

Legislative Analysis



WATER QUALITY GRANT PROGRAM

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

House Bill 4572 as enrolled
Public Act 254 of 2005
Sponsor: Rep. John Stakoe

Senate Bill 789 as enrolled
Public Act 253 of 2005
Sponsor: Sen. Patricia L. Birkholz

House Bill 4573 as enrolled
Public Act 256 of 2005
Sponsor: Rep. Neal Nitz

Senate Bill 790 as enrolled
Public Act 257 of 2005
Sponsor: Sen. Gerald Van Woerkom

House Bill 5297 as enrolled
Public Act 252 of 2005
Sponsor: Rep. Aldo Vagnozzi

Senate Bill 799 as enrolled
Public Act 255 of 2005
Sponsor: Sen. Liz Brater

House Committee: Local Government and Urban Policy
Senate Committee: Natural Resources and Environmental Affairs

Second Analysis (8-28-06)

BRIEF SUMMARY: As a package, the bills would allow local governments to apply for a grant to be used in developing the project plan needed to apply for a loan from Proposal 2 water treatment funds.

FISCAL IMPACT: The bills would have an indeterminate fiscal impact on the state. See [Fiscal Information](#) for a more detailed analysis.

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 SWQIF. Apparently, however, only \$3 million of the available revenue had been utilized by mid-2005. Some feel that local governments are discouraged from applying for loans from the SRF or SWQIF 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 struggling economy. 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 has been introduced in both the House and Senate to create a program to provide grants to local governments to finance the project plans needed to apply for a loan from the State Water Pollution Control Revolving Fund (SRF) or the Strategic Water Quality Initiatives Fund (SWQIF).

THE CONTENT OF THE BILLS:

Together, the bills would create the Wastewater Application Grant Fund and allow local governments to apply for a grant to be used in developing the project plan needed to apply for a loan from Proposal 2 funds. That 2002 ballot 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 aging or inadequate sewage collection and treatment systems.

The bills are tie-barred to each other, meaning that no one bill could be enacted into law unless all are enacted. (All were enacted and took effect December 1, 2005)

House Bill 4573

The bill would amend Part 197 (Environmental Protection Bond Implementation) of the Natural Resources and Environmental Protection Act (MCL 324.19708) to revise the allocation of money received from the sale of Great Lakes water quality bonds. Currently, the act requires 90 percent of the money in the Great Lakes Quality Bond Fund to be deposited into the State Water Pollution Control Revolving Fund (SRF) and ten percent into the Strategic Water Quality Initiatives Fund (SWQIF).

Instead, the bill would specify that, in aggregate, not more than \$900 million of the money in the Great Lakes Quality Bond Fund could be deposited into the SRF and no more than \$100 million into the SWQIF.

Further, the bill would require bonds that were directly deposited into the SRF or SWQIF to be taken into account for the purpose of determining the allocation and transfer of money as described above.

House Bill 4572

The bill would add a new section to Part 52 (Strategic Water Quality Initiatives) of the Natural Resources and Environmental Protection Act (324.5204a). The bill would establish a program to provide grants to governmental units to cover the cost of developing a project plan in applying for a loan from the State Water Pollution Control Revolving Fund (SRF).

Strategic Water Quality Initiatives Grant Program. Under the bill, the Michigan Municipal Bond Authority (within the Department of Treasury), in conjunction with the Department of Natural Resources, would have to establish a Strategic Water Quality Initiatives Grant Program to provide assistance to municipalities to complete the loan application requirements of Section 5308. The grant program would provide grants totaling not more than \$40 million to eligible municipalities. The program would be subject to all of the following:

- Grants could not cover more than 90 percent of the costs incurred by a municipality to complete an application for loan assistance from the SRF or SWQIF.
- The 10 percent local match would not be eligible for loan assistance from the SRF or SWQIF.
- Grant funds could not be used for general local government administrative activities or activities performed by municipal employees.
- A municipality could not receive more than \$1 million in total grant assistance under the bill's provisions.
- Grants under this provision would be available for projects seeking or intending to seek loan assistance after September 30, 2006.
- The DNR stopped accepting grant applications under this provision two years after the date the first grant agreement was entered into.

Application process. Within six months after the bill's effective date, the DNR would have to establish an application and review process for considering grant applications. The application would have to contain the information required by the DNR and the Michigan Municipal Bond Authority. Within 30 days after receipt of an application, the DNR would have to publish notice of the application on the department's calendar. Within 60 days after receipt of an administratively complete grant application, the DNR would have to notify the applicant in writing whether the application was approved or rejected. If a grant were approved, the DNR and the authority would have to enter into a

grant agreement with the recipient prior to transferring funds. The grant agreement would have to contain terms established by the DNR and the authority and a requirement that the grant be repaid by the recipient, within 90 days of being informed to do so, with interest at a rate not to exceed 8 percent per year, to the authority for deposit into the SWQIF if any of the following occurred:

- The applicant failed to submit an administratively complete loan application for assistance from the SFR or the SWQIF for the project within three years of the grant award.
- The project had been identified as being in the fundable range and the applicant declined loan assistance from the SFR or SWQIF in that fiscal year.
- The applicant was unable to, or decided not to, proceed with constructing the project or opted to finance construction by means other than a grant from the SFR or SWQIF.

Reporting requirements. For each year in which the DNR received grant applications under the bill's provisions, it would have to report by July 1 of that year to the standing committees of the Senate and House of Representatives with primary jurisdiction over issues pertaining to natural resources and the environment and to the Senate and House of Representatives Appropriations Committees on the utilization of funds under Part 52 that had been received from the Great Lakes Water Quality Bond Fund. The report would have to include, at a minimum, all of the following:

- The number of grant applications received under the new Section 5204a.
- The name of each municipality applying for a grant.
- The individual and annual cumulative amount of grant funds awarded, including an identification of whether each award was for the purpose of applying for assistance from the SFR or SWQIF.
- A summary of loan assistance, by year, tendered from the SFR and SWQIF.

Further, the Senate and House Appropriations Committees would have to annually review whether there was sufficient money in the SWQIF to implement Sections 5204a and 5202.

House Bill 5297

House Bill 5297 would add a new section to the Shared Credit Rating Act (MCL 141.1016d) to allow government units to enter into grant agreements under Section 5204a of the Natural Resources and Environmental Protection Act (which would be added by House Bill 4572), and to pledge their limited taxing power as security for repayment of their obligations. The bill specifies that the grant agreements would not be subject to the Revised Municipal Finance Act. Further, repayment obligations of the governmental unit under a grant agreement would not be a general obligation or debt of the governmental unit within the meaning of any constitutional or statutory debt limitation, and would not be subject to any notice or referendum. Finally, grant agreements could be entered into

by the Michigan Municipal Bond Authority and would not be required to be in fully marketable form.

Senate Bill 789

Senate Bill 789 would amend Part 52 (Strategic Water Quality Initiatives) of the Natural Resources and Environmental Protection Act (MCL 324.5204), also known as NREPA, to allow the Michigan Municipal Bond Authority, in consultation with the Department of Environmental Quality (DEQ), to spend money from the Strategic Water Quality Initiatives Fund (SWQIF), upon appropriation, for grants under House Bill 4572.

Senate Bill 790

The bill would amend Part 52 of NREPA (MCL 324.5201) to define "grant" as a grant from the program that House Bill 4572 would establish.

Senate Bill 799

The bill would amend Part 53 (Clean Water Assistance) of NREPA (MCL 324.5301) to include in the definition of "construction activities" actions undertaken in the planning of sewage treatment works, storm water treatment, or nonpoint source projects, and project planning services.

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 (data as of mid-2005 when bills were first analyzed).

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).

FISCAL INFORMATION:

There would be an indeterminate fiscal impact on the State of Michigan, and local governmental units would potentially benefit from the grants authorized by this package. This package of bills would direct revenue from Proposal 2 for grants to local governments to cover the up-front costs associated with the loan application process.

These tie-barred bills would provide funding from the Strategic Water Quality Initiatives Fund to support grants to communities for engineering and professional consulting costs as they prepare applications for sewage treatment projects. The cost of an engineering study supported by these bills is estimated to be between \$20,000 and \$50,000. Aside from reducing the amount available for other fund loans, there would not be an additional fiscal impact on the state. It should be further noted that these grants would not be repaid to the DEQ. The actual fiscal impact on the Strategic Water Quality Initiatives Fund would depend on the number of grants made in a given fiscal year.

ARGUMENTS:

For:

By passing Proposal 2 in 2002, voters recognized that a new revenue stream was needed to help ensure the success of efforts to control water pollution by repairing or replacing aging or inadequate sewage collection and treatment systems. 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. As of mid 2005, when these bills were first being discussed, only \$100 million in bonds had been issued, and only \$3 million of that money had 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. 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. After all, 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. The bill package would address this problem by allowing local governments to apply for a grant to be used in developing the project plan needed to apply for a loan from the SRF or SWQIF.

The bills would work in tandem to create the mechanism needed that would allow local governments to seek a grant to help cover the cost of applying for Proposal 2 funds. In a

nutshell, under the bill package, up to \$40 million of the \$100 million of Proposal 2 revenue earmarked for the Strategic Water Quality Initiatives Fund (SWQIF) could be given to communities in the form of grants to be used to develop project and design plans for various wastewater and storm water projects. These project and design plans are needed to complete the application process for loans from the SWQIF and the State Water Pollution Control Revolving Fund (SRF). The grant program would not apply to applications submitted before September 30, 2006, would only be available for a period of two years, and be limited to no more than \$1 million per municipality. Under certain conditions, such as failing to submit an administratively complete loan application within three years of receiving the grant, 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.

In addition, Senate Bill 799 would now allow municipalities to reimburse themselves from an SRF loan for costs incurred when developing a project plan. This provision will aid those municipalities submitting loan applications prior to the start of the grant program and after it ends, as well as for those projects not meeting the grant program's criteria.

Against:

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 had been only one issuance of bonds representing \$100 million as of mid-2005 and that only a small amount had 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. (These are mid-2005 figures.)

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.

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.