House
Legislative
Analysis
Section

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REVITALIZING MICH. CITIES

House Bill 4718 (Substitute H-1)
Sponsor: Rep. James M. Middaugh

House Bill 4720 (Substitute H-2)
Sponsor: Rep. Michael J. Griffin

House Bill 4721 (Substitute H-1)
Sponsor: Rep. Tom Alley

First Analysis (6-10-93)
Committee: Conservation, Environment and Great Lakes Affairs

THE APPARENT PROBLEM:

In its decades-old flight from urban to suburban areas, industry has historically left behind a trail of contaminated soil and groundwater. It has only been in the past two decades that state and federal governments have made efforts to force polluters to clean up these sites. However, in many areas the effect of toxic cleanup legislation has been, in fact, to force many owners to abandon these properties, while some government policies actually encourage and subsidize the development of undeveloped suburban areas to the detriment of older urban areas. In some cases, property owners fear exorbitant cleanup costs: the costs for cleaning up one site can be millions of dollars! Many businesses refuse to undertake cleanup because the costs would drain away substantial amounts of money or force them into bankruptcy. Others refuse because they either did not cause the contamination, but are held responsible because they own the land upon which the contamination occurred; or they are responsible for only a portion of the contamination, but are held liable for the entire cost of cleanup. In addition, many businesses are wary of risking capital by lending money to, or locating, businesses at sites where contamination may have occurred, for fear of being held responsible for possible future cleanup costs. Because of this, areas that contain previous sites of industrial or manufacturing facilities experience less development. (Many contaminated properties that have been abandoned by their owners have reverted, because of unpaid taxes, to the state or to the local unit of government.)

In April, 1992, a citizen advisory group -- consisting of representatives from local governmental units; from labor, business, environmental groups; and from the legal and academic professions -- was appointed to examine the impact of state environmental laws and policies on urban sprawl, and to review approaches for the reuse of contaminated urban properties. Specifically, the advisory group focused its findings and recommendations on Michigan's Environmental Response Act (MERA), and the site reclamation program funded under the Environmental Protection Bond Implementation Act. The advisory group concluded that, although Public Act 234 of 1990 (See BACKGROUND INFORMATION), the "polluters pay for cleanup" bill, was designed to spur redevelopment by providing measures designed to assist local governments in urban redevelopment, there is a great deal of misunderstanding and ignorance about risk, liability costs, and the availability of state assistance for the cleanup and reuse of contaminated sites. In particular, many local governments have been unaware of, or unable to use, many of these measures. Although they are often willing to take a leadership role in attracting new development and to encourage reinvestment in contaminated properties, local governmental units often find themselves without the knowledge, power, or resources to address the environmental concerns raised when redevelopment proposals are made. In turn, investors are discouraged, since they are uncertain about the costs and time involved in cleaning up contaminated sites. Also, although

Michigan's current environmental law, Public Act 307 of 1982, contains protections for commercial lending institutions to reduce their risk in making loans for urban development, they, instead, practice "greenlining" of potentially contaminated properties since they believe that Public Act 307's measures and current federal regulations are not adequately protective. In addition, some government policies have encouraged and subsidized the development of suburban areas, and environmental regulations -- intended to protect the public health and the environment -- often discourage reinvestment in cities and encourage development in suburban fringe areas, where irreplaceable farmland, open space, and wildlife habitat is used up. The advisory group noted that uncertainty on behalf of local governmental units and the private sector must be eliminated, and better information distributed on liability laws and cleanup requirements if reinvestment in contaminated urban areas is to proceed.

Among the recommendations made by the advisory group in its January, 1993, "Revitalizing our Michigan Cities" report to a special legislative ad hoc committee were the following:

1) Recognizing that commercial lending institutions limit loans in urban areas where the property involved is contaminated, or suspected of being contaminated, since they fear potential liability for the contamination under Michigan's Environmental Response Act and the federal Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), the advisory group recommended incorporating into MERA portions of new Environmental Protection Agency (EPA) rules (entitled "National Oil and Hazardous Substances Pollution Contingency Plan; Lender Liability under CERCLA," 40 CFR 300.1100 [1992]) that redefine who is liable under CERCLA in a manner more favorable to the lending community. In order to encourage commercial lending institutions to market contaminated property following foreclosure, the advisory group also recommended incorporating into MERA a portion of the new EPA rules that would permit a lending institution to transfer to the state property on which there has been a release.

2) Recognizing that, under CERCLA, all lenders -- insurance companies, pension funds, foreign banks, and federal agencies and automobile finance corporations, such as GMAC, as well as commercial lending institutions -- are allowed to foreclose on contaminated property without assuming liability for cleanup, the advisory group recommended expanding the definition of "commercial lending institution" to include all lenders.

3) Recognizing that not all sites that are identified under MERA as sites of environmental contamination and eligible for funding under the Site Reclamation Program and Environmental Protection Bond funds can demonstrate that they have "measurable economic benefit" potential, the group recommended increasing the amount of grant funds currently allocated to sites that demonstrate "economic development potential" instead.

4) As a tool to attract private reinvestment in contaminated properties, the state should allow a municipality to transfer its liability exemption to subsequent purchasers if certain conditions are met.

Legislation has been proposed that would incorporate the advisory group's recommendations into current environmental laws, in order to encourage the redevelopment of urban areas.

THE CONTENT OF THE BILLS:

House Bills 4718, 4720, and 4721 would amend various acts to clarify the liability of certain entities for environmental contamination.

Under the Environmental Response Act certain entities are, by definition, exempt from liability as an "operator" or "owner" of a facility where a hazardous substance has been stored or released. Among those excluded are state and local governments that have acquired ownership of a facility involuntarily through, for example, bankruptcy proceedings. House Bill 4718 would amend the act (MCL 299.614c) to permit such an entity to transfer its exempt status, under certain circumstances, to a subsequent purchaser or lessee of a facility. Such a transfer could not be made to a person who, at the time of transfer, may be liable for response activity costs at the facility. Further, the state or local unit of government would be required to have an environmental assessment of the property conducted to evaluate the nature and extent of a release, to inspect permanent structures for the presence of a hazardous substance, to estimate the necessary response activity costs, and to compile information for establishing use restrictions that would assure the protection of public health and safety. A state or local unit of

government would also have to establish that the purchaser or lessee proposed to develop the facility according to an approved economic development plan, and that sufficient funds would be generated to pay for response activities consistent with the proposed uses of the facility, that, at a minimum, assured protection of public health and safety. Otherwise, the local unit of government would be required to record deed restrictions on future uses of the facility, requiring "institutional controls" to assure protection of public health and safety. In addition, the local unit of government would be required to submit a written transfer proposal to the Department of Natural Resources (DNR) to document compliance, and to publish a notice of the proposal. The DNR would hold a public meeting on the proposal, if requested, and would decide, within 45 days following the publication of the meeting, whether the transfer were consistent with the requirements of the bill. Following the transfer of an exemption from liability under the bill, the exemption could be transferred to a subsequent purchaser if: the initial transferee complied with the provisions of the act, response activities had been completed, and any deed restrictions of future uses of the property were recorded. The bill would state that a transfer of an exemption from liability would not protect an owner or operator from liability for a subsequent release of a contaminant.

Under the Environmental Protection Bond Implementation Act, money in the Environmental Protection Bond Fund is allocated to finance environmental protection programs, including components for toxic waste cleanup. The act provides for the disbursement of $40 million for the clean-up of sites that have been identified under the Michigan Environmental Response Act as having toxic contamination, provided that the sites have economic development potential; and of $5 million to a) investigate and verify that vacant manufacturing facilities and abandoned industrial sites, that have not been identified under the Michigan Environmental Response Act, are free of environmental contamination, and b) to make loans to local units of government to redevelop and reuse these locations. House Bill 4720 (MCL 299.678) would amend the act to reduce the first amount to $35 million, and would specify that the funds be used at locations having "measurable economic benefit," i.e., where permanent jobs were created or retained, private capital invested, or the tax base increased, as determined by the Commission of Natural Resources. The bill would also increase the latter amount to $10 million, and would specify that this amount be used to provide grants to cities, villages, or townships (or to a county on behalf of a city, village, or township), that had been identified, as of May 1, 1993, as being eligible under the Neighborhood Enterprise Zone Act, to determine whether property in a community was contaminated, and, if so, to characterize the nature and extent of the contamination. The $10 million could also specifically be used to provide grants to either Marquette, Houghton, Sault St. Marie, or Escanaba. To qualify for a grant, the property would have to be located within an eligible community that had previously received less than $1 million in total grants, not including a grant that had resulted in "measurable economic benefits." Further, the study of the property would have to include an estimate of the cost of cleaning up the contamination in relation to the value of the property if it were cleaned up, and any future potential limitations on the use of the property based on current environmental conditions. The property would have to have "demonstrable economic development potential," but a specific development proposal would not be required.

If, after 18 months, the commission determined that the $10 million allocation was not likely to be expended according to the provisions of the bill, then $5 million of the money would be reallocated for the clean-up of contaminated sites. In addition, a community could retain funds that were recovered from a person identified as being liable for the contamination of a site and used on projects that were eligible, as determined by the DNR, for clean-up funding. If recovered funds were not spent within two years they would be returned to the fund to be used for the investigation of vacant manufacturing facilities and abandoned industrial sites. When accounting for the use of recovered funds, eligible communities could itemize deductions for site preparation and other costs directly related to the reuse of a site funded under this provision.

The Environment Response Act attributes liability for the cleanup of contaminated sites. Under the act, a commercial lending institution that has not participated in the management of a facility, prior to assuming ownership or control as a fiduciary under state or federal banking codes, is not held liable as an owner or operator of the property unless the institution exercised sufficient involvement to control the handling of a hazardous substance, or unless the institution, its agent, employee, or a

person retained by the institution, caused or contributed to the release of a hazardous substance. House Bill 4721 would amend the act (MCL 299.603 and 299.612a) to include under the act's definition of "commercial lending institution" an insurance company, a motor vehicle finance company, a foreign bank, a retirement fund, and a state or federal agency authorized to hold a security interest in real property. The provisions of the bill would apply to an insurance company that is regulated under the Insurance Code; to a motor vehicle finance company with net assets in excess of $50 million that is regulated under the Motor Vehicle Finance Act; and to a retirement fund that is regulated by state law or by a pension fund regulated under federal law with net assets in excess of $50 million.

House Bill 4721 would also define actions, which, under the act, would constitute "participation in the management or operational affairs of a facility." Generally, an institution that has not participated in the management of a facility prior to assuming ownership is not held liable for cleanup costs as an owner or operator of the property unless the institution has been involved to the extent that it controlled the handling of, or contributed to the release of, a hazardous substance. The bill would specify that an institution or person holding a security interest in a facility would be considered to have participated in its management if they actually participated in the management or operational affairs of a facility in acts "that exceed the mere capacity to influence, or ability to influence, or the unexercised right to control facility operations." In addition, an institution or person holding a security interest in a facility would be considered to have participated in its management if, while the borrower was still in possession of the facility, the institution or person exercised decision-making control over the borrower's environmental compliance; undertook responsibility for the borrower's hazardous substance handling or disposal practices; or exercised control at a level comparable to that of a manager in a manner that encompassed the enterprise's day-to-day decisions regarding either its environmental compliance, or "all, or substantially all" of its other operational aspects. However, the following would not constitute participation in the management of a facility:

**The mere capacity to influence, or ability to influence, or the unexercised right to control facility operations.

**An act or omission prior to the time when ownership was held primarily to protect a security interest.

**Undertaking or requiring an environmental inspection of the facility in which ownership was to be held, or requiring a prospective borrower to undertake response activities at a facility, or to comply with any applicable law -- either before or after the time that ownership was held -- primarily to protect a security interest.

**Actions consistent with holding ownership primarily to protect a security interest, whether such authority is contained in a contract or other document.

**Engaging in policing activities prior to foreclosure, unless such actions involve "participation in the management of the facility," as defined under the bill. Permissible actions would include requiring the borrower to undertake response activities at the facility during the term of the security interest; requiring the borrower to comply or come into compliance with federal, state, and local and environmental laws; or securing or exercising authority to monitor or inspect a facility or the borrower's finances. ("Workout" activities [defined under the bill to refer to actions by which an institution or person with a security interest sought to prevent a borrower from defaulting or diminishing the value of the security] conducted prior to foreclosure and its equivalents would remain within the exemption provided that such action did not involve "participation in the management of the facility.")

The bill would also clarify the conditions under which an institution could transfer to the state property on which there had been a release. Under the bill, a commercial lending institution could immediately transfer property on which there had been a release, or threat of release, to the state after it complied with all of the following:

**The facility was listed or advertised as being for sale within 9 months following foreclosure and for a period of at least 120 days.

**The institution took reasonable care in maintaining and preserving the real estate and permanent fixtures.

**The institution provided the DNR with a complete copy of the foreclosure environmental assessment, and all other available environmental information relating to the facility.

**The institution complied with an order issued by the DNR to undertake response activities because of a release of a contaminant to the department's satisfaction.

**The institution undertook appropriate response activities to abate any threat of fire, explosion, or exposure to hazardous substances.

BACKGROUND INFORMATION:

Public Act 307 of 1982, and, later, Public Act 234 of 1990, attempted to provide enforcement mechanisms and incentives to encourage polluters to pay for cleanup measures. Public Act 307 created the Environmental Response Act to eliminate environmental contamination at sites polluted by hazardous materials; to make those responsible for the contamination pay for the cleanup; and to create an environmental response fund, from which funds were to be disbursed for the state's remedial actions, including providing matching funds for federal "Superfund" cleanup activities. Public Act 234 of 1990, the "polluters pay" legislation, provided the Department of Natural Resources (DNR) with enforcement tools to order the cleanup of contaminated sites, and provided incentives -- such as loans to small businesses and exemption from liability for innocent victims who bought contaminated sites -- to help them do so. The act was designed to spur redevelopment by allowing contaminated sites to be cleaned up quickly.

Under Public Act 234, owners and operators of facilities are liable for the costs of response activities. State and local governmental units are not liable for costs or damages as a result of actions taken in response to a release from a facility. Generally, an institution that has not participated in the management of a property prior to assuming ownership or control of property as a fiduciary under state or federal banking codes is not held liable as an owner or operator of the property unless the institution exercised sufficient involvement to control the owner's or operator's handling of a hazardous substance or the institution caused or contributed to the release or threat of release. Neither is a commercial lending institution liable if it did not participate in the management of a facility, but simply acquired it to realize a security interest, and the property was either residential or agricultural; or the institution acquired ownership or control involuntarily, through a court order, for example; or the institution would otherwise be liable solely because it has once owned the facility but did not own it at the time of disposal of a hazardous material, and had acquired ownership or control prior to August 1, 1990. However, under the act, a lending institution that acquires a property through foreclosure may not dispose of it unless the institution provides the department with a copy of the results of a foreclosure environmental assessment and agrees with the department regarding the property's disposition. (If the lending institution and the department are unable to reach an agreement, then the institution may only transfer the property to the state.) The lending institution is not liable once it establishes that it has met the requirements of this provision.

FISCAL IMPLICATIONS:

According to the Department of Natural Resources, the bills have no fiscal implications for the state. (6-9-93)

ARGUMENTS:

For:

It is widely agreed that there is a need to redevelop areas that already have roads, sewers and other public improvements to make these sites attractive to developers. One of the most critical problems in older urban areas is pervasive environmental contamination. However, abandoning these areas in favor of urban sprawl makes no sense economically or environmentally. An environmental regulation task force that was created in May, 1992, by the Southeast Michigan Council of Governments (SEMCOG) to study the problem defined urban sprawl as "sprawling, low-density growth at the suburban fringe, and concurrent disinvestment and abandonment of older/urbanized communities." And in its January, 1993, "Revitalizing our Michigan Cities" report, a citizen advisory group formed to examine the impact of state environmental laws and policies on urban sprawl noted: "There is a building consensus that continued urban sprawl needlessly consumes limited natural and fiscal resources, and encourages further deterioration of the quality of life and economic viability of our older urbanized areas." The bills are an attempt to reverse the growth patterns that have led to suburban sprawl,

and to direct government policy, instead, toward redeveloping former industrial and commercial sites.

For:

The citizen advisory group formed to examine the impact of state environmental laws and policies on urban sprawl reported that state grant programs to local units of government for redevelopment of contaminated sites need to be targeted to older urban areas so that local governments can then market the sites with completed environmental evaluations. House Bill 4720 would redirect $5 million from the Environmental Protection Bond Implementation Act to communities that were eligible for funding under the Neighborhood Enterprise Zone Act and to four towns in the Upper Peninsula that contain contaminated sites. These funds would be used to determine the level of contamination of property so that the sites could be marketed for new developments. In addition, House Bill 4718 would reduce the liability of those who purchased contaminated property for redevelopment by allowing state and local governments to transfer their exempt status to subsequent purchasers or lessees. This would reduce the uncertainty currently faced by developers and investors when considering potentially contaminated properties that are part of urban reinvestment proposals, and would enable more units of government to receive environmental grants to assist in marketing contaminated sites.

Against:

House Bill 4721 would broaden the act's definition of "lender" to include insurance companies, auto finance companies, retirement funds, foreign banks, and federal agency lenders, as well as banks, savings and loans, and credit unions. This would extend protection from liability to more lenders to encourage them to market contaminated properties after they have foreclosed on them. House Bill 4721 also adopts some portions of new Environmental Protection Agency (EPA) rules (entitled "National Oil and Hazardous Substances Pollution Contingency Plan; Lender Liability under CERCLA," 40 CFR 300.1100 [1992]) that redefine who is liable under CERCLA in a manner more favorable to the lending community. The rules protect lenders from liability for cleanups of contaminated property that has been subject to foreclosure when the lender has not actively participated in the management of a facility. (Specifically, the new EPA rules define the term "owner" or "operator." These terms were never defined under CERCLA; instead, Congress combined the terms and has defined them to mean "any person owning or operating a site of environmental contamination." Congress also exempted from the definition "a person who, without participating in the management of a vessel or facility, holds indicia of ownership primarily to protect his security interest in the vessel or facility." Under the new EPA rules, a lender cannot be defined as being a "participant" in the management of a facility unless the lender actually engages in the management of a facility to the extent that the lender could control the borrower's hazardous substances handling and disposal practices). However, the bill would also delete from the act language that establishes that the holder of a security interest in property would not be considered an "operator" of the property, as that term is defined under the act, while retaining language specifying that such a person would not be considered an "owner" of the property. It is confusing and inconsistent to afford lenders protection from liability if they are "owners" of property, while excluding them from the same protection if they are "operators." The bill should be amended to eliminate this confusion and conform to the new EPA rules by reinstating language to exclude from the definition of "operator" those lenders who don't participate in the management of a site. Otherwise, few lenders will be encouraged to make loans in urban areas with potential contamination problems.

Response:

House Bill 4721 already expands liability protection for those lenders who function as "owners" and hold property for security on a loan; however, lenders should not be allowed to "operate" a facility and not be subject to liability. In addition, Michigan's attorney general has challenged the 1992 EPA rule that defines who is liable for the cleanup of contaminated sites under CERCLA. (Attorney General Kelley has been designated one of Michigan's trustees for natural resources under CERCLA. In addition, he is authorized to bring the action on behalf of the state and its governmental entities.) The attorney general has petitioned the U.S. Court of Appeals for the District of Columbia Circuit for a review of EPA's authority to promulgate rules, as well as its interpretation of the lender liability rule. The attorney general's brief cites a case brought by the United States on behalf of EPA in 1990 (United States v Fleet Factors Corp., 901 F.2d 1550, 1557 [11th Cir. 1990], reh'g en banc denied, 911 F.2d 742 [11th Cir. 1990], cert.

denied 111 S.Ct. 752 [1991]), in which the court opined that a secured creditor could incur liability without being an operator if the creditor participated in the financial management of a facility to a degree indicating a capacity to influence the corporation's treatment of hazardous wastes. According to the petition, the EPA ruling flies in the face of this decision and contradicts the meaning of the phrase in CERCLA by allowing a lender to maintain a "secured credit" exemption even though it has foreclosed on contaminated property and operated the foreclosed business. The petition goes on to maintain that the EPA is unlawfully shifting the burden of proving the entitlement to CERCLA's secured creditor exemption from secured creditors to plaintiffs, and that its lender liability rule unlawfully exempts lending institutions from the term "operator." Since the definitions for "liability" for contaminated property and for "operator," are a major issue of dispute, lenders should not be granted an exemption from liability as "operators" until the issue has been clarified.

POSITIONS:

A representative of the Michigan Bankers Association testified before the committee in general support of the bills, and also to appeal for an adoption of all the new CERCLA rules adopted by EPA in 1992. (6-8-93)

The Michigan Recreation and Park Association testified before the committee in support of House Bill 4720. (6-8-93)

The Department of Natural Resources supports the bills. (6-9-93)

The Michigan Municipal League supports the bills. (6-8-93)

The Michigan United Conservation Clubs supports the bills. (6-8-93)