UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

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OFFICE OF
ENFORCEMENT AND
COMPLIANCE ASSURANCE

MEMORANDUM

FROM: Walker B. Smith, Director WBS
Office of Regulatory Enforcement

TO: Regional Counsel
Regional Enforcement Coordinators
Regional Media Division Directors

SUBJECT: Environmental Compliance Audits as a Component of Injunctive Relief in Enforcement Settlements

Purpose:
The purpose of the memorandum is to share Regional and Headquarters experiences and recommendations in managing audits in settlements. On March 20, 2001, Regions and Headquarters met to discuss experiences with requiring audits in settlements[1] and the issues related to crafting such settlements. This memorandum relays some of the agency's collective lessons learned with such experiences and, in light of those lessons, factors to consider when dealing with audits in settlements.

Background:
In the past few years, EPA has included environmental compliance audits as a component of injunctive relief in an increasing number of enforcement settlements. EPA has often required such audits at facilities not the direct subject of the enforcement action. Most frequently, this scenario arises where an investigation at some, but not all, of the defendant's facilities yields

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[1] This document refers to "audits" for simplicity sake; often the type of settlement referred to here requires the defendant to implement a compliance management system (CMS), and the audit may be one component of the CMS or of the settlement in general.

significant violations and the extent of violations at the defendant's remaining facilities is largely or wholly unknown. In light of constraints on agency resources, in appropriate cases, EPA may determine that an audit performed by the defendant under the terms of a consent decree is an efficient mechanism to obtain facility information and assist in achieving compliance.[2] In a number of settlements, defendants have agreed to single-media or multi-media audits. These audits may track the basis of the complaint (e.g., stormwater auditing of other facilities in a stormwater case) or may require auditing of another program/media.

In the context of an enforcement settlement, and with the right defendant, auditing can provide an opportunity for the company to identify the root causes of noncompliance on a comprehensive and system-wide basis and design a modern compliance management system while correcting the specific violations at issue in the case.

Lessons Learned:
Three basic questions should be considered when deciding whether to require a compliance audit as part of a national settlement:

(1) Does the defendant possess characteristics that are optimal for this type of undertaking?
(2) Should the defendant be required to disclose violations discovered during the audits?
(3) If disclosure is required, how should penalties associated with the disclosed violations be addressed?

These questions provide some structure for designing settlements with auditing components, while recognizing that case-specific facts are the single-most important consideration in any settlement. The Agency's experience with these settlements indicates that thorough consideration of the questions and factors posed in this document will likely yield greater environmental benefit and a more productive experience for the Agency and company.

1. Does the defendant possess the characteristics optimal for this type of undertaking?
To ensure that an audit is performed competently and on schedule, a defendant should be interested and cooperative, and should have or have access to sufficient financial and technical resources. Audits may be especially appropriate for a company that has been chronically noncompliant and/or suffers from infrastructure problems that have complicated compliance and compliance assessment. In addition, audits may be particularly beneficial for those companies that have been involved in a recent merger or acquisition, and those that engage in a significant amount of regulated activity (either broad in scope or frequent in application).

2. Should the defendant be required to disclose violations discovered during the audits?

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[2] Such audits are not performed in lieu of penalties and, therefore, do not trigger an examination of the conditions of EPA's Supplemental Environmental Projects (SEPs) Policy (May 1998) — most notably, the general prohibition against environmental compliance audits conducted by entities other than small businesses or small communities.

2. Should the defendant be required to disclose violations discovered during the audits? Once the case team has decided that requiring an audit would be appropriate and would likely yield environmental benefits through compliance, it is helpful to consider what will become of the information that is discovered during the audit. This issue is very case-specific and requires taking a comprehensive look at what is known about the facility(ies) that is the subject of the enforcement case, the nature of the violations to be discovered, the number of facilities being audited, and the historical interactions with the defendant.

One of the most fundamental considerations is whether the agency wishes to receive the volume of information related to the violations discovered. That may depend largely upon whether the agency wishes to get a better understanding of the specific compliance issues at the audited facilities (or aspects of those facilities) because the audits will serve to gather critical facility compliance information that may be largely unknown to the agency, or instead, whether the potential violations are a less critical aspect of the enforcement action (e.g., not the regulatory subjects of the enforcement action). If the potential violations are thought to be significant and pervasive throughout the company's facilities and are a fundamental part of the enforcement action or an area suspected of significant noncompliance, EPA may likely wish to require disclosure. Case teams should think carefully about the scope of required disclosures and may wish to positively identify priority compliance areas to avoid inundation with information regarding relatively less significant violations.[3]

Requiring disclosure may also depend largely on whether the agency wishes to have an active role in measures taken by the company to bring its facility into compliance. For certain violations (e.g., EPCRA 313 Form R), the Agency may simply require a certification that the company has made the corrections, along with a description of what the corrections entailed. For violations of other regulations (e.g., CAA New Source Review), EPA will likely want to require that it receive violation information and that it play a role in selecting the appropriate corrective measures. Similarly, the cost of corrections may be a factor to consider in establishing the appropriate amount of disclosure required; where significant capital expenditures are required, EPA may have a greater interest in obtaining information regarding those violations to ensure that appropriate followup activity remains a corporate priority. In some instances, EPA may not wish to receive all violation information, but instead may wish to preserve optional access to the company's audit reports.

There are additional factors that are unrelated to violation type that may be relevant to establishing disclosure requirements. The case team may want to consider whether any environmental justice issues have arisen at the facilities to be audited that may warrant additional disclosure of information, and the defendant's history of openness with regulators. The case team may also wish to consider whether the company is a significant source of pollutants and the value to the agency of receiving certain types of information or being involved with certain

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[3] This approach may be most applicable in cases of multi-media audits where the Agency may have greater concern for certain priority areas.

corrections associated with that source, including any effect the corrections may have on the industry of which the defendant is a part. The role of a consultant auditor may influence the case team's decision regarding disclosures; in general, where disclosure is required, consultant auditors are required.[4]

If the case team decides to require disclosure of all or some violation types, it should give some thought in advance to process and data management. The case team should consider whether a contract mechanism for data management would be most efficient, and develop a communication and processing strategy for disclosures from facilities located in other Regions (e.g., will the lead Region review the disclosures? the Region in which the disclosing facility is located? Headquarters?). In communicating with other Regions, the case team should provide all relevant information regarding approved audit protocols and the extent of disclosure requirements, and be clear about expectations for any followup work (e.g., in resolving subsequent liabilities, will the other Regions be providing support to a national settlement, or primarily responsible for resolving the violations that occurred within their Region?).

3. If disclosure is required, how should penalties associated with violations discovered during the audit be addressed?

For settlements that require all or certain violations discovered during the course of the audit(s) to be disclosed, the case team should consider and address in advance how potential penalties associated with those violations will be handled. There are numerous options for addressing penalties, ranging from collecting violation-specific individually-calculated penalties to no collection of penalties.

Whatever penalty structure the case team determines is appropriate for the disclosed information, it is critical that the issue be analyzed vis a vis the entire scope of the settlement, including the total benefit to the public health and the environment, the total penalty collected under the terms of the settlement, whether the audit was conducted as a significant or minor aspect of the settlement (including, e.g., consideration for the number of facilities to be audited), and the gravity of the violations to be discovered, if known.

Methods for Addressing Penalties:

1. The case team may consciously decide that the consent decree remain silent on the issue of penalties for violations discovered as part of the audit. If so, and if the audit is conducted as a component of agreement terms to implement a comprehensive environmental management system, EPA's Audit Policy (*Incentives for Self-Policing: Discovery, Disclosure, Correction and Prevention of Violations*, 65 Fed. Reg. 19618

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[4] In such cases, EPA will likely wish to have a role in the selection of an auditor, often including the ability to strike an auditor from a list of proposed auditors submitted by the defendant. To the extent that in-house auditors are truly independent of the facility, and the corporate audit group appears trustworthy and qualified, such auditors may be appropriate for cases in which disclosure is not required.

(Apr. 11, 2000) provides for penalty mitigation. Based on our experience, silence regarding penalties to be collected in a consent decree may create inefficiencies for EPA in subsequent penalty pursuits. It is advisable that if the case team intends to impose penalties for the disclosed violations that it address the issue affirmatively in the consent decree, to clarify for both the defendant and other Regions that become involved with the facilities at a later date.

2. The case team may wish to identify the media-specific penalty policies as the bases for resolving penalties associated with disclosed violations (the Audit Policy would not be specified). This may provide penalty reductions for certain aspects of the disclosed violations, but will vary among the media programs.

3. The case team may wish to specify that Audit Policy credit would be possible if policy conditions are met, and include in the consent decree an exception for timely disclosure (obviated by the settlement provisions for a disclosure schedule). This would require that disclosed violations be reviewed individually to determine eligibility for penalty mitigation.

4. The case team may wish to grant Audit Policy credit and stipulate in advance that certain policy conditions are met by the terms of the audit structure and schedule (e.g., for purposes of the disclosures under settlement, the disclosures are deemed to have met the systematic discovery, voluntary discovery, prompt disclosure, independent discovery and disclosure, and no repeat violation conditions). This approach would require a less intensive review of policy conditions to determine eligibility for penalty mitigation and may contemplate a global resolution of all disclosed violations at the completion of the audit period; consistent with the Audit Policy, any economic benefit gained would be recovered. For many cases, this option will be the most efficient while yielding the greatest environmental benefits.

5. The case team may wish to stipulate in the consent decree the penalties, corrections, or both, associated with certain violation types. This option may require more agency resources during settlement, but would likely yield resource savings at the point of resolving the disclosed violations. This may be most practical for cases in which the scope of applicability requirements, and, therefore, potential violations are limited; it may be difficult for violations that have significant variations in the economic benefit gained from noncompliance. Where appropriate, stipulations of this type could be extremely efficient for any violations discovered by the company.

Whether to Collect Penalties: Factors to Consider

Situations for which seeking no penalty for disclosed violations may be most appropriate include those where the economic benefit is likely to be insignificant, the audit is not a significant component (environmentally or financially) of the settlement, and a significant penalty was collected earlier as a critical part of the case.

Situations for which seeking some penalty (including unspecified amounts) for disclosed violations may be most appropriate include those involving an audit as a central component of the settlement; actual harm to the environment; suspicion of repeat violations; culpable behavior; and anticipation of significant economic benefit (although full collection may not be appropriate, based on litigation risk factors).

Situations in which advanced penalty stipulations are most appropriate include those involving significant litigation risk; potential violations and/or penalties associated with them are known in advance; advanced agreement as to the type of corrective measures to be performed; and the value of corrective measures known with some certainty.

Conclusion:
We recognize that the case-specific factors affecting settlement are numerous and that ultimately each case must be considered individually. The discussion here is based on experiences to date and provides a general approach and factors to consider in reaching a sound decision. If you have questions regarding this topic, you may wish to call Leslie Jones at 202-564-5123 or Peter Moore at 202-564-6014.