Structural Abandonment Public Policy:

The Michigan Fire Insurance Withholding Program

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Introduction

The removal of blighted structures is often cited as one of the key elements to Detroit's revitalization. Abandoned properties in the Motor City, like many other rust belt communities, have made a significant presence over time, acting as symbols to the decline of a once industrious region. In recent years, with Detroit emerging from bankruptcy in 2014, a more rapid increase in demolition work began to occur, and with that also came the need for major funding avenues. During this time, the Detroit Blight Removal Task Force reported $850 million would be required for neighborhood blight elimination (plus another $500M – $1 billion for commercial sites); since 2014, the city has allocated and received enough funds for about half the price tag, through many state and federal initiatives, including the Hardest Hit Fund, the Michigan State Housing Development Authority, among others. One of these funding sources, outlined through current Michigan policy, is a system named the Fire Insurance Withholding Program. Also known as the Fire Escrow Fund (FEF), the program relieves some of the financial burden for demolishing abandoned, fire-damaged structures in participating municipalities. Abandoned lots and blighted buildings can be susceptible to fires, and in the case of Detroit, many homes fit into this category. After the first comprehensive city-wide parcel survey was conducted in 2014, over 10,000 structures were found to have some form of fire-damage present (Motor City Mapping). Because of these variables, the FEF has been identified as a potentially important tool for eliminating hazardous sites in older communities where abandonment exists. This report will examine the legislative aspect of the Fire Insurance Withholding Program and outline key requirements and processes, providing a background for further research and public policy advancement towards mitigating the negative effects of structural abandonment.

Overview of the Fire Escrow Fund

Established in 1982, Public Act 495 created the FEF under the Michigan Insurance Code of 1956. The law specifies:

> "If a claim is filed for a loss to insured real property due to fire or explosion and a final settlement is reached on the loss to the insured real property, an insurer shall withhold from payment 25% of the actual cash value of the insured real property at the time of the loss" (Sec. 500.2845).

This transpires if the inspected damage reaches above 49% of the insured property value and only when said property lies in a municipality taking part in the program (township, city, or village). This 25% outlined, which has a 2017 maximum of $12,508 for residential properties (adjusted for inflation annually, concurrent with the consumer price index), is placed into a community escrow account by the insurer, where it remains until either the owner completes removal/repairs, or, following 120 days with no evidence of improvements, the municipality can proceed to demolish the structure with the funds made available [see flow chart, pg. 6].

> "If with respect to a loss, reasonable proof is not received by or shown to an authorized representative of the city, village, or township designated by the governing body of the city, village, or township within 120 days after the policy proceeds portion was received by the treasurer, the city, village, or township shall use the retained proceeds to secure, repair, or demolish the damaged or

> destroyed structure and clear the insured property so that the structure and property comply with local code requirements and applicable ordinances of the city, village, or township. […] The city, village, or township may extend the 120-day time period under this subsection" (Sec. 500.2845).

It is the responsibility of the insurance company to notify the municipality when a property loss has occurred that falls under the program. Once a settlement between the insurer and insured has been agreed upon, the company sends notice of withholding to the municipality, after which the municipality can request for the funds so that a check can be processed into the escrow account, again, only to be paid to the property owner or contractor following demolition up to the point that funds are needed to complete work. Interest earned while in escrow can remain with the fund. Anything that might be left over after a municipality has completed removal must be returned to the insured. One other option for funding utilization by the municipality is also outlined by the code in Subsection 7. As it reads,

> "A city, village, or township may retain and use policy proceeds for demolishing any property if on or before the effective date of the amendatory act that added this sentence the authorized representative had not received or been shown reasonable proof within 1 year after the insurer provided notice to the insured under subsection (1) and the insured property has been demolished. The insured may file a civil action against the city, village, or township for the return of the policy proceeds. An action filed under this subsection must be filed within 3 years after the insurer provided notice to the insured under subsection (1) or 1 year

after the effective date of the amendatory act that added this sentence, whichever is later”

Essentially, if a municipality did not keep track of, or demolish a structure within one year, and that structure somehow was demolished without the municipality being aware, then the withheld amount could be used for another demolition, not necessarily one that falls under the FEF. The subsection appears to be very restrictive and would not likely be an available choice in most cases today, but for cities with major abandonment issues and lack of resources/oversight in the past, like Detroit, there may possibly be properties and lots that provide withheld funds fitting into the description above, though actual statistics to this occurrence are currently unknown.

Multiple amendments have been made to the FEF over the past three decades, one of the more significant occurring in 1998. Under this new rule, the program was spilt into two sections of the insurance code, 500.2845 and 500.2227, which added new definitions to participating communities, dividing it based on population size.

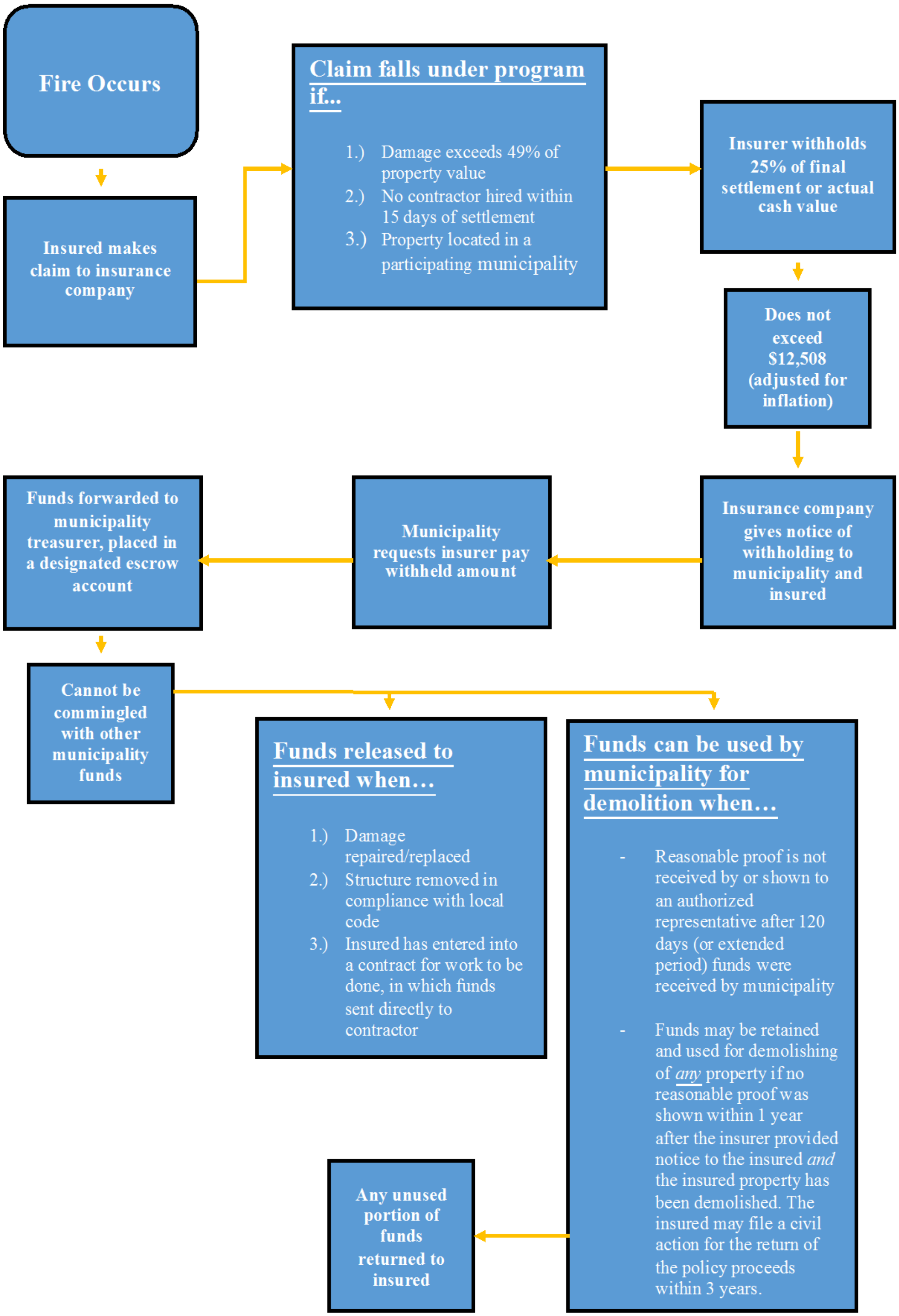
Section 2845 applies to:

- Any municipality of less than 50,000 in population located in counties of less than 425,000.
- Property damage caused by fire or explosion

Section 2227 applies to:

- Counties of 425,000 or more, regardless of the size of the municipality or cities of 50,000 or more, regardless of the size of the county.
- Property damage caused by fire, explosion, and vandalism, malicious mischief, wind, hail, riot, or civil commotion

Fire Insurance Withholding Program Flow Chart



These additions provide a broader meaning to the definition of damage in urban areas (such as communities in Kent, Macomb, Wayne, or Oakland counties), opening up the program to more demolition possibilities in cases of criminal behavior, riot (like the Detroit Riots of 1967), or severe weather (a common summer occurrence in Southern Michigan). Another, more recent amendment was made in 2014 to increase the maximum amount of the 25%[1]. Originally capped at $6,000, the Michigan Legislature increased the limit to $12,508 (adjusted for inflation), meant to cover a larger sum of total demolition costs per home, which averaged $13,774 in 2015 according to the Detroit Fire Report, a yearlong comprehensive study of fires in the city.

Currently, the FEF is overseen by both the Michigan Department of Insurance and Financial Services (DIFS) and each local municipality. The DIFS reviews new program applications, regulates insurance companies, monitors compliance, and maintains a complete list of active municipalities, updated and released quarterly to insurance companies (Fire Insurance FAQ, 2017). The DIFS provides a simple process for municipalities to adopt the program, which includes: passage of a resolution including "specific wording concerning the establishment of an escrow account" (State of Michigan) for legal purposes, filling out an application for approval, and the appointment of a city official to oversee the local FEF. As of January 2018, 649 communities

[1] Passed as Public Act 509, the initial bill (HB 5062) was sponsored by House Representative Amanda Price of District 89-Grand Haven (term-limited, left the house in 2017) and reviewed by the Local Governments Committee. Other cosponsors were from Districts 9, 19, and 31; Rep. Adam Zemke, District 55-Ann Arbor (final term ends in 2019) is the remaining member currently in the house (Michigan Legislature). Future amendments to the program, or new legislation altogether on this topic, could be brought to the attention of representatives from a variety of communities, but especially those who have a municipality participating in the program or deal with property abandonment on a large scale.

participate in the system, about 36% of all Michigan municipalities. Notable examples include Detroit, Lansing, Grand Rapids, Flint, Muskegon, Kalamazoo, and Saginaw (State of Michigan, 2017). Each municipality maintains control over its funds and handles each insurance claim that falls under the FEF without state interference. There is currently no tracking by the state of the overall program's application or the total amount in each FEF. To research a particular FEF, the DIFS's list of participating municipalities contains the name and contact information for the city official who oversees the fund.

Conclusion

Michigan's Fire Insurance Withholding Program was designed to help cities manage and remove dangerous, fire damaged property vacated by owners. In general, structural abandonment has affected many communities in Michigan, as economic and social factors have altered over the past century. Today, many of these same cities have been engaged in demolishing blight to help refocus neighborhoods and prevent more abandonment from occurring. The FEF provides a possible funding opportunity to eliminate a fraction of these lots. For example, Detroit Mayor Mike Duggan expected 400 buildings to be demolished under the program by December 2015 (City of Detroit, 2015). Many structures, though fire damaged, might not be covered by the FEF, and an improvement to the law could be trying to expand its definitions to pull more under its umbrella, such as lowering the required 49% property damage value. The FEF could also be a template for new legislation dealing with structural abandonment and blight beyond fire damage, possibly providing a stable source of funding for future demolitions or other activities. While Detroit is the poster city for abandonment, the FEF also serves a purpose outside those boundaries too. Other cities in the state face similar issues, with varying levels of blight and the need for more demolition funding. Further research should be conducted towards the role of FEF to see if its implementation has been an effective device for funding and removal. The use of the FEF in less populated regions is also a question that can be examined. Does it have a purpose if it is only applied sparingly? Based on the research presented, it might. Knowing that approximately 36% of state municipalities have adopted the Fire Escrow Fund, more districts have the opportunity to include this public policy and can be encouraged to do so. Whether used in a rural township or a larger urban area, the program is straightforward, along with being simple to implement and enforce. Even for places not in decline, it offers a financial safeguard to eliminating hazardous sites and protecting communities.

- **List of all participating municipalities in Program, and contact information for each FEF (as of January 2018):** https://www.michigan.gov/documents/difs/FIWP_464230_7.pdf

- **Application for a municipality to adopt Program**:

- **Link to 2014 amendatory bill and other related documents:** http://legislature.mi.gov/doc.aspx?2014-HB-5862

The statements, findings, conclusions, and recommendations expressed herein are solely those of the respective authors, and do not necessarily reflect the views of Michigan State University

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