Legal and Practical Issues Associated with Stormwater Construction Permits in the New Economy: Tales from the Recession and Recovery

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The Traditional Stormwater Enforcement Paradigm

- Almost exclusively complaint driven
- Contractors/subcontractors moving too quickly or delays between stages of construction; lack of coordination
- Exceptional weather events
- Lack of clear responsibility for compliance during various phases of construction
  - “Co-permittee” concept devised in response; makes all working parties equally liable for misfeasance/nonfeasance of any single party
- Before advent of MS4 DHEC had uniform enforcement process; purely civil process under PCA
- MS4 program brings county/municipality into mix; local permitting, compliance, enforcement through code officers
The Housing Bubble

- Demand for mortgage based securities $\Delta \uparrow$
- Corresponding increase in new housing starts
- Subdivision construction $\Delta \uparrow$
- Phased method of construction mirrors phased method of financing
  - Phase I land clearing, roads, infrastructure, then construction of residences and completion, then on to phase II; generally loans were phased as well
  - Developments/phases often cross-collateralized
Market Collapse

- Not all at once; not for all projects, all at different stages
- Delays in financing often preceded/triggered events of insolvency
- Most projects were in some level of noncompliance when they became insolvent
- Partially completed, unstabilized sites
Bankruptcy - The World Turned Upside Down

- Noncompliant developer now referred to as “debtor” under “protection” of Court
- Property now referred to “estate” of debtor
- Those seeking relief referred to as “creditors” and “claimants”
- Section 362 of the Bankruptcy statute provides for an automatic stay
  - stays commencement/continuation of judicial, administrative, or other action or proceeding that was or could have been commenced before petition, or to recover a claim against debtor that arose before commencement of case
  - “any act to exercise control over property of the estate”
  - Very narrow police power exception which must be raised in bankruptcy court
Bankruptcy

- Under bankruptcy, any expenditure by debtor is subject to court approval
  - Even if debtor wanted to take action to stabilize site, it cannot, not without court approval
- Very cumbersome; slow, expensive process
- Government cannot discriminate against debtor
  - Example- may not revoke air permit for nonpayment of fees, may not impose fines for noncompliance, may not require action that requires an expenditure without a finding of necessity under the police power exception—and only then with court approval
Upshot:

- Assessment of fines to penalize noncompliance—treated as general unsecured claims and subject to discharge
- Action to force return to compliance highly impractical
  - Will be resisted by debtor and other creditors
- Site conditions remain unresolved and deteriorate
- Secured creditors face risk if they take unilateral action
  - At best, held to be “volunteer” and costs sunk; at worst, held to violate automatic stay
- Creditor taking over project to protect security interest usually faces long delays
Case Study 1

- 2 subdivisions in upstate
- 1 30% finished, the other 60% finished; most of both projects have experienced land disturbance/clearing
- Developer spirals into insolvency during summer, noncompliance noted and increasing as situation becomes more dire
- County enforcement process implemented; code enforcement officer issues summons/criminal complaint against named individual on permit
- Bankruptcy petition filed; County realizes that permittee cannot legally comply; County terminates all efforts at forcing compliance
- Sites remain out of control for months
Case Study 1 (Cont’d)

- Sedimentation ponds silted over 50%, some breached
- Silt fencing gone
- Inlet protection absent
- Stormwater infrastructure clogged with sediment
- Severe erosion
- Cost to resolve problem: in excess of $250,000
- Secured creditor (bank) dealing with distressed asset that is getting worse by the day, a soft real estate market, and will have difficulty reselling asset
Case Study 1- Representing the Creditor

- Cooperative debtor- bankruptcy smooth, deed in lieu of foreclosure
- Debtor agrees to cooperate with creditor
  - Problem- permits not transferrable, permit is an older (easier to comply with) version- NOT/NOI process not simple
  - Creditor faces (theoretical) liability for permit violations if it agrees to be co-permittee
    - Solution: Debtor stays on permit; agrees to allow creditor’s contractors to become co-permittees
    - Work performed, sites stabilized
    - Assets enhanced; marketability improved
Case Study 2- Representing the Redeveloper

- Marina (leased from Corps)
  - Slips, UST, restaurant
- Subdivision project
- Phase I- Town homes on frontage
- Phase II- Individual residences at rear of development
- Individual septic tanks and shared tile field with fund for permanent maintenance of system
Insolvency

- Lease from Corps in jeopardy
- Project stalls halfway through phase I, one unimproved phase II lot sold; 50% townhomes built, several townhomes sold
- Some land disturbance in rear of subdivision, some infrastructure installed
- Sedimentation problems
- Sewage permit noncompliance
  - Maintenance fund looted
  - Possible claims from homeowners
Solution

- Sewer provider available
- Siltation manageable
- Long term redevelopment plans
- Rectify noncompliance
- Stabilize site
- NOT- Debtor had dissolved
- New NOI when development resumes
Case Study 3 - Representing the New Developer

- Stalled subdivision, foreclosure
- Angry, intractable, obstructive prior owner
  - Had filed *lis pendens* on own site to delay/obstruct/frustrate foreclosure
- Would not comply with permit process to add co-permittees
- Lack of transferability/older permit/expiration issues
  - Significant administrative effort would be expended in getting new permit
Solution

- Timing

- Many lots already finished; site permitted before OCRM change to require MS4 submittal

- Had to resubmit to OCRM

- Guidance from DHEC required
Some Thoughts

- Permitting process made more cumbersome because of peculiarities of MS4 program
- Instead of delegated individual permitting authority (as in case of CAA, NPDES point source permitting), delegated authorities are governed as permittees and extend coverage under DHEC general permit
- Added complications of local stormwater regulations creates a patchwork system and lack of consistency,
- Lack of transferability is a serious flaw; need authority for voluntary transfer and involuntary transfer in certain cases
- Status of MS4 delegate receiving authority as permittee, not as independent authority, causes rigidity in implementation
- Concerns over intervention by DHEC, EPA, citizen’s suits
- Fact that coverage under older vintage permits would be more difficult to obtain under new permit is another issue
- Provisions allowing new permittee to become successor without having to reapply
- Standstill provisions needed
- Need for DHEC to wait for next round of permits to fix problems is cumbersome
DHEC Response

- Use of consent orders to provide flexibility; limitations
- Active provision of guidance
- Departure from command/control enforcement response to real-world compliance oriented approach
- Permanent solution for problems as general permits reissued
Questions, Comments?

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