Negotiating Resolution of Environmental Enforcement Actions

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INTRODUCTION

The best defense against an environmental enforcement action is aggressive identification and correction of compliance problems before they come to the attention of government regulators or citizens’ groups. Periodic compliance audits and education of employees responsible for environmental compliance will help prevent many enforcement actions from ever being brought. Management’s commitment to maintaining environmental compliance is also an essential element in avoiding enforcement action.

Unfortunately, even the most conscientious company will occasionally be subject to enforcement action. A recent survey of corporate counsel who handle environmental compliance matters found that nearly seventy percent (70%) of those surveyed acknowledged that their businesses operated at least a portion of the previous year in violation of state or federal environmental laws.1 In addition, seventy percent (70%) of those corporate counsel surveyed believed that full and continuous compliance with all environmental requirements was not achievable2 “due to the complexity of the law, the varying interpretations of regulations, the ever-present role of human error and cost.”3

At the inception of a formal enforcement action, the target of the action must develop an effective strategy. Although development of an effective strategy is extremely dependent upon the facts and legal issues present in the case and typically changes as the enforcement action progresses, some basic steps must be taken. First, the target of the enforcement action should evaluate the strength of the government’s claims. At a minimum, this evaluation must include:

- Careful examination of factual allegations and statutory or regulatory authority cited in the complaint or administrative order.

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2. See id.
3. Id.
Comparison of the alleged violations with the company's recollection of the facts or events, with an analysis of the company’s version of the facts with the regulations allegedly violated.

Once the company has a basic understanding of the government’s claims, it should evaluate whether it has any effective defenses. Defenses available to the company typically fall within one of three categories: regulatory, legal and factual. Regulatory defenses are the most common in environmental enforcement actions and are identified by the following questions:

- Is the regulation allegedly violated applicable to the company’s operations?
- Does a different regulation or exemption apply?
- Does there exist a conflict between regulations?

Legal defenses, in general, will bar the enforcement of regulations, even though the regulations are valid and the facts alleged by the government are basically true. Legal defenses can include lack of jurisdiction, the doctrine of res judicata and expiration of the applicable statute of limitations, as well as defenses expressly available under the statute being enforced.

Factual defenses are the easiest to identify, but may not be the easiest to prove. Factual defenses include such arguments as:

- It did not happen the way the government alleged in its complaint or administrative order.
- We reported it to the government in the manner alleged, but we did not report additional facts which show no violation occurred.
- We reported the facts all wrong and the government’s allegations are based on a mistake.

The availability of viable defenses will weigh heavily in the decision to settle the case and in the ultimate outcome of the proceeding. Even where defenses are not particularly strong, they often affect the government's position on the appropriate amount of civil penalties and/or the extent of mitigation. Settlement discussions will always be affected by defenses which diminish the strength of the government’s case.

The final step in the strategic analysis is to evaluate the possibility for and potential benefits of reaching an early settlement of the enforcement action. Even if there are defenses available which make winning a distinct possibility, the question remains, “At what cost?”

As a practical matter, the company’s managers must consider the costs of disputing a penalty or other enforcement action. Legal fees can often be
substantial. In addition, a successful defense may require the use of environmental consultants or other expert witnesses. There are also related litigation expenses, such as the cost of deposition transcripts, copies, travel and other out-of-pocket costs that need to be considered. Finally, the company's managers should be aware that its employees may be devoting a substantial portion of their work day assisting with defense of the enforcement action.

The final step in developing a strategic resolution of an environmental enforcement action is to evaluate the potential civil penalties at stake. In many cases, the government agency pursuing the action will voluntarily share its penalty calculations with the company. The calculations should be analyzed to verify compliance with statutory criteria established for that purpose. Alternatively, the government may not have properly considered mitigating factors which serve to lower the amount of penalty considered "appropriate." Finally, there may be options available for the company to realize some true "value" for its penalty payment rather than as a contribution to the government's coffers, such as through Supplemental Environmental Projects.4

The purpose of this article is to provide an understanding of how civil penalties are calculated, how they can be reduced and ways to secure some "return of value" to the company. The concept of recouping the economic benefit of non-compliance is also addressed. Finally, there may be unanticipated consequences of settling an environmental enforcement action.

I. OVERVIEW OF ILLINOIS LAW APPLICABLE TO CIVIL PENALTY ASSESSMENTS

A. STATUTORY PROVISIONS APPLICABLE TO CIVIL PENALTY ASSESSMENTS

The Illinois Environmental Protection Act (the Act) sets forth statutory criteria that must be followed in establishing appropriate civil penalties for violations of the Act or implementing regulations.5 Section 33(b) of the Act authorizes the Pollution Control Board (the Board) to impose civil penalties for violations of "the Act or of the Board's rules and regulations or of any permit or term or condition thereof . . . in accord with Section 42 of this Act."6 Section 42(a) of the Act provides for a civil penalty not to exceed

$50,000 for each violation and an additional penalty not to exceed $10,000 for each day in which the violation continues.\(^7\)

1. **Section 33(c) "Reasonableness" Factors**

Section 33(c) sets forth five factors which the Board must consider in making its determinations, including determinations to impose civil penalties.

Section 33(c) states:

(c) In making its orders and determinations, the Board shall take into consideration all the facts and circumstances bearing upon the reasonableness of the emissions, discharge or deposits involved including, but not limited to:

(i) the character and degree of injury to, or interference with the protection of the health, general welfare and physical property of the people;

(ii) the social and economic value of the pollution source;

(iii) the suitability or unsuitability of the pollution source to the area in which it is located, including the question of priority of location in the area involved;

(iv) the technical practicability and economic reasonableness of reducing or eliminating the emissions, discharges or deposits resulting from such pollution source;\(^8\) and

(v) any subsequent compliance.\(^9\)

The Board is required to consider the factors outlined in section 33(c) of the Act in determining the "reasonableness" of the alleged pollution.\(^10\) This does not mean, however, that the Board must find against the company with respect to each of the five statutory criteria to support a lawful determination to impose civil penalties.\(^11\) Nor is the Board precluded by the section 33(c)

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10. See Mystik Tape, Div. of Borden, Inc. v. Pollution Control Bd., 328 N.E.2d 5, 8 (Ill. 1975).
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After noting that the section 33(c) criteria provide guidelines to govern the conduct of those affected by the Act, the Illinois Supreme Court in *Wells Manufacturing Co. v. The Pollution Control Board* affirmed the appellate court's reversal of a Board Order imposing $8,500 in civil penalties, a pollution abatement plan and performance bond. Essentially, the court found that the Board had not proven the "unreasonableness" of odorous emissions from a foundry operation through application of the section 33(c) criteria. In upholding reversal of the Board's Order and civil penalty, the court found it significant that the foundry was in operation at its existing location long before most of the neighboring residents who complained about the foundry's objectionable odorous emissions (the section 33(c)(iii) factor); and the absence of a proven technical solution to control the odorous emissions (the section 33(c)(iv) factor).

In more recent enforcement actions, the section 33(c) criteria have been considered together with the section 42(h) factors to determine whether the civil penalty is appropriate. Where four of the five section 33(c) criteria favored the alleged violator, the Board in a fairly recent case reduced the amount of the civil penalty from $254,100 proposed by the Illinois Environmental Protection Agency (IEPA) to $60,000 and refused to revoke the company's operating permits. The reviewing court upheld the Board's order despite evidence of subsequent noncompliance (the section 33(c)(v) factor), and proof of all of the aggravating factors specified in section 42(h) save a serious and harmful violation.

2. **Section 42(h) Factors to "Mitigate" and "Aggravate" the Civil Penalty**

In determining the appropriate civil penalty to be assessed for statutory or regulatory violations, the Board must consider any matters of record in mitigation or aggravation of a penalty, including but not limited to the factors

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15. *Id.* at 152-53; *see also* CPC Int'l, Inc. v. Pollution Control Bd., 336 N.E.2d 601, 605 (Ill. App. Ct. 1975) (stating that because the Board's Order did not specify whether the statutory standard of section 33(c) had been met, the court vacated the Board's Order imposing $10,000 in civil penalties).
18. *See* ESG Watts, 668 N.E.2d at 1021.
specified in section 42(h). Those factors are as follows:

(h) In determining the appropriate civil penalty to be imposed under subdivisions (a), (b)(1), (b)(2), (b)(3), or (b)(5) of this Section, the Board is authorized to consider any matters of record in mitigation or aggravation of penalty, including but not limited to the following factors:

1. the duration and gravity of the violation;
2. the presence or absence of due diligence on the part of the violator in attempting to comply with requirements of this Act and regulations thereunder or to secure relief therefrom as provided by this Act;
3. any economic benefits accrued by the violator because of delay in compliance with requirements;
4. the amount of monetary penalty which will serve to deter further violations by the violator and to otherwise aid in enhancing voluntary compliance with this Act by the violator and other persons similarly subject to the Act; and
5. the number, proximity in time, and gravity of previously adjudicated violations of this Act by the violator.

Historically, Illinois courts have held that the primary purpose of civil penalties is to aid in enforcement of the Act, and punitive considerations are secondary. The decisions in civil penalty cases, which predate the 1990 effective date of section 42(h), suggest that whenever compliance has been achieved, punishment through civil penalties is not necessary. With the incorporation of the section 42(h) factors into the Act it is now clear that the deterrent effect of civil penalties on the violator and on potential violators is a legitimate goal for the Board to consider when imposing penalties.

Although the section 42(h) factors are somewhat self-explanatory,

20. Id.
22. See ESG Watts, 668 N.E.2d at 1021.
23. Id.
decisions by the Board and the court in applying those factors to particular factual scenarios provide guidance to companies faced with an enforcement action. The court’s decision in Park Crematory, Inc. v. The Pollution Control Board, is a particularly good example of how the section 42(h) factors can work to the Company’s favor. In that case, the Board imposed a civil penalty of $9,000 for operating an incinerator for a period of nine years without a permit, and by failing to obtain a construction permit for a second incinerator. The court reversed the Board and held that no civil penalty was authorized by the Act because the company “realized almost no economic advantage from the noncompliance,” was “not beyond the regulatory awareness of the agency,” and acted in “good faith.”

II. GUIDANCE FROM FEDERAL STATUTORY PROVISIONS AND EPA POLICY DOCUMENTS

All of the major federal environmental statutes provide for the imposition of administrative violations of penalties, civil penalties and criminal penalties for violations of the law, implementing regulations, or for violations of an administrative order or permit issued pursuant to the law. Because environmental statutes are public welfare statutes, any of these potential penalties (including criminal penalties) may result from a violation, even though the offensive conduct was performed with a “good faith” belief that the conduct complied with relevant laws. In other words, these potential liabilities are based on what is essentially a standard of strict liability.

A. CLEAN AIR ACT STATUTORY PROVISIONS APPLICABLE TO CIVIL PENALTY ASSESSMENTS

Federal laws empower the United States Environmental Protection Agency (EPA) with a great deal of discretion in determining whether to pursue a violation and in determining which penalties are appropriate. That discretion is limited, however, by statutory constraints and enumerated factors

25. See id. at 521.
26. Id. at 525.
that must be considered when determining what level of civil penalty is "appropriate."

In addition, the EPA has developed extensive guidance materials which the EPA uses in calculating civil penalties and in evaluating settlement options. The EPA's penalty policies were developed to provide EPA enforcement staff with a logical calculation methodology for determining appropriate penalties. The policies allow the EPA to "apply the statutory penalty factors in a consistent and equitable manner so that members of the regulated community are treated similarly for similar violations across the country." Understanding the published EPA guidance documents will allow the company faced with an enforcement action to verify that the civil penalty proposed by the government was properly calculated and more importantly, to identify aggravating and mitigating factors that may not have been properly considered by the EPA. There are almost always facts that can be developed by the company to show that additional mitigation of the government's proposed civil penalty is warranted.

As one of the oldest and most comprehensive environmental statutes, the Clean Air Act (CAA) provides a good example of what factors are considered by the government in calculating a civil penalty and common statutory constraints imposed by the legislature. Under section 113 of the CAA, the administrator of the EPA may commence a civil judicial action or initiate administrative proceedings to recover civil penalties for violations of the law, implementing regulations, an agency order or permits issued pursuant to the CAA.

The 1990 CAA amendments added section 7413(e) to clarify the rules for penalty assessments by the administrator or the courts. Factors to be considered are, "the size of the business, the economic impact of the penalty on the business, the violator's full compliance history and good faith efforts..."

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30. See id. at *8.
to comply, the duration of the violation as established by any credible evidence (including evidence other than the applicable test method), payment by the violator of penalties previously assessed for the same violation, the economic benefit of noncompliance, and the seriousness of the violation.\textsuperscript{34}

The courts are also bound by the statutory criteria when determining the maximum applicable statutory fine. If the court decides to reduce the fine, it must be done in accordance with the statutory factors. The court must indicate the weight it gives to each factor and the findings that support its conclusion.\textsuperscript{35}

\textbf{B. U.S. ENVIRONMENTAL PROTECTION AGENCY’S CIVIL PENALTY POLICIES}

The EPA’s methodology for calculating a civil penalty for violations of the CAA are set out in a policy document that was last revised on October 25, 1991.\textsuperscript{36} The general policy applies to most CAA violations; however, ten appendices cover noncompliance with certain CAA program requirements that warrant more specific treatment than the general policy provides. Appendix I covers stationary source permit requirements.\textsuperscript{37} Appendix II covers vinyl chloride National Emissions Standards for Hazardous Air Pollutants (NESHAP) violations.\textsuperscript{38} Appendix III covers asbestos NESHAP demolition and renovation violations.\textsuperscript{39} Appendix IV covers Volatile Organic Compounds (VOCs) sources using reformulation to low solvent technology.\textsuperscript{40} Appendix V is a civil penalty work sheet.\textsuperscript{41} Appendix VI covers the volatile hazardous air pollutant civil penalty policy.\textsuperscript{42} Appendix VII covers residential wood heaters.\textsuperscript{43} Appendix VIII deals with substances that deplete stratospheric ozone.\textsuperscript{44} Appendix IX establishes civil penalty assessment criteria for individuals who service motor vehicle air conditioners and who sell small

\begin{thebibliography}{9}
\bibitem{34} 42 U.S.C.A. § 7413(e)(1) (West 1995).
\bibitem{35} \textit{See} Atlantic States Legal Found. v. Tyson Foods, 897 F.2d 1128, 1142 (11th Cir. 1990); \textit{see also} United States v. SCM Corp., 667 F. Supp. 1110, 1126 (D. Md. 1987).
\bibitem{38} \textit{Id.} at *72.
\bibitem{39} \textit{Id.} at *77-78.
\bibitem{40} \textit{Id.} at *104-05.
\bibitem{41} \textit{Id.} at *112.
\bibitem{42} EPA--CAA, \textit{supra} note 37, at *113.
\bibitem{43} \textit{Id.} at *119.
\bibitem{44} \textit{Id.} at *124.
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containers of refrigerant. Appendix X provides guidance for calculating civil penalties for violations involving the maintenance, service, repair and disposal of appliances containing refrigerant.

The general Civil Penalty Policy focuses on the two elements of a civil penalty — an amount to remove any significant "economic benefit" resulting from noncompliance and the "gravity" component to reflect the seriousness of the violation. One source of economic benefit that results from non-compliance is the savings from "deferred cost." This includes failure to install needed air pollution control equipment, failure to effect process changes to reduce pollution control equipment, failure to effect process changes to reduce pollution, failure to perform required tests, and failure to install required monitoring equipment. Economic benefits are to be computed using Technical Appendix A of the EPA's "BEN User's Manual."

The second source of receiving an economic benefit or advantage as a result of noncompliance with environmental requirements is by avoiding costs that the source otherwise would have been required to incur. The benefit from "avoided costs" must also be recouped through the civil penalty imposed on the alleged violator. Types of violations that enable a violator to permanently avoid certain costs associated with compliance include:

- Disconnecting or failing to properly operate and maintain existing pollution control equipment (or other equipment if it affects pollution control);
- Failure to employ a sufficient number of adequately trained staff;
- Failure to establish or follow precautionary methods required by regulations or permits;
- Removal of pollution equipment resulting in process, operational, or maintenance savings;
- Failure to conduct a test which is no longer required;
- Disconnecting or failing to properly operate and maintain required monitoring equipment; and
- Operation and maintenance of equipment that the violator failed to install.

45. Id. at *144.
46. Id. at *174.
47. EPA–CAA, supra note 37, at *161.
49. EPA, supra note 29, at *11-12.
The benefit from avoided cost also must be computed using Technical Appendix A of the BEN User’s Manual.50

It is the EPA’s general policy not to mitigate the economic benefit component of penalties, but there are at least two exceptions where the amount is insignificant or compelling public policy calls for mitigation. Under the CAA Civil Penalty Policy, the EPA may agree to accept a civil penalty that does not recoup the full economic benefit under the following three scenarios:

- If the economic benefit resulting from the noncompliance was calculated to be less than $5,000;51
- If there is a compelling public concern. For example, if it would result in a plant closing that would not occur otherwise or if the action is against non-profit public entities, such as municipalities and publicly-owned utilities, where an assessment would threaten to disrupt essential public services.52
- If EPA has already recovered the economic benefit of noncompliance in a previous administrative action under Section 120 of the Clean Air Act and would not seek a double recovery in a subsequent judicial enforcement action under Section 113 of the Act.53

The “gravity” component of the civil penalty requires the EPA to consider the elements set forth in CAA Section 113(e). The policy guideline further explains key terms such as the amount of the pollutant, the sensitivity of the environment to the toxicity of the pollutant, the length of time a violation continues, and the size of the violator.

Calculating the gravity component is a function of three determinations. First, the EPA assesses the actual or potential harm caused by the violation. A dollar figure is assigned based on the level of violation, toxicity of the pollutants, sensitivity of the environment, and the length of the violation.54 Second, the EPA assesses the importance of the offense to the regulatory scheme. The policy enumerates specific dollar penalties to be assessed in connection with reporting violations and operation and maintenance

51. EPA, supra note 29, at *14.
52. Id. at *15.
53. See id. at *17.
54. See id. at *19-23.
shortcomings. Finally, the EPA takes into account the size of the violator. The policy provides a sliding scale of penalties to be assessed based on the violator’s net current assets.

The civil penalty program is intended to be equitable and allow for a certain amount of administrative flexibility. The “gravity” component can be adjusted to reflect considerations such as the degree of willfulness and/or negligence, the extent of cooperation or lack thereof, the speed with which the violation was corrected, the history of noncompliance, and the environmental benefit of reaching a prompt solution. The Policy essentially applies the factors specified by the statute to reduce the “gravity” component of the civil penalty.

1. **Degree of Willfulness or Negligence** (aggravation). This factor only may be used to raise a penalty. In deciding whether a penalty should be raised, the EPA must consider the violator’s degree of control over and ability to foresee the events leading to the violation, the level of sophistication within the industry for dealing with compliance issues, and the extent to which the violator knew of the legal requirement that was violated.

2. **Degree of Cooperation** (mitigation). The EPA expects all sources in violation to comply expeditiously and to negotiate in good faith. The gravity factor may be lowered by thirty percent (30%) if the violator immediately reports the noncompliance, if violations are properly corrected, and if cooperation is shown during the investigation. The EPA considers the “prompt correction of environmental problems” to include such efforts as paying for extra work shifts, paying to have control equipment installed quickly, or the shutting down of a facility until compliance can be achieved.

3. **History of Noncompliance** (aggravation). This factor only may be used to raise a penalty. In determining this adjustment, the EPA must consider the similarity and the number of past violations and the time that has elapsed since the last such violation. “Similar” may mean a violation of the same permit, emissions standard, or statutory or regulatory provisions, a similar act or omission, or a violation at the same process points of a source.

4. **Environmental Damage** (aggravation). Although the gravity component takes into account damage to the environment, it may be further increased if the violation is so severe that the gravity component alone is not

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55. See id. at *23-27.
56. See id. at *27-28.
57. EPA, supra note 29, at *28-30.
58. See id. at *31-32.
59. See id. at *31-32.
60. Id. at *32.
61. See id. at *33-34.
a sufficient deterrent. An example would be a significant release of an air toxic in a populated area.

5. Ability to Pay (mitigation). The Company’s “ability to pay” is considered as another justification for mitigation of the civil penalty. The EPA will generally not require penalties beyond the violator’s ability to pay. Ability to pay is considered in adjusting the preliminary deterrence amount and the gravity as well as the economic benefit component. The EPA reserves the right to seek a penalty that may contribute to a company going out of business but the Courts have generally refused to impose a penalty that would cause economic bankruptcy. It is unlikely that the EPA would reduce a penalty if a facility refuses to correct a serious violation or if a source has a long history of previous violations.

The EPA only may consider the financial well-being of a company if the source raises it as an issue and if it provides the necessary financial information relating to its claim. If a violator proves that it is unable to pay a penalty and EPA is unwilling to reduce the amount of the penalty, EPA may consider delaying the payment schedule with interest. In court, the violator must sustain its burden of proof showing that a penalty would have a “serious” impact on their business, before the court will reduce an otherwise appropriate penalty amount.

In addition, both the economic benefit and the gravity components may be mitigated based on litigation risk. Litigation risks may involve evidentiary problems, caps on the amounts that are imposed by the statute, and adverse legal precedent. There may also be offsets allowed for penalties paid to state and local governments or citizen groups for the same violations. If supplemental environmental projects are to be used in lieu of a penalty, such projects are subject to the May 1, 1998, Final EPA Supplemental Environment-

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62. See id. at *36.
65. EPA supra note 29, at *39-41.
67. See EPA supra note 29, at *36.
68. See id. at *37-38.
69. See id. at *41-43.
The use of Supplemental Environmental Projects is discussed in more detail in the following sections.

Note that where the EPA relies on one of its Civil Penalty Policies during the course of a hearing to justify its assessed civil penalty, it must through evidence, support the assumptions, findings, and conclusions on which that policy rests. From an evidentiary standpoint, no presumption of validity attaches to an Agency policy statement. At least one EPA Administrative Law Judge has reduced the civil penalty because the EPA did not proffer evidence to support the findings, conclusions and estimate of a Civil Penalty Policy.

C. CASE HISTORY—APPLICATION OF EPA'S CIVIL PENALTY POLICY IN AN ENFORCEMENT ACTION BROUGHT UNDER THE EMERGENCY PLANNING AND COMMUNITY RIGHT-TO-KNOW ACT (EPCRA)

The following discussion summarizes resolution of an actual administrative enforcement action brought by the EPA under the EPCRA program against "the Company," for alleged violations of the EPCRA implementing regulations.

The statutory factors under section 325 of EPCRA that must be considered by the EPA and the courts when determining the amount of civil penalty to be imposed are almost identical to the CAA factors noted in the preceding discussion. Similar to the EPA's Civil Penalty Policy for CAA violations, the EPA's Civil Penalty Policy applicable to EPCRA cases uses mathematical formulas to first calculate the "overall seriousness" of the noncompliance and the economic benefit gained by the alleged violator. Once the base penalty is calculated, the agency applies the statutory factors to aggravate (increase) or mitigate (reduce) the base penalty amount. The

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74. EPA, Final Penalty Policy for Sections 302, 303, 304, 311 and 312 of the Emergency Planning and Community Right-to-Know Act and Section 103 of the Comprehensive Environmental Response Compensation and Liability Act, 1990 CPP LEXIS 19 (June 13, 1990) [hereinafter EPCRA].

75. See id at *39-53.
EPA’s EPCRA Civil Penalty Policy lists the following factors to be used in the “adjustment” process: ability to pay/continue in business (downward adjustment only); prior history of violations (upward adjustment only); and the degree of culpability, i.e., knowledge, control and good faith (upward or downward adjustment).76

The civil penalty reductions realized in the case described below were directly related to the EPA’s Civil Penalty Policy for EPCRA cases. It provides a good example of how the EPA applied its Policy to calculate a penalty and how the penalty can be reduced by establishing the presence of the mitigating factors. Identities have been changed or omitted to preserve confidentiality and to protect individual privacy rights, even though this proceeding is a matter of public record.

1. Background and Initiation of EPA Enforcement Action

Based on discussions with EPA personnel, primarily the Assistant Regional Counsel and the Staff Engineer, this enforcement action was initiated as a result of an employee accident.77 This accident resulted in the injury of one employee and the death of another, after being overcome by fumes while cleaning a trichloroethylene ("TCE") solvent storage tank.

Following the accident, the EPA began investigating the Company’s compliance with the EPCRA program and implementing regulations. Letters were sent to the local fire department, the County health department, and the State Department of Natural Resources (“DNR”), requesting information on the Company’s compliance with the EPCRA program. The appropriate official at each agency was asked to prepare an affidavit attesting to the Company’s noncompliance with various provisions of the EPCRA program.

As a result of its investigations, the EPA determined that the Company had violated Section 311 of EPCRA, which requires submittal of Material Safety Data Sheets (“MSDS”) to the local fire department, the local emergency planning committee (“LEPC”) (which was the County Health Department), and the State Emergency Response Commission (“SERC”). Because the Company had filed its comprehensive emergency response plan with the local fire department, and the plan contained the MSDS sheets, the Company was cited for failing to submit MSDS sheets to the LEPC and SERC, but not the local fire department. Two violations were alleged for failing to submit the appropriate MSDS sheets to the County and the MDNR.

76. Id. at *40-41.
77. This information comes from an actual case in which the author was involved.
In addition to the EPCRA section 311 violations, the EPA cited the Company for violating section 312 of EPCRA, which requires preparation and submittal of a Tier I or Tier II emergency and hazardous chemical inventory form (inventory forms) to the local fire department, LEPC, and SERC. Based on the investigations conducted by the EPA, which consisted primarily of requests to the appropriate agencies, the EPA alleged violations of EPCRA section 312 for the years 1987 through 1991.

In summary, the EPA was alerted to a situation of potential noncompliance through the July 1992 employee accident, either through media reports or possibly citizens' complaints. The EPA then contacted the local fire department, the County health department, and the State to determine whether the Company had submitted the required EPCRA paperwork.

2. Calculation of the Proposed Civil Penalty Under EPA's EPCRA Civil Penalty Policy

Enforcement actions brought under the EPCRA program are subject to a published Civil Penalty Policy, which is a document issued by EPA as guidance to EPA enforcement personnel. The EPCRA Civil Penalty Policy is similar to the CAA Civil Penalty Policy discussed in the preceding section, particularly in the evaluation and application of the various mitigating and aggravating factors. The EPCRA Civil Penalty Policy establishes a three-step procedure for determining the appropriate civil penalty for a violation of the EPCRA requirements. First, the "extent of deviation" from the regulatory requirement is assessed. A failure to submit the necessary EPCRA paperwork is considered the maximum extent of deviation under the Policy. Second, the "gravity of violation" is assessed. In considering this second component, the EPA is directed to determine the maximum amount of a specific chemical present during the previous calendar year. If the amount of any hazardous chemical not reported in the EPCRA inventory form was greater than the reporting threshold (e.g. 10,000 pounds for TCE), then the "gravity of violation" is considered. If the amount of chemical present at the facility was 5 times the threshold (i.e., 50,000 pounds for TCE), the "gravity" component is a Level B moderate violation.

Third, the EPA is required to consider the circumstances of the alleged violations to arrive at a specific penalty figure within a specified range. It

78. EPCRA, supra note 74, at *1-5.
79. See id. at *20-29.
80. See id. at *29-33.
81. See id at *33-37.
is this component of the penalty calculation where the EPA is given wide discretion. In this case, most of the company’s arguments for reducing the civil penalty related to the “circumstances” of the alleged violations.

In calculating the appropriate civil penalty for the alleged EPCRA violations, the EPA relied on supplemental information obtained from Company personnel. The EPA sent two separate Information Requests to obtain this additional information. One critical item of information the EPA requested was the amount of TCE solvent present at the Company’s facility during each year. Based on the responses provided by the Company, the EPA determined that the amount of TCE present during the 1987 through 1991 reporting periods was greater than five times the reporting threshold. This translated into a Level B category for the “gravity of violation” component of the penalty. The Penalty Policy directs that the penalty range for a Level 1 “extent of deviation” (failure to submit forms) and a Level B “gravity of violation” is $13,200-$16,500 per violation. [Note: If less than 50,000 pounds of TCE was present at the facility during any one of the reporting periods (1987 through 1991), the penalty range would have been reduced by half to $6,600-$8,250 per violation (designated a Level C “gravity of violation”)].

3. Mitigation of the Proposed Civil Penalty

The EPCRA Penalty Policy states that the EPA may consider as an aggravating factor “any actual problems that first responders and emergency managers encountered because of the failure to . . . submit reports . . . in a timely manner,” as circumstances to be considered in assessing the appropriate penalty within the applicable range.82 In addition, the Policy allows consideration of the “potential for harm” resulting from the nonreporting, and the public policy against undermining the statutory or regulatory purposes of the EPCRA program.83

The EPA personnel substantially increased the proposed penalty because local fire department and police department personnel encountered substantial problems on the date of the employee accident. For example, fire and police personnel were not aware that the injured workers were being overcome by TCE vapors, and were unsure of the level of protection needed to safely enter the tank to rescue the unconscious workers. Although we successfully argued that the workers’ injuries were solely workplace safety and OSHA issues, EPA personnel maintained that the alleged injuries to the fire and police

82. *Id.* at *36.
83. *Id.* at *34.
personnel demonstrated that the EPCRA noncompliance created a dangerous situation. In a September 1993 newspaper article about the accident, the EPA Attorney was quoted as stating, "Fifteen people who tried to rescue [the employee,] including eight firefighters and four police officers, were treated for varying chemical burns. The missing Tier I Inventory Forms were intended to prevent just that sort of danger."84

Based on subsequent investigations, the EPA's statements that 15 rescuers were injured at the time of the accident were inaccurate and misleading. A number of rescue personnel were sent to the local hospital, with one firefighter kept for observation for approximately 8 hours. Although the alleged "injuries" were suspect, there was some documentation to support the EPA's argument that the first responders were physically affected by the TCE vapors and encountered problems caused by lack of information. As explained in the Penalty Policy, actual harm and problems encountered by emergency and rescue personnel are consequences that relate to the core of the EPCRA regulatory program.85

The original administrative complaint issued by the EPA requested a civil penalty of $219,450 to be paid within 30 days. In our discussions with the EPA, we argued for reductions in the assessed civil penalty on the grounds that the company had "substantially complied" with the program; that the "circumstances" of the alleged violations did not warrant the maximum penalty within the range; that the amounts of TCE present at the facility was actually lower than the 50,000 pound threshold; and that the civil penalty was generally excessive. We also argued that the EPA should select the lower bounds of the penalty range, due to the company's "good faith" in resolving the noncompliance and agreement not to proceed to hearing.

The EPA responded that medical records and related documentation established at least minor "injuries" to emergency response personnel. The EPA also believed that "substantial compliance" through local fire department inspections addressed only one of the three points of compliance (i.e., local fire department, LEPC, and SERC), the amounts of TCE at the facility exceeded 50,000 pounds as documented in the company's responses to official EPA Information Requests, and that the EPA considered the July 1992 incident a potential undermining of EPCRA program goals.

Initially, the EPA agreed to reduce the civil penalty from $219,450 to $186,531 plus interest based on the company's "good faith" in responding to the complaint. After submittal of additional information regarding "ability to

85. ECPRA, supra note 74, at *4-12.
pay/continue in business” and the “degree of culpability,” the EPA agreed to further reductions in the civil penalty to $175,500 to be paid in quarterly installments.

An administrative consent agreement and final order was executed to formalize the settlement agreement. Pursuant to the settlement, the company was allowed to pay the penalty in four quarterly installments over a one-year period.

III. ECONOMIC BENEFIT OF NONCOMPLIANCE

The government’s goal in every enforcement action is to recover any economic benefit that may accrue as a result of delayed pollution control investment, thus removing the economic advantage a violator gained over competitors that complied on time. The concept of economic benefits through noncompliance, often referred to as “BEN,” is relatively easy to understand. A company that delays installation of pollution control equipment saves money by delaying the purchase of equipment thereby earning interest on the money it has not spent and by not paying the annual costs of operating and maintaining the equipment needed for compliance. Delays in spending money on pollution control allows the company to use the money it saves for other, revenue-producing activities and therefore gain an economic advantage over its competitors that have complied on time. Alternatively, the company may realize an economic benefit by completely avoiding expenses that it otherwise would have incurred had it timely complied. For example, the company completely avoids the expenses associated with operating and maintaining pollution control equipment that it failed to install or installed late.

A. METHODOLOGY OF CALCULATING “BEN”

The EPA uses the “BEN” computer model to calculate the economic gain from noncompliance. The computer program compares the present value of the cost of compliance with the present value of noncompliance and the difference equals the net gain from noncompliance. The model uses default values when the EPA believes that data supplied by a polluter is inaccurate.

B. PROBLEMS WITH EPA'S "BEN" METHODOLOGY AND RECENT CASE LAW

Since BEN was adopted, its use has been controversial.88 A public interest group sued the EPA in 1993, alleging that the EPA deceived alleged violators during penalty negotiations "by using a discredited [BEN] Model . . . ."89 The Washington Legal Foundation successfully moved for release of the EPA internal documents pertaining to the BEN model and changes made to it which lowered penalty amounts. The documents included the User's Guide and an "internal" memorandum stating that the EPA was under no obligation to inform alleged violators of changes made to the BEN model.90

In what has become known as the Dean Dairy case,91 the U. S. District Court for the Eastern District of Pennsylvania, lacking guidance from economic experts, accepted a novel theory of economic benefit advanced by the government. The court accepted the government's claim that the proper measure of economic benefit gained by the company as a result of the alleged environmental violations included the net revenues obtained during the period of noncompliance by not reducing plant production sufficiently to achieve compliance.92 The court reasoned that by producing less product, the facility would have generated a lower volume of the wastewater which caused violation of applicable effluent limitations.93

The district court's decision was disturbing because it followed the parties' stipulation that the company enjoyed no "economic benefit" as defined under existing EPA guidance and legal precedent, by delaying the costs associated with the wastewater pretreatment systems that ultimately achieved compliance. Without expert testimony at trial to provide a proper framework for its analysis of economic benefit, the Dean Dairy court accepted a theory of economic benefit that was in direct conflict with previous decisions, EPA guidance, and fundamental economic principles. The decision accepts a novel theory that economic benefit includes not only the traditional concept of the benefit from delayed and avoided compliance costs, but also "wrongful profits" earned during the period of noncompliance.

88. See generally Robert H. Fuhrman, A Discussion of Technical Problems with EPA's BEN Model, 1 ENVTL. LAWYER 561 (Feb. 1995) (evaluating the application of EPA's BEN Model and its attempts to assess civil penalties).
92. Id. at 806.
93. Id. at 807.
RESOLVING ENVIRONMENTAL ENFORCEMENT ACTIONS

The district court judgment imposing a civil penalty in excess of four million dollars in the Dean Dairy case was recently affirmed on appeal to the Third Circuit Court of Appeals.94

IV. SUPPLEMENTAL ENVIRONMENTAL PROJECTS

Supplemental Environmental Projects (SEPs) have been used in settling enforcement actions since the early 1980s. A SEP is a settlement between the EPA and a violator that reduces a proposed penalty in return for the violator performing an environmentally beneficial project.95 The EPA defines SEPs as "environmentally beneficial projects which a defendant or respondent agrees to undertake in settlement of an enforcement action, but which the defendant or respondent is not legally required to perform."96

A. EPA’s SEP GUIDANCE DOCUMENTS

SEPs can be used to settle judicial or administrative enforcement actions and citizen suits. The EPA expects a SEP to cost a company more than the amount of reduction of a fine. At a minimum, the reduction in a fine cannot exceed the benefits gained from the violation. A SEP may be a depreciable asset whereas the fine which it offsets is not tax deductible. Environmentalists frequently support the use of SEPs because they result in environmental improvement rather than in money going to the U.S. Treasury.

The EPA’s original SEP policy was published February 12, 1991, as "Policy on the Use of Supplemental Environmental Projects in Enforcement Settlements."97 On May 10, 1995, EPA published the interim version of its revised policy on the use of SEPs.98 On May 5, 1998, the EPA issued final policy guidance to refine and clarify the appropriate use of SEPs in settlements of environmental enforcement cases.99

94. U.S. v. Municipal Auth. of Union Township and Dean Dairy Prod., Inc., 150 F.3d 259, 267 (3rd Cir. 1998) (noting that no other Clear Water Act penalty case had ever adopted the concept of "wrongful profits," the court of appeals nevertheless affirmed the lower court’s "approximation" of the economic benefit that resulted from the admitted noncompliance as a decision falling squarely within the district court’s discretion).


96. Id. at 24,798.


In general, the new 1998 guidance document is consistent with the EPA's 1991 SEP Policy, but it has some important clarifications and enhancements of the EPA's previous position on the use of SEPs in settlements and should promote the use of SEPs. Those distinctions are summarized below:

- The new SEP policy establishes a specific five-step process which should be followed by agency personnel in reviewing and approving SEPs in the context of a proposed settlement.

- The 1998 guidance specifies "legal guidelines" which the EPA and states will use to determine whether or not the proposed SEPs can be approved. Of significance is the requirement that all SEPs must be identified within the context of the settlement agreement; the EPA will not allow the settlement agreement to specify a dollar amount to be spent on a SEP, the details of which are to be determined at some later date.

- The new SEP policy identifies two additional categories of SEPs which were not included in the 1991 guidance. For example, the EPA now allows a project focused on "public health" related to the actual or potential damage that may have been caused by the alleged violation. In addition, the EPA now recognizes a SEP for "emergency planning and preparedness" which includes such activities as providing computers and software, communication systems, HAZMAT equipment, etc. to assist local organizations with their EPCRA programs.

- The 1991 guidance allowed the use of environmental assessments and audits as SEPs, but the new SEP policy expands and enhances the types of assessments and audits that are authorized as SEPs. For example, the new guidance clearly allows as approvable SEPs, pollution prevention assessments, as well as site assessments on the environmental conditions of the site or facility.

100. See Steven A. Herman, EPA's Revised Supplemental Environmental Projects Policy Will Produce More Environmentally Beneficial Enforcement Settlements, NAT'L ENVTL. ENFORCEMENT J. 9 (July 1995).

101. Id. at 10.
The most significant change in the new SEP guidance is the adoption of fairly rigid procedures for calculation of the "net-present after-tax costs of the SEP" which will be used to offset civil penalties for the alleged violations. This new guidance establishes a bright line test which requires the overall settlement (which includes a SEP) to recover at a minimum, "the economic benefit of noncompliance plus 10% of the gravity component" of the assessed civil penalty, or in the alternative, "25% of the gravity component only" whichever dollar amount is greater.\textsuperscript{102} In addition, the new guidance specifies the procedures to be used to calculate the value of the SEP and recommends use of an EPA computer model called "PROJECT."

The EPA has acknowledged that all federal administrative settlements are using the new 1998 Policy on the use of SEPs.\textsuperscript{103} In addition, the EPA and the U.S. Department of Justice are now utilizing SEPs more frequently in the context of federal judicial settlements embodied in court-approved Consent Decrees. To a much lesser extent, the Illinois Environmental Protection Agency ("IEPA") and Attorney General's Office are following the EPA's SEP Policy and incorporating SEPs more often in settling enforcement actions.\textsuperscript{104} The IEPA recently entered into an August 1996 agreement where SEPs were used to offset civil penalties in a Saline County enforcement action.

B. APPLICATION OF THE SEP POLICY TO ACTUAL ENFORCEMENT CASES

Following are two examples of the application of the SEP Policy in the settlement of actual environmental enforcement actions. Although both proceedings are a matter of public record, identities have been omitted or altered to preserve confidentiality and to protect the privacy rights of the individuals involved.\textsuperscript{105}

Case History No. 1. This first example of a settlement incorporating SEPs illustrates an unusually liberal scope of the types of projects approved by the government. It also serves as an example of a principal benefit of incorporating SEPs in a settlement, which is to create or increase "good will" in the community most impacted by the environmental harm caused by the noncompliance.

\textsuperscript{102} Id. at 11.
\textsuperscript{103} Interview with Ann Klein, Esq., EPA Office of Enforcement and Compliance Assurance (June 15, 1998).
\textsuperscript{104} Interview with Matthew J. Dunn, Office of the Attorney General, State of Illinois (Jan. 1998).
\textsuperscript{105} Identification of the entities and individuals involved as well as copies of non-privileged public documents generated in these proceedings can be obtained by contacting the author.
Company A acquired a pulp and hardboard mill that had been in existence since the 1940s. Similar to many other industrial operations sited fifty years ago, the mill was located within the limits of a small municipality, surrounded by a lower-income residential area.

Operations at the mill generated a variety of odorous emissions, which at times, caused a significant impact on the neighboring residents. Previous owners of the mill had ignored residents' complaints and managed to avoid any significant enforcement action through threats of closing the facility. The prospect of losing several hundred jobs in a community whose economy depended on the mill was an effective deterrent.

Soon after acquiring the mill, Company A encountered labor disputes which resulted in breaking the union and downsizing of the work force. At the same time, the nuisance odors continued and the state agency became less responsive to threats of economic blackmail.

After more than five years of operation by Company A, the state environmental agency brought an administrative enforcement action for a variety of air pollution violations and for maintaining a public odor nuisance. The Agency's initial demand requested over $350,000 in civil penalties. Through the course of defending the action, the Agency was persuaded to reduce its proposed civil penalty to $99,000. Those reductions were based in large part on the Company's commitment to install new pollution control equipment to reduce odorous emissions from specific process lines.

During our discussions with Company A's management, it was acknowledged that the civil penalty should be applied toward SEPs that would create "good will" in the community. It was thought that increasing "good will" would neutralize the effect of certain individuals with strong feelings against Company A and would reduce the number of individuals who were willing to call-in complaints to the Agency about any odors from the mill, even tolerable odors.

The ultimate resolution of the enforcement action resulted in the following breakdown in the total $99,000 paid in "penalties" for the air quality violations and public nuisance:

- $35,000 to reimburse the State for its costs of investigation and enforcement (non-negotiable)
- $20,000 in true civil penalties
- $20,000 in SEP “donations” to two elementary schools “for the purchase of multimedia computer hardware and software for environmental training of school students”
- $8,000 SEP donation to a non-profit local conservation
group to “provide environmental education training to school children”

- $8,000 SEP donation to a local fishing club “toward the costs of installing small boat ramps”
- $8,000 SEP donation to the municipality for equipment to outfit the local Emergency Response Team

Since the settlement was finalized, Company A has noticed more favorable treatment by the local media and a substantial reduction in the number of complaints made to the state Agency. In addition, residents who notice objectionable odors will call the mill with complaints rather than the Agency and are more willing to forgive short-term nuisance odors caused by malfunctions or process upsets. As Company A completed its agreed-upon compliance program and reduced the level of nuisance odors, its “good will” in the community has further improved.

Case History No. 2. The second case example of the application of the SEP policy illustrates how the company received a return of some of the value of its civil penalty. This occurred through physical improvements to a manufacturing plant that were paid for, in large part, by the SEP component of the civil penalty.

Company B operated a gray iron foundry located in an industrial section of a large metropolitan area. The foundry had been constructed in the early 1950’s and certain “scrubbing” equipment used to control particulate emissions from one of its molding lines was old technology. The existing control equipment could achieve compliance with the applicable emission limits, provided it was operated correctly and maintained frequently.

Due to general economic upturn in its business, Company B had initiated a program to improve and replace manufacturing equipment and pollution control equipment at the foundry. Equipment and process lines were scheduled for improvements as budgeting allowed, but all plans were subject to management approval.

Based on opacity observations and resident complaints, the government agency initiated an administrative enforcement action against Company B for violating applicable particulate emission and opacity limits. The initial civil penalty proposed by the Agency was in excess of $50,000. The case was ultimately settled for the payment of a $3,000 fine and for a SEP which required replacement of the aging “scrubbing” controls on the molding lines with an advanced, state-of-the-art baghouse system. Because the new controls reduced particulate emissions more than was required to meet the applicable emission limits, the equipment qualified as a SEP despite the fact that it would directly benefit the company.
Use of the SEP Policy in this case allowed the company to purchase new, modern control equipment for its own foundry, with penalty money that otherwise would have gone to the State. Although the expenditure was substantial, it was already planned and budgeted for. Finally, the improved pollution controls provided insurance against future violations of the applicable regulations and government prosecutions.

CONCLUSION

Environmental protection laws and regulations continue to increase in number and stringency. With this reality facing the regulated community and in particular heavy industry, enforcement actions become a distinct possibility for many companies.

If faced with an environmental enforcement action, there are strategies that can be implemented to minimize the economic impacts of substantial monetary penalties. Crucial to a successful strategy is recognizing the statutory limits placed on the governments' discretion in calculating and assessing proposed penalty amounts. Of equal import are the specific statutory criteria that must be considered to mitigate and aggravate the dollar amount of civil penalties deemed "appropriate." The EPA-developed guidance on how to calculate penalties and how to apply the statutory factors in mitigation and aggravation provide valuable insight and justification for penalty reductions, particularly with respect to the "seriousness" of the alleged noncompliance. Finally, the use of Supplemental Environmental Projects can allow the return of a portion of the economic value of a civil penalty through improving facility processes and creating good will in the community most likely to have been affected by the noncompliance.