of the provision. *(Note: many improvements in state Earned Income Tax Credits will likely fall under this de minimis amount. Treasury says in the guidance it determined the 1% threshold based on the average historical cost of EITC improvements. See p. 90.).*
- If a state or territory enacts tax cuts in a fiscal year that total to more than the de minimus amount and they are unable to document equivalent spending reductions or revenue increases, then they are subject to losing an equivalent amount of the Fiscal Recovery Funds.
- The guidance includes a detailed description of how these calculations are made – see pp 81-96.
- The IRF reiterates earlier Treasury guidance that conforming to federal tax law changes, such as the American Rescue Plan's increase in the Earned Income Tax Credit, is considered exempt from the net tax cut provision.

Treasury encourages community engagement
(See p. 9)

- In its guidance, Treasury explicitly, "urges State, territorial, Tribal, and local governments to engage their constituents and communities in developing plans to use these payments, given the scale of funding and its potential to catalyze broader economic recovery and rebuilding."

Providing income and services regardless of immigration status

- The American Rescue Plan does not require government entities or grantees to ask about immigration status when using the Recovery Funds, and such status checks prevent many people from getting help, including non-immigrants who may not have ready access to documents proving their status. Strong reasons exist to believe that no such test is required and this view is supported by Treasury's not including any such requirement in the IFR. For more information, see this memo: https://drive.google.com/file/d/1426VOd_ma28w3BidqPM2qNfpRObcvu_m/view