

KENTUCKY RECLAMATION GUARANTY FUND 2022 STATE FISCAL YEAR ANNUAL REPORT



Kentucky Reclamation Guaranty Fund Commission
300 Sower Boulevard
Frankfort, Kentucky 40601

December 1, 2022



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KRGF MISSION

The Kentucky Reclamation Guaranty Fund (KRGF or Fund) is an interest-bearing account established for the purpose of providing additional monies for the reclamation of forfeited coal mining operations where the permit-specific performance bonds are insufficient for the Commonwealth to complete reclamation to program standards. Participation in the Fund is mandatory for all companies mining coal in the Commonwealth, with certain exclusions. The Fund is sustained through the annual assessment and collection of coal tonnage and acreage fees paid by participating companies, as well as accrued interest.



KRGF HISTORY

The United States Office of Surface Mining, Reclamation and Enforcement (OSMRE) issued a report in January 2011 entitled “National Priority Oversight Evaluation, Adequacy of Kentucky Reclamation Performance Bond Amounts”, following a lengthy study of Kentucky’s bonding requirements. The study determined Kentucky bonds were inadequate to complete reclamation for a significant number of bond forfeitures. On May 1, 2012, OSMRE sent Kentucky a Part 733 letter notifying that its reclamation bonding program was deficient, which required immediate and long-term steps to ensure bond amounts are adequate to complete reclamation upon forfeiture.

Kentucky addressed the letter’s demands by adopting regulatory amendments that increased individual bond amounts, which became final September 2012. In addition, The Energy and Environment Cabinet (Cabinet) proposed the establishment of the KRGF during the 2013 session of the General Assembly. On March 22, 2013, the legislation was passed by the General Assembly and signed into law by the Governor.

On July 1, 2013, the KRGF, administratively attached to the Cabinet, was established, along with the KRGF Commission (Commission) to administer the Fund. The legislation also established the Office of the Reclamation Guaranty Fund (ORGF), attached to the Department for Natural Resources (DNR), to perform administrative functions in support of the Commission.

The Kentucky Bond Pool, established by KRS 350.700, and the Kentucky Bond Pool Commission, established by KRS 350.705, were abolished. All assets, obligations, and liabilities of the former bond pool were transferred to the KRGF.

The Cabinet, on behalf of the Commission, filed new regulations 405 KAR 10:070, 405 KAR 10:080 and 405 KAR 10:090 that became effective on November 7, 2013. Amendments to 405 KAR 8:010, 405 KAR 10:001 and 405 KAR 10:015 were also filed. These amendments and regulations were necessary to enact the requirements of the statute and further detail the duties and functions of the Commission and the ORGF. In November 2014, the Cabinet, on behalf of the Commission, promulgated 405 KAR 10:025. The regulation provides the Commission the authority to issue bonds to mining companies seeking to succeed to permits issued to members of the former Kentucky Bond Pool for which the Cabinet has initiated bond forfeiture proceedings. This ability to issue bonds to the industry at large can result in a savings to the KRGF in that a viable successor company will complete mining and reclamation operations on a permit at no cost to the Fund and reduce the environmental impacts of an unreclaimed mine site in a timely manner.



KRGF COMMISSION

The Commission is comprised of seven members representing the Cabinet, coal, financial, and insurance industries. Members of the coal industry represent small, medium, and large coal producers with respect to the tonnage mined on an annual basis. Representatives from the financial and insurance industries have experience related to the coal industry. In accordance with KRS Chapter 350.506, the Commission currently meets on a quarterly basis, unless otherwise necessary.

In State Fiscal Year 2022, KRS 350.506 was amended to clarify that members of the KRGF Commission representing the coal mining industry are representatives of coal mining permittees that participate in the fund, allowed for smaller sized operators to be selected to represent different sized operators if a larger operator could not be found to serve and deleted obsolete language regarding initial appointments and meetings.

The Commission is comprised of the following:

Rebecca Goodman	EEC Cabinet Secretary	Chairman of the Commission
Kelly Short	Richmond, KY	Blackhawk Mining, LLC
Charles Justice	Pikeville, KY	Wayland Land Company, Inc.
Lyman Hager	Lexington, KY	RFH, PLLC
Coal Permittee Representative	Vacant	
Insurance/Banking Representative	Vacant	
Insurance/Banking Representative	Vacant	

ORGF STAFF

The Office of the Reclamation Guaranty Fund (ORGF) is the governmental agency statutorily mandated and charged with the administration and execution of the Kentucky Reclamation Guaranty Fund (KRGF), on behalf of the Kentucky Reclamation Guaranty Fund Commission.

The ORGF employs the following individuals:

Jeff O'Dell	Executive Director
Joe Adcock	Staff Assistant
Wendy Bohn	Executive Staff Advisor
Environmental Scientist IV	Vacant





DUTIES AND FUNCTIONS OF THE COMMISSION

In accordance with KRS Chapter 350.509, the Commission is charged with the review, recommendation, and promulgation of regulations necessary to:

- Monitor and maintain the fund;
- Review and assign classification of mine types;
- Establish a structure for the payment of fees and assessments;
- Establish a structure for processing claims and making payments;
- Establish the mechanisms to review the viability of the fund;
- Set a schedule for penalties for late payment or failure to pay fees and assessments;

In addition, the Commission, through the ORGF, performs the following functions:

- Notifies permittees of suspension or reinstatement of fees;
- Conducts an audit of the fund every two years or more frequently if Commission deems necessary;
- Performs an actuarial study every two years or more frequently if Commission deems necessary;
- Authorizes expenditures from the fund;
- Reports to the Governor and Interim Joint Committee on Natural Resources and Energy annually;
- Conducts investigations to verify reporting, payment, and other activities of permittees; and
- Brings actions as necessary in Franklin Circuit Court against any permittee for the recovery of funds spent by the Commission by reason of forfeiture of that permittee.



PROVISIONS AND REQUIREMENTS OF THE KRGF

- As required by KRS 350.515, the Commission assessed Initial Capitalization Fees on August 1, 2013. These fees were comprised of an assessment of \$1,500 per permittee (member entity) for every company holding a coal mining permit in the Commonwealth as of July 1, 2013; and an assessment of \$10 per active permitted and bonded acre for all permits held by a permittee, with certain exclusions;
- Permittees that were members of the former voluntary Kentucky Bond Pool continue to receive bond subsidies by the Fund for existing permits and for new permits, subject to certain restrictions;
- New permittees, having never mined coal in the Commonwealth and becoming members of the Fund after July 1, 2013, are required to pay a one-time fee of \$10,000 prior to issuance of their first permit.

ANNUAL CLASSIFICATION

In January 2022, all eligible permits in the state were classified for the purpose of collecting annual tonnage and acreage fees to maintain a revenue stream for the Fund. In accordance with KRS 350.518, these fees are comprised of:

- 7.57 cents per ton for “Surface” coal mining operations, including auger and highwall mining;
- 3.57 cents per ton for “Underground” coal mining operations;
- Permits approved for both methods of operation (“Combination”) will pay a tonnage fee according to the predominant method of extraction;
- \$10 per bonded acre for permits classified as “Non-production”. Examples of non-production permits are: preparation plants, coal refuse fills and impoundments, haul road only permits, load-outs, and permits that only contain acreage for mine maintenance and other support facilities; and
- \$6 per bonded acre for permits classified as “Dormant”. Dormant permits consist of all remaining permits that have not achieved an initial phase of bond release or did not produce or mine and sell coal in a calendar quarter.

Permits, and increments of permits, that have received at least a Phase I bond release or are undisturbed are exempt from these fees.

Annual Classification fees may be paid for the entire year or paid on a calendar quarter basis, with payments due within thirty days of the close of the quarter. Pursuant to 405 KAR 10:070 Section 4(1)(a) and (d), failure to submit a report and/or fees by the due date shall subject permittees to penalties of five (5) percent of the original fee or minimum penalties of \$100.00 for each month or fraction thereof elapsing between the due date and the date on which the payment is submitted.

Figure I provides the distribution of the permits according to classification at the beginning of calendar year 2022.

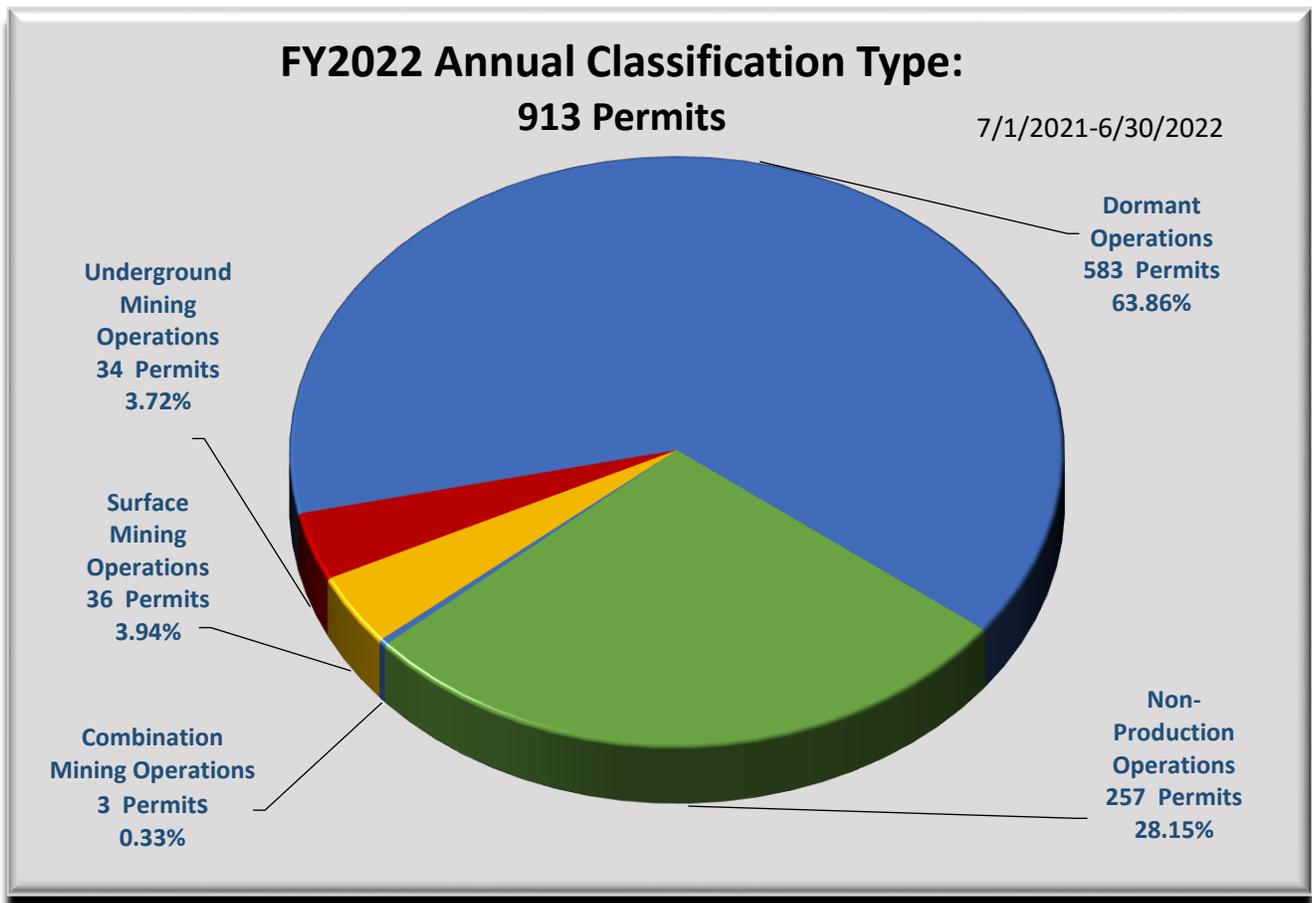


FIGURE 1

In 2022, payments to the KRGF were received for acreage fees, tonnage fees, membership fees and penalties. Figure 2 shows the distribution of Net Fees Collected in each classification.

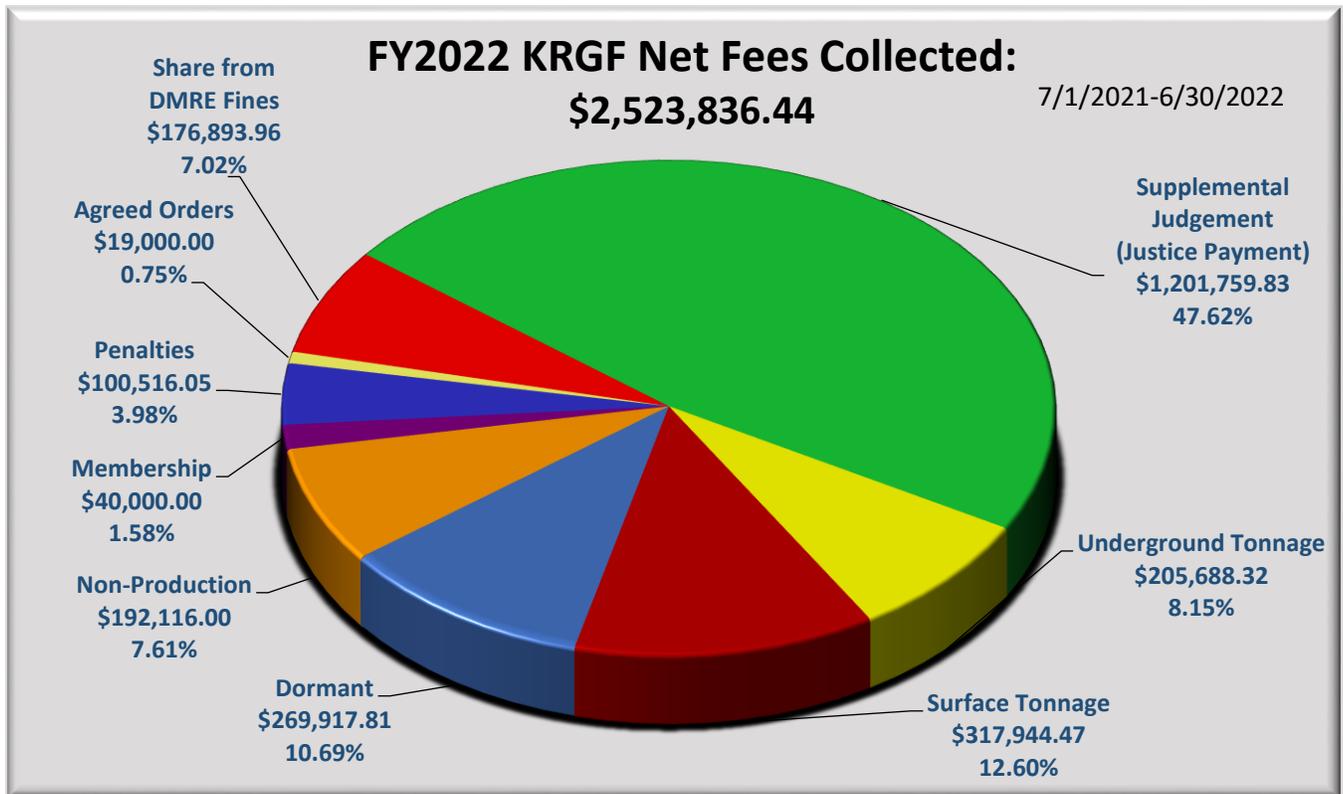


FIGURE 2

Table 1 demonstrates the distribution of tonnage of coal mined and sold for the production classifications and that mined and sold under the dormant and non-production classifications, as of June 30, 2022.

KRGF CLASSIFICATION	SURFACE PRODUCTION	UNDERGROUND PRODUCTION
Surface Mining Operations	3,214,549.05	0
Underground Mining Operations	1,856.88	5,798,080.65
Combination Mining Operations	46,359.69	446,054.92
Dormant Mining Operations	761,980.57	363,698.83
Non-Production Operations	0	15,811.50
Total	4,024,746.19	6,623,645.90

TABLE 1

KRGF BONDING ACTIVITY

As previously mentioned, members of the former Kentucky Bond Pool receive bond subsidization from the KRGF for existing and new permits. Existing permits continue to pay permit-specific bonds at a rate of \$500/acre, while new permits issued after July 1, 2013 pay permit-specific bonds at a rate of \$2,000/acre. The KRGF provides the remainder of the total original bond amount.

Table 2 shows the KRGF bonds written and posted to former Kentucky Bond Pool members from July 1, 2021 through June 30, 2022:

NUMBER OF PERMITS	NUMBER OF BONDS	BONDED ACRES	BOND AMOUNT
6	20	214.77	\$638,200.00

TABLE 2

Table 3 shows the Bond Release Activity for permits held by former Kentucky Bond Pool members from July 1, 2021 through June 30, 2022:

BOND RELEASE PHASE	NUMBER OF PERMITS	ACREAGE AFFECTED	BOND LIABILITY REDUCTION
Phase I	2	491.31	\$923,800.00
Phase II	1	229.57	\$209,700.00
Phase III	4	368.21	477,800.00

TABLE 3

KRGF AUDIT

In accordance with the requirements of 350.509(3), an audit of the KRGF is required for the first five years of operation of the Fund. The first five years have been completed and published by the Auditor of Public Accounts (APA). The KRGF was most recently audited for SFY2022 and no programmatic issues or concerns were found. The audit can be found on the Kentucky Auditor of Public Accounts (APA's) website (<https://auditor.ky.gov/>).

KRGF INVESTMENT STRATEGY

At the close of state fiscal year 2022, the balances of Fund 6385, 6389, and 240A were \$42,049,838.67, \$13,516,494.60, and \$93,857.79 respectively. Table 4 and Figures 3 and 4 display the amount of interest/funds these three accounts earned or lost during state fiscal year 2022.

OFF-BUDGET FUND 6385 & 6389 INTEREST LOST	ON-BUDGET FUND 240A INTEREST EARNED
(\$1,037,659.85)	\$127.84

TABLE 4

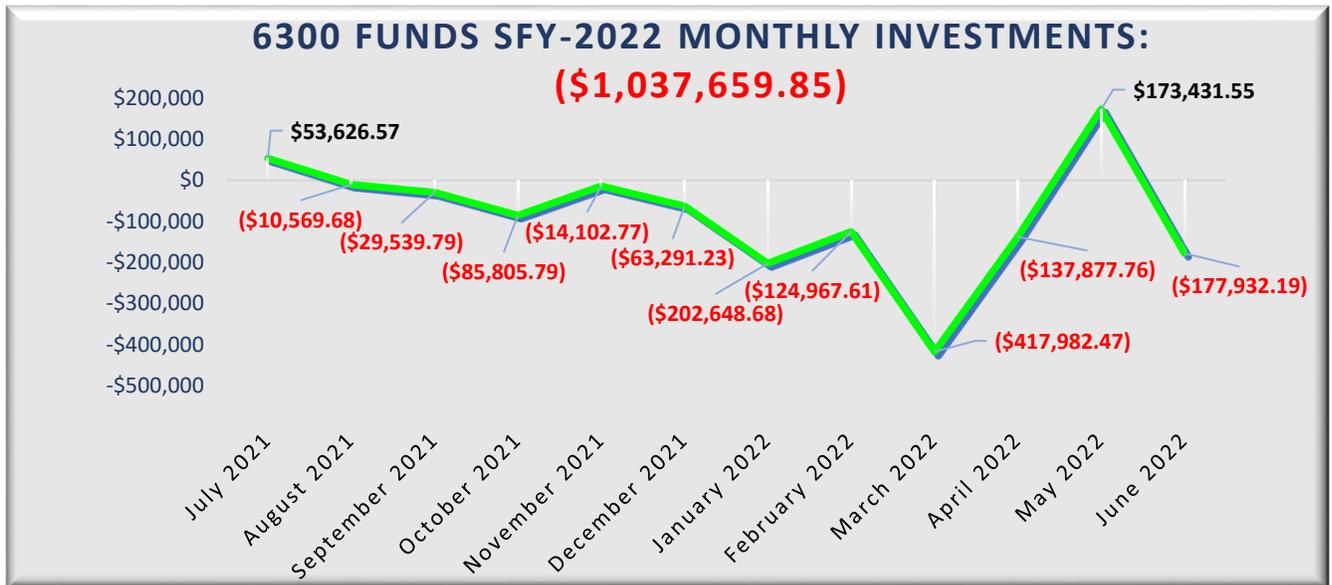


FIGURE 3



FIGURE 4

* Please see pages 15 and 16 for Investment Protocol and Performance explanation.

Investment Protocol and Performance:

Funds held by the Commonwealth are required by statute to be invested and the responsibility for that investing resides with the State Investment Commission (SIC) and Office of Financial Management (OFM) within the Finance Cabinet (KRS 42.500; 200 KAR 14.011, 14.081, 14.091). Agencies do not determine how their funds are invested and only decide which pool their funds are in; Limited Term (Lower Risk, Lower Return) or Intermediate Term (Higher Risk, Higher Return).

Funds are heavily restricted in the types of assets the Office of Financial Management (OFM) is allowed to invest the funds into and all funds tied to each pool are invested into the same thing regardless of amount, agency, fund type, etc.

The KRGF is currently invested in both the Limited Term and Intermediate Term Investment Pools:

Limited Term Pool (Fund 6389 - Bond Forfeiture Obligations and Fund 240A - Operating Budget)

- Limited Term Pool Management: Mimics money market mutual funds.
 - The investments in the Limited Term Pool are:
 - U.S. Treasuries and Agencies
 - Money Market Securities
 - Repurchase Agreements
 - Money Market Mutual Funds

The Limited Term Pool has performed based on the benchmark, changing 6 basis points since 2011. Despite the fluctuations month-to-month, it has recently shown a positive return. Although volatility is often focused on, positive, consistent, high-grade, short-term returns are achieved in this pool.

Intermediate Term Pool (Fund 6385 - Fees Collected)

- Intermediate Term Pool Management: Managed as an enhanced cash bond mutual fund.
 - The investments in the Intermediate Term Pool are:
 - U.S. Treasuries and Agencies
 - Mortgage-Backed Securities
 - Asset-Backed Securities
 - Corporate Debt (don't currently do)
 - Money Market Securities
 - Repurchase Agreements
 - Municipal
 - Money Market Mutual Fund

What is posted as negative earnings is indicative of the last year or year-and-a-half of rates increasing. It takes a few years for some securities to mature and then rates go up, they are effective.

They mature at the full value, so unrealized gains are never capped, and unrealized losses are not a real loss. Accounting just shows fluctuations.

Investment Protocol and Performance (continued):

- 6389 Account:
 - Month-to-month shows negatives because when rates rise, there will be monthly postings of negatives, but overall, for a year or two duration, they mature. The good thing is if rates go down, held securities produce more. If rates go up when maturities mature, they can be re-invested and can buy higher rates. Unrealized gains are not real money since security is held in the losses. The State Investment Commission (SIC) is mandated to do it this way. It is also important since there are hundreds of millions of dollars moving in and out of investment accounts daily and if there is an outflow and SIC has to sell and take a loss, they want to protect the account.

- 6385 Account:
 - The accounting book loss in 2022 shows a big decline in overall market rates. Real earnings are the actual income. A 2% security is the income being made on the securities held. The fees that are de minimis to the average balances, which are about 6 or 7 basis points, are really the unrealized monthly earnings. The unrealized is just a durative of increasing rates and an accounting calculation on what it would be worth if all securities were sold. That will not happen since SIC rarely sells security, only for liquidity reasons. The funds will be recouped as each security matures, along with producing real earnings. In a negative loss accounting calculation, maturities will mature, SIC will re-invest at a higher interest rate, so it produces more in the real earnings column. The negative unreal earning will go away since it is just a mandatory accounting method. When rates increase, that would be the value if sold.

The Federal Reserve Board (FED) controls interest rates within the market. Due to the COVID-19 pandemic, the FED cut interest rates to zero in early 2020 to help mitigate damage to the economy. Investments can only be made at current rates in the market when there are investable dollars and market rates literally change by the second.

Due to the pandemic's economic impacts, yields in this market have hit rates that are unprecedented and both the Limited Term Pool (Treasury bill) and Intermediate Term Pool (Treasury notes) have taken a sharp decline over the last year. As such, accounts statewide within the Commonwealth experienced this decline in interest along with the KRGF.

KRGF MONIES USED FOR RECLAMATION OF FORFEITED MINE SITES.

In accordance with its statutory mandate, the Fund provides additional money to assist in the reclamation of forfeited mine sites. The Division of Abandoned Mine Lands (DAML), under the DNR, is the agency responsible for performing reclamation on behalf of the Commonwealth of Kentucky on all bond forfeitures. During State FY-2022, two (2) permits were forfeited for a total amount of \$3,085,300.00. During that same period, the ORGF transferred permit-specific original bonds for the reclamation of four (4) permits to the DAML in the amount of \$433,105.30. (Tables 5 and 6).

In state fiscal year 2022, the Fund provided excess money in the amount of \$526,500.15 needed to cover reclamation costs above the original bond collected for three (3) forfeited mine sites. All told, in state fiscal year 2022, the ORGF transferred a total of \$959,605.45 to the DAML for the reclamation of forfeited mine sites (Table 6).

PERMITS FORFEITED	PERMITS RECEIVING PAYOUTS FOR RECLAMATION	PERMITS NEEDING EXCESS FUNDS FOR RECLAMATION
2	4	3

TABLE 5

2022 Bond Forfeiture and Reclamation Revenues and Payouts				
BOND FORFEITURE MONIES RECEIVED	ORIGINAL BOND MONIES TRANSFERRED TO AML FOR RECLAMATION	EXCESS FUNDS TRANSFERRED TO AML FOR RECLAMATION	TOTAL TRANSFERRED TO AML FOR RECLAMATION	UNSPENT ORIGINAL BOND MONIES RETURNED FROM KRGF TO FINANCIAL INSTITUTIONS
\$3,085,300.00	\$433,105.30	\$526,500.15	\$959,605.45	\$0.00

TABLE 6

CASE STUDY OF KRGF FUNDED DAML RECLAMATION

J & M EQUIPMENT AND CONSTRUCTION 918-0168 / JOHNSON COUNTY, KENTUCKY	
Original Performance Bond Forfeited	\$121,700.00
Original Bond Money Used for Reclamation	\$121,700.00
Excess Funds from KRGF Needed for Reclamation	\$30,913.35
Total to Complete Reclamation	\$152,613.35

TABLE 7



MINE CONDITION AT TIME OF BOND FORFEITURE



CURRENT CONDITION UPON COMPLETION OF RECLAMATION BY DAML

KRGF FINANCIALS

The KRGF and the associated ORGF operate as separate accounts and both receive only restricted funds and federal funds. No general fund monies are received or expended by either account.

The KRGF Fund is an off-budget account and receives revenue from coal mining entities with operations within the Commonwealth of Kentucky. Revenue for the Fund during state fiscal year 2022 consisted of membership fees, annual classification and production/tonnage fees, late payments/penalties, interest earned and a federal grant.

The KRGF began state fiscal year 2022 with a Fund balance of \$52,200,050.33. Revenues into the Fund (Interest, Regulatory, Bond Forfeiture and Overpayments) totaled \$4,584,221.62, while Expenses out of the Fund (Refunds, Bond Forfeiture Payouts and Non-Forfeiture) totaled \$1,217,938.68. This brought the state fiscal year 2022 ending Fund balance to \$55,566,333.27 (Table 8).

Month	Interest Earned	Regulatory Revenues	Bond Forfeiture Revenues	Over-payments	Refunds	Bond Forfeiture Expenditures	FUND Expenses Non-Forfeiture	Fund Balance
Beginning KRGF Fund Balance 7-1-2021:								\$52,200,050.33
July	\$53,626.57	\$43,649.82	\$497,800.00	\$0.00	(\$4,133.23)	(\$599,246.80)	(\$254,200.00)	\$51,937,546.69
August	(\$10,569.68)	\$226,949.04	\$0.00	\$2,485.20	\$0.00	\$0.00	\$0.00	\$52,156,411.25
September	(\$29,539.79)	\$22,561.22	\$0.00	\$800.50	\$0.00	\$0.00	\$0.00	\$52,150,233.18
October	(\$85,805.79)	\$57,407.20	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$52,121,834.59
November	(\$14,102.77)	\$1,386,543.31	\$2,587,500.00	\$0.00	\$0.00	\$0.00	\$0.00	\$56,081,775.13
December	(\$63,291.23)	\$24,835.24	\$0.00	\$6.72	\$0.00	\$0.00	\$0.00	\$56,043,325.86
January	(\$202,648.68)	\$92,435.02	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$55,933,112.20
February	(\$124,967.61)	\$188,950.95	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$55,997,095.54
March	(\$417,982.47)	\$25,966.21	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$55,605,079.28
April	(\$137,877.76)	\$62,708.80	\$0.00	\$5,995.50	\$0.00	\$0.00	\$0.00	\$55,535,905.82
May	\$173,431.55	\$200,220.78	\$0.00	\$200.00	\$0.00	(\$99,132.60)	\$0.00	\$55,810,625.55
June	(\$177,932.19)	\$194,800.96	\$0.00	\$65.00	\$0.00	(\$261,226.05)	\$0.00	\$55,566,333.27
Totals	(\$1,037,659.85)	\$2,527,028.55	\$3,085,300.00	\$9,552.92	(\$4,133.23)	(\$959,605.45)	(\$254,200.00)	\$55,566,333.27

TABLE 8

ORGF FINANCIALS

Administration of the KRGF is executed through an On-Budget Account utilized by the ORGF to pay for the personnel and related operating expenses of the ORGF and the KRGF Commission.

Expenditures are monitored and monies are transferred either quarterly or as necessary from the KRGF to the ORGF to cover operating expenses. The State Fiscal Year 2022 beginning budget for the ORGF was \$1,815,700.00.

The budgetary needs of the ORGF are consistently reviewed and adjusted as necessary to meet the needs of the agency (see Table 9).

July 1, 2021 through June 30, 2022

BUDGET ITEMS	BUDGETED	EXPENDITURES	BALANCE	NOTES
Personnel	\$1,761,300.00	\$504,849.30	\$1,256,450.70	Includes Staff, Audit, Actuarial Study and Legal Services
Operating	\$ 54,400.00	\$ 47,676.93	\$ 6,723.07	Includes IT, SMIS, Invoicing and KRGF Web Portal
Year-to-Date Total	\$1,815,700.00	\$552,526.23	\$1,263,173.77	

TABLE 9