

Legislative Analysis



WASTEWATER APPLICATION GRANT FUND

Mitchell Bean, Director
Phone: (517) 373-8080
<http://www.house.mi.gov/hfa>

House Bill 4572 (Substitute H-1)
Sponsor: Rep. John Stakoe

House Bill 4573 as introduced
Sponsor: Rep. Neal Nitz
Committee: Local Government and Urban Policy

First Analysis (4-19-05)

BRIEF SUMMARY: House Bill 4572 would amend the Shared Credit Rating Act to create the Wastewater Application Grant Fund and House Bill 4573 would amend the Natural Resources and Environmental Protection Act to allocate 10 percent of the revenue in the Great Lakes Water Quality Bond Fund to the Wastewater Application Grant Fund.

FISCAL IMPACT: These tie-barred bills would earmark 10 percent of Great Lakes Water Quality Bond proceeds to a new fund called the Wastewater Application Grant Fund and used for grants to cover engineering and professional consulting costs incurred by communities as they prepare applications for sewage treatment projects. Aside from reducing the amount available for project assistance, there would not be any additional fiscal impact on the State. These grants, however, would not be repaid to the DEQ (thus reducing dollars available for sewer projects). Local governmental units would be eligible for these grants, and would potentially benefit fiscally if these bills are enacted.

THE APPARENT PROBLEM:

In the November 2002 general election, voter approval of Proposal 2 authorized the State of Michigan to borrow up to \$1 billion to improve the quality of the state's waters by financing sewage treatment works projects, storm water projects, and water pollution projects; authorized the state to issue general obligation bonds; and provided for the repayment of the bonds from the general fund of the state. No more than 10 percent of the water quality bonds can be sold in any one year. Under legislation that accompanied the ballot proposal, proceeds from the bonds were to go into the Great Lakes Water Quality Bond Fund and then distributed as follows:

- 90 percent to the existing State Water Pollution Control Revolving Fund (also known as the State Revolving Fund or SRF) for treatment plant upgrades and expansions, combined sewer overflow abatement, new sewers designed to reduce existing sources of pollution, nonpoint source pollution management, sludge management, and similar efforts.
- 10 percent to a new fund established to make loans to municipalities to help them reduce the flow of groundwater or storm water entering sewer systems or to help them upgrade or replace failing on-site septic systems. This fund is called the Strategic Water Quality Initiatives Fund (SWQIF).

In December of 2003, the first bonds were issued under the provisions of Proposal 2, thus making \$90 million in bond revenue available under the SRF and \$10 million under the SWQUIF. Apparently, however, only \$3 million of the available revenue has been utilized so far. Some feel that local governments are discouraged from applying for loans from the SRF or SWQUIF because the loans cannot be used to cover the costs associated with developing the project plan and initial engineering studies needed for the application process. These costs are estimated to range between \$20,000 and \$50,000. Though comparatively small when the overall design and construction costs can total in the tens of millions of dollars, local governments are still faced with financial uncertainty due to the state's slow economic recovery. Revenue from many funding sources has either been decreased or ended altogether, forcing local governments in turn to cut or end funding for various community projects. Simply put, it is a difficult time for some communities to find up to \$50,000 in order to apply for a loan to fix their outdated sewage treatment and storm water systems.

In an attempt to spur utilization of the revenue generated by Proposal 2, legislation is being offered to create a third fund. This third fund would funnel some of the Proposal 2 revenue into grants that could be used by local governments to cover the upfront costs associated with the application process.

THE CONTENT OF THE BILLS:

The bills are tie-barred to each other, meaning that neither could be enacted into law unless both are enacted.

House Bill 4573 would amend the Natural Resources and Environmental Protection Act (MCL 324.19708) to redistribute the allocations from the Great Lakes Water Quality Bond Fund so that 80 percent (reduced from the current 90 percent) of the bond revenue would be deposited in the SRF, 10 percent in the Strategic Water Quality Initiatives Fund, and the remaining 10 percent in a new Wastewater Application Grant Fund that would be created under House Bill 4572.

House Bill 4572 would add a new section to the Shared Credit Rating Act (MCL 141.1066c) to create the Wastewater Application Grant Fund within the state treasury. Money could be expended from the fund only for grants to governmental units to cover the total cost of engineering and professional consulting when developing the project plan for applying for loan assistance from the State Water Pollution Control Revolving Fund (SRF). Grant funds could not be used for public notice activities, general local government administration costs, or costs associated with educating the public about the proposed project. A governmental unit could not receive more than an accumulated total of \$3 million in grants to use for developing the project plan.

An application and review process would be established by the Department of Treasury. Within 60 days of receipt of an administratively complete application, the applicant would have to be notified if the application was accepted or rejected; if rejected, a written notice containing the reasons for the rejection would have to be sent to the applicant.

A grant agreement would have to be entered into between the department and an approved applicant before the grant money could be released. This agreement would have to require repayment, with interest not to exceed eight percent per year, for any of the following reasons:

- The grant recipient failed to submit an administratively complete loan application for assistance from the SRF within 12 months after the grant was released.
- The grant recipient did not use funding from the SRF for the project after receiving approval for an SRF loan.
- The grant recipient obtained a loan from the SRF, but substantial progress toward implementing the project was not made within 18 months of the issuance of the loan.

If a local government's administratively complete application for a loan from the SRF was rejected, it would not have to repay the grant from the Wastewater Application Grant Fund.

Money or other assets could be received by the state treasurer for deposit into the Wastewater Application Grant Fund, and the treasurer would be responsible for directing the fund's investments. Interest and earnings from the fund investments would be credited to the fund, and money in the fund at the end of a fiscal year would remain in the fund and not lapse to the general fund. The Michigan Municipal Bond Authority within the Department of Treasury would act as fiscal agent for the fund.

BACKGROUND INFORMATION:

State Water Pollution Control Revolving Fund, commonly called the State Revolving Fund (or SRF), is the principal source of water quality assistance to local communities in Michigan. The SRF provides subsidized low-interest loans to municipalities for use in upgrading wastewater treatment systems. Eligible projects include treatment plant upgrades and expansions, combined sewer overflow abatement, new sewers designed to reduce existing sources of pollution, nonpoint source pollution management, sludge management, and similar efforts to address the problems of the state's aging wastewater treatment infrastructure. (Nonpoint sources include runoff from the land and deposits from the air.) Federal funds are channeled to local units through this fund; the state is required to provide a 20 percent match.

The fund is administered jointly by the Department of Environmental Quality and the Michigan Municipal Bond Authority. Municipalities apply for the loans, which are repaid into the fund. Assistance is awarded based on a project priority list developed by the DEQ. According to the DEQ, 240 projects have received \$2.1 billion in loans since 1989.

Proposal 2 of 2002 has the potential to pump up to \$1 billion in additional state revenues into state loan programs to help municipalities to finance various pollution control

projects, with \$900 million slated to go into the SRF and \$100 million into the newer Strategic Water Quality Initiatives Fund (SWQIF).

ARGUMENTS:

For:

By passing Proposal 2 in 2002, voters recognized that a new revenue stream was needed to ensure that efforts to control water pollution by repairing or replacing aging or inadequate sewage collection and treatment systems would succeed. The proposal authorized the state to issue up to \$1 billion in bonds with the proceeds going into two funds to make low interest, subsidized loans to local governments to repair or replace these systems. To date, only \$100 million in bonds has been issued, and only \$3 million of that money has been utilized to accomplish the goals of Proposal 2.

Some feel that one obstacle to applying for a loan from the State Water Pollution Control Revolving Fund (SRF) or Strategic Water Quality Initiatives Fund (SWQIF) is the cost of assembling the application. The application requires submission of a project plan. The initial design and engineering study costs associated with completing an acceptable project plan can range from \$20,000 to \$50,000. Therefore, before a community can even apply for a loan, it must secure the revenue to complete a project plan. Once it secures the loan, it cannot use money from the loan to reimburse itself for the costs spent in developing the project plan.

Due to the state's slow economic recovery, many local governments are facing difficulties funding basic programs such as fire and police services, and have been forced to cut recreation programs and other nonessential services. Though projects to fix wastewater treatment systems and reduce the flow of groundwater or storm water entering sewer systems are essential, some communities may be hard pressed to free up the money needed to cover the expenses associated with the application process.

The bills would provide much needed assistance to local governments by allowing them to apply for a grant to be used in developing the project plan needed to apply for a loan from the SRF or SWQIF. Under certain conditions, such as receiving a loan but failing to make substantial progress in completing the plan's objectives within an 18 month time period, the grant would have to be paid back with interest. By providing local governments with the upfront money needed to complete the loan application process, it is hoped that more communities will avail themselves of Proposal 2 funds.

Against:

A number of objections have been raised to the bills.

** There is some question as to the legality of the proposed legislation. Public Act 397 of 2002 (enrolled House Bill 5892), which was part of the legislative package creating the bond program, amended the Natural Resources and Environmental Protection Act to establish the Great Lakes Water Quality Bond Fund. The bond proceeds are deposited into this fund and money in the fund is to be used only for loans and for the costs of

administering the fund. Since the bills would be funneling 10 percent of the bond proceeds from this bond fund into a grant program, they would conflict with this provision of law and with the type of programs voters believed they were approving. Moreover, since the bonds involve state debt, an opinion is needed from the attorney general and from private bond counsel before the legislation proceeds much further in the legislative process.

**** Under Proposal 2, as much as \$1 billion can be generated for actual sewage and water treatment projects, whereas the bills will funnel \$90 million into a grant program. Once that money is spent, there will be no more money to pay for grants for local governments to apply for funding from the SRF and SWQIF, plus there will be \$90 million less to fund needed projects. Due to the way these two funds are leveraged as revolving funds, that same \$90 million could fund about \$270 million in projects over the next 20 years. In short, taxpayers would get more bang for their buck if the bond proceeds remained earmarked for loans only.**

**** Loans generated under provisions of the Drinking Water Act allow the money to be used to cover costs associated with the application process. A better and simpler approach would be to also allow loans from the SRF and SWQIF to cover project planning costs needed to apply for the Proposal 2 funds.**

**** House Bill 4572, by amending the Shared Credit Rating Act, would require the Department of Treasury to carry responsibility in reviewing grant applications. Since these applications would entail evaluating sewage and water treatment projects, it would be more appropriate for the Department of Environmental Quality to handle such tasks.**

**** The low figure cited by proponents of the bills to justify turning bond money meant to be dispersed in the form of loans into grants is misleading. It is true that there has been only one issuance of bonds representing \$100 million and that only a small amount has been used so far, but proceeds from Proposal 2 are not the only revenue in the SRF. The fund also receives some federal money with an accompanying state match. Indeed, since the proposal passed in 2002, at least 53 projects have received loans from the fund with more in the works. All totaled, 240 projects have been funded via loans from the SRF without any help to pay for the application costs.**

The overall financial uncertainties faced by many municipals due to a weak economy may be the leading cause of hesitancy to commit to a major sewage project, rather than just the inability to come up with \$50,000 or less to complete a project plan to apply for a loan from the SRF or SWQIF. As the economy strengthens, more applications are sure to follow.

POSITIONS:

A representative of the Michigan Municipal League testified in support of the bills. (4-13-05)

A representative of the Michigan Townships Association indicated support for the bills. (4-13-05)

A representative of the Michigan Association of Counties indicated support for the bills. (4-13-05)

A representative of the Department of Environmental Quality testified in opposition to the bills. (4-13-05)

A representative of Clean Water Action testified in opposition to the bills. (4-13-05)

A representative of the Michigan Environmental Council testified in opposition to the bills. (4-13-05)

Legislative Analyst: Susan Stutzky
Fiscal Analyst: Kirk Lindquist

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.