“Disadvantaged Communities” and Affordability Criteria Fact Sheet

Key Takeaways

- State Revolving Funds (SRFs) often do not reach overburdened communities due to significant barriers, including:
    - Limited technical capacity to develop a project, lengthy application processes, and financial constraints in funding pre-development project costs or verifying ability to repay loans.
    - Overly broad (or narrow) criteria for defining disadvantaged communities eligible for additional subsidies, or other policies that determine the kind of assistance provided and how SRF assistance is distributed within the state, can lead to the inequitable distribution of SRF assistance.
- About half (49 percent) of funds appropriated through the Bipartisan Infrastructure Law (BIL), must be provided as additional subsidies to communities that meet the state’s affordability criteria or that qualify as a state-defined disadvantaged community.
- Each state defines disadvantaged communities (DAC) and affordability criteria for its SRFs. Therefore, state advocates should ensure that their state’s DAC and affordability criteria accurately capture and prioritize overburdened communities. It is also important to ensure that these are not overly broad, otherwise the limited amount of funds available for grants/principal forgiveness will be spread too thin.

SRF Basics: Equitable Implementation of State Revolving Funds

States have significant discretion to determine:

1. which communities benefit from Drinking Water (DWSRF) and Clean Water (CWSRF) State Revolving Funds;
2. the amount of funding distributed as grants or principal forgiveness;
3. which projects are prioritized to receive additional subsidization; and
4. how loan and grant/principal forgiveness funding is distributed across proposed projects.

For more information, go to www.srfadvocatesforum.org

Each state is required to establish DAC definitions and affordability criteria to direct additional subsidies to communities most in need.* However, other policies determined by the states also influence whether SRF assistance is distributed equitably. For example, how projects are ranked for the allocation of assistance and caps on the amount of additional subsidies each community receives can undercut the equitable distribution of principal forgiveness. This fact sheet focuses on how states define DACs and affordability criteria. See EPIC's briefing on state policy frameworks for additional detail on policy choices of SRF administration.

Useful Terms

Additional subsidization: Awards with more generous terms come in three forms:

1) **Grants** – An award of financial assistance that does not have to be repaid. If an applicant is awarded a grant, there are other laws, regulations, and requirements that the state must follow. More information regarding EPA grants can be found here.

2) **Principal Forgiveness** (PF) – An award in which a portion of a loan is forgiven and does not need to be repaid. While PF works similarly to a grant, it does not follow federal grant reporting requirements, therefore reducing administrative costs. States develop criteria to determine which projects qualify for principal forgiveness.

3) **Negative Interest Rate Loans** – An award that reduces the total repayment amount – this is uncommonly used by states.

Under the Clean Water Act, states must consider income, unemployment data, and population trends when formulating CWSRF affordability criteria – states can include additional criteria as well. These affordability criteria are used to identify public water systems and/or service areas within public water systems that would benefit from additional subsidization in order to reduce the burden placed on ratepayers to repay a loan. The Clean Water Act requires states to provide between 10–30 percent of their annual CWSRF funding as additional subsidy to projects that meet the state's affordability criteria or other environmental objectives. Congress has sometimes included additional requirements for further additional subsidies when it appropriates CWSRF funds.

The Safe Drinking Water Act (SDWA) requires states to define "disadvantaged community" (DAC) to assist water systems that would otherwise face financial, managerial, and technical constraints if they were only able to receive loans from the DWSRF. The Safe Drinking Water Act requires states to provide between 12–35 percent of their annual DWSRF funding as additional subsidy to DACs. Congress has sometimes included additional requirements for further additional subsidies to DACS when it appropriates DWSRF funds.

In addition, states must provide 49 percent of funds appropriated through the BIL for general supplemental DWSRF and lead service line replacement as grants or principal forgiveness to state-defined DACs. States must also provide 49 percent of general supplemental CWSRF funds appropriated through the BIL to projects that meet the state's affordability criteria, or which meet other environmental or sustainability objectives.

* Because additional subsidy does not revolve back to the SRF, program administrators must balance need against the state's reduced lending capacity in later years. However, states can provide principal forgiveness to the maximum allowed by federal law and then increase their lending capacity by issuing bonds against their SRF programs. To 'leverage' the funds in this way in practice, bond proceeds are deposited in the SRF and debt service payments would be made from future SRF revenues.

A state may use the same method in determining their CWSRF affordability criteria and DWSRF DAC definition, or they may use different methods. Always check your state's DWSRF and CWSRF Intended Use Plans (IUP) to ascertain how these two similar but separate concepts have been defined by your state.

If a community is identified as a DAC or meets affordability criteria, they may receive additional benefits for their projects, including longer loan terms, lower interest rates, higher priority ranking, and/or additional subsidization in the form of principal forgiveness or grants.

Constraints of Common Indicators Used for Affordability Criteria – Population and Income

The two most common indicators states use to establish DAC and affordability criteria are population size and median household income (MHI). But these are insufficient for identifying and prioritizing the most overburdened communities within a state.

Definitions based solely on population size can be a barrier to overburdened communities because the size of a community does not correlate well with its financial capacity, which is more relevant to a community's need for additional subsidization. To illustrate this point, consider a large community with a high poverty rate. In general, using population size as one metric of a points matrix or sliding scale approach tends to be preferable to using a strict population cut-off to determine eligibility for additional subsidies.

The Median Household Income metric (MHI) refers to the middle income level of a defined community—meaning 50% of that community earns more income and 50% earns less income. Because many households that would be most financially burdened likely fall below the median for their community, using MHI as the primary tool to determine affordability is ineffective.

Additional Criteria to Consider

There are many factors shaping a community's ability to pay for water infrastructure projects, and states should consider additional indicators to provide a clearer understanding of where additional subsidization and other support would be most beneficial. For example:

- **Flexible Spatial Boundaries:** Many states apply affordability criteria and DAC definitions to entire areas served by a water system, thereby missing pockets of poverty within water systems that also serve moderate income and affluent neighborhoods.

- **Economic Indicators**, such as the Lowest Quintile Income threshold, which measures the severity of poverty; Unemployment Rate, which measures the share of population unable to pay for water services; or the Poverty Rate, which measures the prevalence of poverty.

- **Social Vulnerability Indicators**, such as social determinants of health, level of formal education, population with disability; population under 5 and over age 65; and linguistic isolation.

- **Environmental Risks and Burdens**, such as proximity to wastewater discharge; proximity to Superfund sites; level of flooding risk; proximity to an impaired water body; percentage of failing decentralized systems; groundwater contamination; and exposure to lead pipes.

To rectify the historical and persistent underinvestment and disinvestment of majority-Black and other communities of color, many advocates would like to see states use **race and ethnicity** as indicators for DAC and affordability criteria. There is currently a concern that explicitly using race and ethnicity as indicators would be legally prohibited. In their place, additional criteria (i.e., Social Vulnerability Indicators, Environmental Risks and Burdens, and Economic Indicators) can serve as proxies to not only direct resources to communities most in need but to ensure that new investment does not replicate and amplify existing disparities. To that end, several states have already started using environmental justice mapping tools, including EJScreen, the CEQ's Climate and Economic Justice Screening Tool, and state-level mapping tools.

It's important to consider the mix of criteria used in each state to ensure that the end result is not overly restrictive or expansive. For example, states can choose to use in/out criteria (i.e., communities that meet X criteria are qualified as DACs). Other states, like Wisconsin, can instead adopt a scaled scoring system to accord points for various criteria to rank communities' according to their DAC scores. The ranking enabled by a scaled scoring system allows states to prioritize communities according to their relative need and award a higher percentage of project costs as grants and principal forgiveness to those with the highest DAC scores. See EPIC's briefing for further discussion of in/out criteria versus scaled scoring systems.

Finally, it is important to consider not only the kinds of indicators used, but also the thresholds used for eligibility. If DACs and affordability criteria are defined too broadly, this can lead to additional subsidies being spread too thinly across a large number of communities including some with relatively moderate needs, rather than targeted to communities most in need.

Advocacy to Secure SRF Funding for Communities with Greatest Need

1. **Check out Existing Resources:** Appendix E of the EPA's Implementation Guidance provides suggestions for states to develop strong DAC definitions and affordability criteria, as well as recommended indicators and thresholds for criteria commonly used.

2. **Identify the criteria, indicators and thresholds for your state:** Identify which criteria are used to define "disadvantaged community" and affordability, including the indicators and thresholds used for these criteria, by looking at your state's most recent Intended Use Plans (IUPs) for the DWSRF and CWSRF. See examples of this in the SRF Advocacy Toolkit.

3. **Advocate for changes to your state's DAC and/or affordability criteria**: Work with advocates across your state to help ensure that overburdened communities fall within your state's DAC and affordability criteria. Communicate with your state SRF program staff through public comments on state IUPs and by scheduling meetings with them to provide suggestions on how they define DACs and affordability criteria. This is critical in getting grant/principal forgiveness funds for your community's water infrastructure project.

4. Connect to other communities and advocates within your state through the SRF Advocate Forum and check this spreadsheet for links to comments others have provided on IUPs in your state and other states.

Additional Resources

DWSRF Disadvantaged Community Definitions: A Reference for States | US EPA, 2022

A 50-State Survey of State Policies and Decision Makers to Help Ensure Federal Investments Go to "Disadvantaged Communities" Under Biden's J40 Initiative | Lawyers for Good Government, 2022

A New Era for the Drinking Water State Revolving Funds: Identifying Ways to Better Assist Disadvantaged Communities | ASDWA

EPIC briefing on SRF State Policy Framework (*forthcoming*)