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## Cost Recovery Summary

DTSC is committed to fundamental reform in the way it recovers the costs incurred overseeing and investigating the cleanup of contaminated sites and costs incurred performing investigation and cleanup activities. The oversight, cleanup, and other costs incurred by the Department are collectively known as “response costs.” The Department is authorized to recover its response costs from responsible parties. Recovering

response costs is a complex process that goes far beyond simply sending a bill. Historically, DTSC has been better at cleanup than bill collecting. However, DTSC has accomplished much since DTSC embarked on its Fixing the Foundation effort, when it started on an unflinching approach to fixing its cost recovery problems.



### COST RECOVERY HISTORY

DTSC spent more than \$1.9 billion between 1987 and 2013 cleaning up contamination as part of its central mission to protect public health and the environment. That work has been transformational. DTSC has restored contaminated sites to space for parks, schools, homes and businesses. Along with its primary mission, DTSC also has a fiduciary responsibility to the people of California. As a result, DTSC operates on a “polluter pays” principal; those who are responsible for the pollution should pay for regulation or clean up, not the taxpayer. From 1987 through 2013, more than 90% of cleanup costs were recovered or otherwise assigned and accounted for.

On May 31, 2013 DTSC publicly disclosed that its unrecovered response costs were \$184.5 million at 2,700 sites. This was for the 25-year period from July 1987 through December 2012. This amounts to about 10% of the total response costs during this period.

Next, DTSC formed a cost recovery team and began to make sweeping changes. In late 2013, DTSC issued 27 departmental procedures consisting of 276 pages of guidance. In spring 2014, more than 400 employees were then trained on this guidance. Later in 2014, about 200 employees with primary cost recovery responsibilities received additional targeted training. DTSC is continuing its training of employees in small groups on cost recovery procedures.

In addition, DTSC sought help from the California state legislature to help eliminate the cost-recovery backlog. In 2014-15, the Legislature approved 14 limited-term cost recovery positions. Those positions will expire on June 30, 2016. Also, in August 2014, the State Auditor issued findings and recommendations for DTSC’s Cost Recovery program. The Auditor added another year of data and found DTSC had failed to recover \$194 million at 1,661 sites. DTSC uses the Auditor’s numbers as a baseline when we analyze our cost recovery progress.



## HISTORICAL CHALLENGES TO EFFECTIVE COST RECOVERY

There are several factors that contributed to DTSC's uncollected response costs. DTSC didn't have standardized cost recovery procedures until the end of 2013, when it issued the departmental procedures noted above. Further, the computer systems used by staff in the field and accountants in billing weren't linked and information often wasn't shared. As a result, sometimes cleanup would be initiated to protect the public and cost recovery wasn't pursued until later. Finally, project managers, who are the scientists and engineers who oversaw the technical cleanup, were also put in charge of money collection. In order return the technical experts to restoring the environment, DTSC created "Administrative Project Managers" to lead its cost recovery efforts.

## ONGOING AND STRUCTURAL CHALLENGES

DTSC has solved many of the historical challenges but there are some ongoing challenges that remain. Some of these challenges are inherent to the complexities of recovering response costs and some are structural challenges that DTSC must overcome. The ongoing challenges point to the time, expense and complexity of recovering response costs and involve identifying who should pay as "responsible party(s)". DTSC investigates if anyone sent hazardous materials to a site for treatment, storage or disposal, looks at who owns and who once owned the property, and looks at current and past operators on the land and if they had insurance policies.

This task of identifying responsible parties varies with difficulty. For those who transferred hazardous waste to the site, DTSC must establish a connection between an individual and the waste. For past owners and operators, DTSC must document that a release of a hazardous substance did indeed occur during the time they were associated with the site. Companies can have complex ownership structures, sometimes with a host of subsidiaries, divisions, joint ventures and shareholdings. Piercing through each layer takes time and effort.

Once a responsible party is identified, DTSC undertakes the complex process of determining if those responsible have the means to pay. Issues such as bankruptcy complicate the picture, as does determining if an insurance policy might be in force, or even filing a claim against an estate if the party has passed away. Where no viable party remains, DTSC has a separate program fund to cover cleanup costs. All these steps take time, multi-disciplined staff, and money. The following examples illustrate how complex cost recovery efforts can be:

A site called Technichem – in Emeryville – is a company that recycled solvents from many small dry cleaners from 1987 to 2003. DTSC had to pull about 25,000 manifests to determine who sent waste to the site – and how much. The AG's office filed a lawsuit in federal court in 2012. The case is ongoing.

A site called Chemical and Pigment – in Contra Costa – turned out to be a dissolved company. Eventually DTSC discovered insurance policies active during the time that hazardous substances were released. In an attempt to recover costs, DTSC worked with the Attorney General's office to file claims in England.

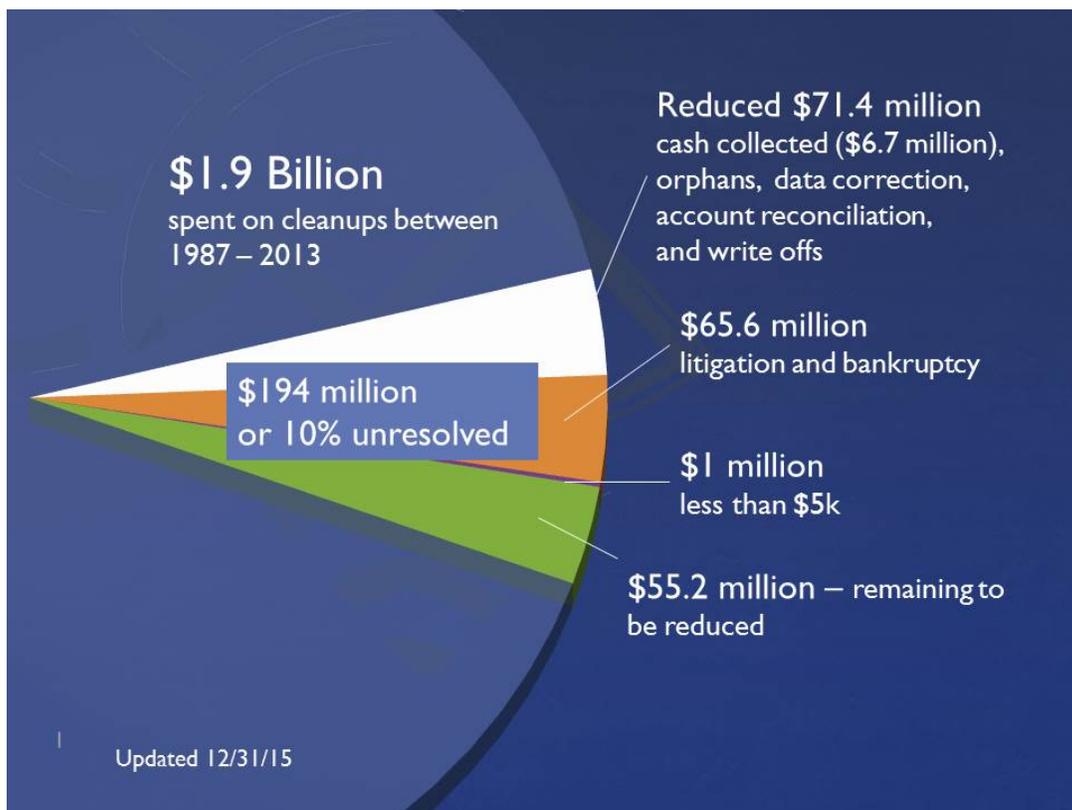


DTSC has to collect its costs within timeframes specified under statutes of limitation. The beginning of the timeframe is based on the time and type of actions taken on each individual site.

The Department also faces structural challenges in sustaining its recent cost recovery success. As mentioned earlier, cost recovery is a labor-intensive process. DTSC received 14 limited-term analyst, fiscal, and attorney positions to address the backlog and sustain cost recovery going forward. These positions will expire in June 2016 and the Department is evaluating options to address that upcoming loss in capacity. A second major structural issue involves DTSC's archaic and unsupported billing system, which is discussed in more detail below.

### COST RECOVERY BACKLOG PROGRESS

DTSC has a number of pathways to clear out unresolved cost recovery cases. The breakdown of the \$194 million and current backlog resolution status is depicted in the pie chart below.



Since the audit was released in August 2014, DTSC has made substantial progress on its backlog, reducing the number of sites from 1,661 to 713 – a 57 percent reduction. The baseline cost recovery figure - the \$194 million reported in the audit - represents both dollars owed as well as data errors. The pie chart above shows that of the \$194 million, the Department has already reduced that amount by \$71.4 million. That reduction includes cash collected, settlements, and data clean up. Because of its



antiquated billing system, DTSC cannot determine how much of that amount is cash collected, but it has identified at least \$6.7 million has been collected since March 2014.

In some cases, DTSC has determined that it won't be able to collect on its costs. Often, there is no viable party who can pay the bill. When DTSC documents that fact, it classifies these projects as "orphan sites." In those cases, DTSC becomes the safety net for California, ensuring that cleanup is paid for and completed. So far, DTSC has confirmed that \$30.7 million of the unrecovered costs is attributable to those orphan sites. Those sites should never have been included on the backlog list; this is a data cleanup issue. Also, DTSC has confirmed that some sites were erroneously placed on the list – they have zero balances.

Beyond the \$71.4 million reduction, DTSC has referred numerous sites to the state Attorney General's office. Sites totaling \$65.6 million are being evaluated for legal action, are in active litigation, or are in bankruptcy. As DTSC continues to analyze its backlog, it is anticipated that more will end up in litigation and will result in dollars collected.

An ongoing challenge is sites where DTSC uses liens to support cost recovery because a lien is not a sole or final solution. Often, a lien will not guarantee money paid because cleanup costs can often far exceed what the land is worth. DTSC has 88 liens recorded on properties throughout the state; the value of these liens totals nearly \$92.8 million but the value of the underlying properties is only assessed at \$25.3 million. In addition, a lien can also have a chilling effect on the ability to sell the land.

After determining that DTSC's top priority cases should be those with balances above \$1 million and those of any amount with an expiring Statute of Limitations date, DTSC has prioritized its sites and is working methodically down the list. DTSC has identified that there are 23 Priority 1 sites worth \$33.4 million of the \$55.2 million left to resolve.

## **STATE AUDITOR RECOMMENDATIONS**

Of the auditor's 11 recommendations, nine called for action by DTSC and two recommended action by the state legislature. DTSC has fully implemented seven of its nine recommendations.

The Department:

- Created a tracking system to ensure statutes of limitations are not missed.
- Established settlement-tracking procedures to ensure agreements and the resulting payments are recorded and the billing system is accurately adjusted.
- Standardized the way DTSC conducts responsible party searches to ensure all responsible parties are identified and invoiced.
- Developed procedures to ensure collection letters are sent when warranted.
- Issued a statutory lien policy to provide guidance on effectively utilizing statutory liens as a tool for cost recovery.



- Finalized written procedures for tracking payments associated with the Cleanup Loans and Environmental Assistance for Neighborhoods (CLEAN) loan program.
- Reconciled payments associated with federal grants that were showing up as unbilled receipts.

There are two recommendations DTSC has partially implemented:

- The State Auditor recommended DTSC investigate its authority to write off some backlog costs of \$5,000 or less. Because work necessary on these sites costs more than what is owed, the state legislature passed and the governor signed a bill allowing DTSC a one-time authorization to write off some costs of \$5,000 or less. That went into effect January 1, 2016 and DTSC is working on resolving these sites. They total about \$1 million but account for 418 of the remaining 713 unresolved sites. The Auditor indicated that once DTSC successfully writes these sites off, the Department will have fully implemented this recommendation. Our schedule is to have this done by the end of March 2016.
- The Auditor also recommended that DTSC review and ensure the accuracy of the data before putting the information into the new Statewide Financial System for California or Fi\$cal. Last December, Fi\$cal concluded it was unable to meet the Department's unique cost recovery billing system needs. This created a significant structural challenge and DTSC is now moving forward within the state's IT approval process. According to the recently revised state IT approval process, the project scope and contracting will be approved in 2018. Development and deployment of the new system will take an additional 3-4 years. Although DTSC does not currently have a new system to manage the data, all cost recovery backlog data will be reviewed and updated in the current system, consistent with the Auditor's recommendation, by June 30, 2016.

The auditor noted – and DTSC agreed – that DTSC has a good framework for a successful cost recovery system.

### **KEYS TO FUTURE SUCCESS**

The mechanisms and metrics DTSC creates will ensure an effective and efficient cost recovery effort going forward. DTSC looks forward to the Independent Review Panel's insights on how to optimize these elements to overcome the challenges discussed above and to maximize DTSC's cost recovery efforts.

Some of the keys to future success include:

- A dashboard tool that DTSC uses to instantly view a number of key progress points for the cost recovery program as a whole – for instance how much of the backlog has been resolved. With this tool, DTSC can set goals for numbers of documents that need to be processed and measure progress. That same tool allows DTSC to drill down at individual sites to see its cost recovery status. It helps detect bottlenecks and resource issues so DTSC can continue moving forward.



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- The new department procedures and the various flowcharts and desk manuals developed to address cost recovery processes are also keys to future success. DTSC's various tracking systems and its standardized procedures create an effective checks and balance system.
- Continuing and institutionalizing the prescribed interdepartmental meetings initiated to clear roadblocks and penetrate siloes.
- The new billing system that will replace DTSC's current archaic and unsupported system. The delay in acquiring this system represents a significant risk to the department.
- Ensuring adequate analytical, fiscal and legal staffing to sustain an effective and efficient cost recovery program is a significant key to success.