

EPA's Self- Audit Policy for New Owners

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The Environmental Protection Agency (EPA) has a long standing Self-Audit Policy – launched in 1995 and updated on April 11, 2000 – that if a company discovers environmental violations through its own voluntary audit, it has the option of reporting the violations to EPA within 21 days of discovery in exchange for significant reductions in civil penalties.



EPA's civil penalty policy has two components: The gravity portion and the economic benefits portion. The gravity portion of the civil penalty refers to the part of penalty that pertains to how much damage is done to the environment. In other words, it is based on the severity (or gravity) of the violation. A violation that causes more severe environmental damage will result in a larger cash penalty. The economic benefits portion of the penalty is the amount of money the violator has saved by not being in compliance. For example, if you have been dumping your toxic wastes into the river for a year, you have saved a certain amount of money by not having to pay for the proper disposal of those wastes. The economic benefits portion of the civil penalty would be the amount of money you have saved that the agency wants from you. In this example, your gravity portion of the penalty will be very large.

There are nine conditions to the audit policy. A company must meet all nine conditions to be eligible for a 100% reduction of the gravity portion of the civil penalty. The 9 conditions are:

1. The audit must be systematic in nature. You must have an audit program in place that looks at your operation on a systematic schedule.
2. It must be a voluntary act on your part.
3. You must disclose your violations to EPA within 21 days.
4. The audits must be independent of permit or settlement conditions. In other words, an audit that is required under a permit will not qualify.
5. You must correct your violations within 60 days.
6. You must prevent recurrence of the violations.
7. No repeat violations. The same or closely-related violation must not have occurred within the past three years. (Note: This 3-year limit would not apply to new owners).
8. There must not be any serious harm to human health or the environment.
9. You must cooperate with EPA to determine your eligibility to the program.

Here is a recent case study of the self-audit policy at work. On April 30, 2004, subsidiaries of Koch Industries purchased 40 manufacturing plants from DuPont. Twelve of these facilities are located in the United States. The company entered into a corporate-wide auditing agreement with EPA under EPA's self-audit policy and uncovered over 680 violations of water, air, hazardous waste, emergency planning and preparedness and pesticide regulations. The company disclosed these violations in accordance with its agreement with EPA.

On April 13, 2009, the company reached a settlement with EPA to resolve the violations. According to EPA's press release, the company conducted 45 separate audits of environmental practices and compliance at facilities located in Seaford, Del.; Athens, Calhoun, and Dalton, Ga.; Kinston, N.C.; Camden, S.C.; Chattanooga, Tenn.; LaPorte, Orange, and Victoria, Texas; and Martinsville and Waynesboro, Va.

As part of a Consent Agreement, EPA waived the gravity portion of the civil penalty but fined the company \$1.7 million as the economic benefits portion of the civil penalty. This would be the amount of money EPA estimated the company would have saved by not being in compliance from the time it acquired those 12 facilities to the time when all the violations are corrected. The company also agreed to spend between \$240 million and \$500 million to correct all the environmental violations at those facilities.

According to EPA, this was the largest settlement under EPA's audit policy since its inception in 1995. The policy provides incentives to companies that voluntarily discover, promptly disclose, and expeditiously correct environmental violations. The companies must also take steps to prevent future violations. EPA may reduce or waive penalties for certain violations if the facility meets the conditions of the policy. Consistent with the audit policy, EPA waived a large portion of the penalty in this case.

EPA's experience in this settlement guided the development of a national interim audit policy for new owners—announced in August 2008—designed to encourage other new owners to make a “clean start” at their recently acquired facilities.

This is a classic case of how a large company and a new owner can take advantage of EPA's self-auditing policy to “start over” with a clean slate. By agreeing with EPA to conduct a self-audit, the company appeared to have averted most if not all of the gravity portion of the penalty for over 680 violations. Without the self-audit agreement with EPA, the company would have to pay a substantial gravity portion of the civil penalty in addition to the \$1.7 million for economic benefits recovery.

The national interim audit policy for new owners states that if you purchase a facility and conduct a voluntary self-audit of that facility within 9 months from the

date of acquisition, you may be eligible for waiver of the gravity portion of the civil penalty as long as you meet the nine conditions cited above.

There are several conditions that define the term “new owner”. A “new owner” must not have been responsible for environmental compliance at the facility prior to acquisition. The violations being disclosed must have originated with the prior owner. Neither the seller nor the buyer had the largest ownership of the facility and they did not have a common corporate parent.

Keep in mind that you may still be liable for the economic portion of the civil penalty if as a new owner you are substantially benefiting from the non-compliance status during the period between disclosure and final compliance. For example, if you discover in your self audit that the prior owner should have been treating a wastewater stream and you disclose that fact to EPA. The agency may calculate how much money you are saving by not having to treat that waste stream while you are installing the treatment process. That money would be your economic benefits and would likely be assessed by EPA against you as a civil penalty.

The decision to enter into a self-auditing arrangement with EPA is a management and legal decision that should not be taken lightly. As with most remedies, it is not a one size fits all solution. What works for one company may not work for others.

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