OREGON STATE BAR
SECTION
Environment & Natural Resources

OUTLOOK

Environmental & Natural Resources Section

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Table of Contents

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SUPPLEMENTAL ENVIRONMENTAL POLICIES (SEP)

Supplement Environmental Projects in Region 10

By Elin Miller, Administrator, Region 10, Environmental Protection Agency

Supplemental Environmental Projects (SEPs) are environmentally beneficial projects that violators are not otherwise legally required to perform, but agree to undertake in settlement of enforcement actions. SEPs offer unique opportunities to further our Nation's goals of ensuring clean air and water, safe food, and better waste management, and of expanding the public's right to know about their environment. While the U.S. Environmental Protection Agency (EPA) has secured significant public health and environmental benefits through SEPs, across the nation, I suggest there is room for growth in these endeavors in EPA Region 10, even as we remain mindful of the guideline in the Agency's 1998 SEP policy.[1]

As Administrator of Region 10, I want to create an environment that encourages violators to suggest, develop and implement creative community-based SEPs. Agreeing to take on SEPs in the settlement of enforcement actions provides a great opportunity to take a negative situation and turn it into a positive one for everyone. Communities where violations occurred benefit from the additional environmental or public health outcomes; and violators benefit from improved public relations.

EPA is a regulatory and enforcement agency. It is the expectation of Congress and our citizens that we protect the environment and, when necessary, take enforcement action to compel violators to return to compliance and to pay appropriate penalties. There is no question that a strong enforcement program serves as a significant deterrent to illegal conduct.

Regularly considering and agreeing to SEPs as part of the enforcement settlement process creates the potential for new and lasting working relationships between regulated entities, EPA, and community beneficiaries. SEPs may form new relationships that didn't exist or improve upon those that were not positive. EPA not only encourages violators to consider SEPs as part of a settlement, but also encourages violators to involve the community in identifying and developing potential SEP projects.

Continued on next page

Take for example Emerald Services, Inc., of Tacoma, Washington. Emerald was required to pay over $38,000 for not reporting the release of approximately 1,697 pounds of toluene, a hazardous substance, into a storm sewer at its hazardous waste treatment and storage facility in 2005. Two weeks after the release, the toluene ignited, setting off multiple explosions. Only then did Emerald report the chemical release to the National Response Center. Failure to notify appropriate agencies of the toluene release is a violation of the federal Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA or "Superfund").

In addition to paying the penalty, Emerald agreed to a SEP that provided $31,585 worth of emergency response equipment to the City of Tacoma Fire Department's Fire Prevention Bureau, as well as $37,980 worth of equipment to the City of Tacoma's Environmental Services Source Control division for use in tracking information about discharges from industrial facilities to the city's pretreatment facility. This SEP not only enhanced the City's ability to respond to accidental chemical releases that could harm the public and the environment, but also reduced the likelihood that such releases would go undetected in the future.

I believe that most people want to and will do the right thing. Violators, through SEPs, have an opportunity to create a stronger or new community service ethic for the community in which they are located. As the saying goes, "Good neighbors beget good neighbors."

A recent example of this is an enforcement settlement reached last December with Coeur Alaska Inc., in Juneau, for violating the company's construction storm water discharge permit limits into a salmon-bearing creek. In addition to paying a penalty of $18,334, and conducting injunctive relief valued in excess of $1,000,000 to resolve federal Clean Water Act violations at its Kensington Gold Project, the company agreed to perform a SEP to acquire a wetland near Juneau. The wetlands acquired are a valuable property within the Strawberry Creek drainage near mile 25 Glacier Highway. The Southeast Alaska Land Trust will administer a conservation easement that will protect a complex drainage of fen, marsh, uplift meadow, ponds and wetlands.

Both the mining industry and wild salmon fisheries play important roles in Alaska's economy. The Coeur Alaska SEP demonstrates that the community benefited by the SEP can be more than the residents adjacent to a violating facility. Rather, the community can be creatively defined to include diverse economic interests such as salmon fisheries needing protection of salmon supporting waters from construction-related sediment discharges.

SEPs also can provide communities with an opportunity for projects that directly address the problems of environmental justice. A residential apartment building owner and manager in the Seattle metro area, Longwell Company, this year reached a $2,259 settlement for violations of EPA's lead-based paint disclosure rules. Selling or leasing pre-1978 housing includes an obligation to inform parents how they can protect their children from the health hazards associated with lead-based paint and lead-based paint hazards. In this case, the company agreed to perform a SEP valued at $150,000. The project will include the replacement of existing windows, window frames and sills, sliding doors and sliding door frames with new *lead-free* fixtures at the Pinewood Square Apartments, in Lynnwood, Washington.

Having children suffer lead poisoning from deteriorating paint is an avoidable tragedy. By agreeing to the SEP, Longwell Company took a positive step to reduce the hazards of exposure to lead in the housing it leases.

In a recent Region 10-sponsored colloquium, community, government, and industry leaders agreed that SEPs can be utilized to highlight the opportunity for other investments, commitments, and actions that can benefit the community where a project is undertaken. Lang Marsh's article appearing elsewhere in this issue focuses on how the use of collaborative processes can achieve enhanced environmental and health benefits for affected communities.

Once a company has participated in a settlement involving a SEP, other industries in that same sector, as well as other sectors, learn about the process and how successful it is and have incorporated SEPs into their own enforcement settlements.

Currently, only 10 percent of the enforcement settlements nationwide annually include SEPs. After reviewing the benefits, one may ask "why?" I see two areas that are ripe for discussion. First, there is a need to increase awareness among regulators and the regulated community about SEPs and EPA's SEP policy. Second, it generally takes more time and resources to negotiate a SEP and to oversee milestones accomplished. We must find appropriate ways to streamline SEP negotiations, and other appropriate means to oversee SEP implementation in accordance with the settlement agreement. If we can succeed in these areas – increased awareness and enhancing SEP negotiations and oversight - we could increase the use of SEPs in this region and across the country.

For further information, contact Mark MacIntyre, Public Affairs Officer (206) 553-7302.

Endnotes

1 *See*, Final Supplement Environmental Policy Guidance (April10, 1998) at http://www.epa.gov/compliance/resources/policies/civil/seps/fnlsup-hermn-mem.pdf. All EPA SEP Policies and Guidances are available at http://cfpub.epa.gov/compliance/resources/policies/civil/seps.

Recent Revisions to the Oregon DEQ Policy

By Les Carlough, Office of Compliance and Enforcement, Oregon DEQ

The Oregon Department of Environmental Quality has long considered a violator's willingness to invest in a project that improves the environment when settling penalties for violations of environmental law. DEQ's goal in its Supplemental Environmental Project (SEP) program is to use the penalty as incentive to obtain environmental benefits that would not otherwise occur, either because the actions are not required by law or because the violator would not have seen the project as economically viable. Although a SEP does not reduce the amount of money the violator pays out as a result of the enforcement, violators often prefer to expend their penalty dollars in a way that benefits the environment and local community and also partially mitigates the public-relations impact of the violations.

In deciding whether to agree to reduce a penalty in exchange for a project, DEQ has applied an internal management directive based substantially on the federal SEP policy. Four important requirements under DEQ directive are:

- the project must achieve a measurable benefit for human health or the environment in Oregon;
- the project must not be something otherwise required by law;
- the project must not create an economic advantage for the violator although otherwise acceptable projects can be valued accordingly to meet this requirement; and
- when publicizing the SEP, the violator must state in a prominent manner that the project is being undertaken as part of the settlement of a DEQ enforcement action.

One important distinction between DEQ's directive and EPA's policy is that when settling penalties with EPA, violators must show that the SEP has a logical nexus to the violation. Although the nexus requirement does not apply in Oregon settlements DEQ's SEP directive focuses the SEPs toward important work through a series of "preference criteria" including a preference for SEPs that relate to the same environmental program as the violation and will be implemented in the same geographic area as the violation.

Oregon's SEP policy and the projects it has produced have been a boon to many Oregon communities. In 2006, DEQ agreed to allow the Cascade Healthcare Community, Inc. (St. Charles Medical Center) to partially settle penalties for solid waste disposal violations by contributing $24,488 to the Central Oregon Community Action Agency Network's Food Recovery Project. Using those funds the "COCAAN" will be able to expand its efforts to collect waste food from food processors and distributors, grocery stores, restaurants, and other outlets that serve food. Collected food that is usable for human consumption is provided to about thirty emergency and supplemental food programs that serve Crook, Deschutes, and Jefferson Counties. Waste food that is unusable is composted by local farmers. Either way, the waste food is diverted from taking up landfill space and instead used constructively. In another, more recent settlement with DEQ, Jeld-Wen, Inc. agreed to partially mitigate penalties for air contaminant permit violations by contributing $11,600 toward retrofitting Klamath Falls school buses with clean diesel technology. Jeld-Wen's contribution will be leveraged to obtain additional matching funds and will result in less diesel particulate emitted from the buses, less exposure to diesel by school children, and less impact to the local air. DEQ has had great success with its SEP programs and, during 2007, agreed to another six SEPs, equally innovative and beneficial to human health and the environment. However, this is only a small portion of the 224 penalties that DEQ concluded in 2007, demonstrating that there are more gains to be made through better implementation of DEQ's SEP authorities.

In October 2007, DEQ adopted revisions to its policy in an effort to streamline the proposal and approval process and also to make SEPs a more attractive settlement alternative for violators. The new directive can be obtained at http://www.deq.state.or.us/programs/enforcement/SEPpolicy07.pdf. The most important of the changes are that DEQ:

- Eliminated the prohibition on SEPs for violations done willfully, flagrantly, or with criminal intent. That requirement addressed DEQ's concern that intentional violators might be untrustworthy or less capable which could translate into excessive oversight effort for DEQ. The new directive states a preference that SEPs for these high mental-state violations be handled by third parties and a requirement that the violator's responsibilities be commensurate with its expertise and capabilities;
- Eliminated a complicated SEP valuation formula based on the type of project. That formula was designed to encourage SEPs that result in actual benefit. The new directive simply specifies a preference for SEPs that result in tangible environmental outcome;
- Eliminated the prohibition on SEPs for penalties less than $2,000. That requirement addressed a concern that the environmental return of small SEPs would not justify the

Continued on page 15

Best Practices for Administering a SEP Program[1]

By Monica Kirk, Environmental Justice Attorney, Office of Enforcement and Compliance Assurance, EPA Region 10[2]

Highlights of Federal SEP Policies and Practices

Since the *1988 Final SEP Policy,* EPA has issued several additional SEP policies.[3] These policies incorporate congressional and judicial guidelines and address several important issues including categories of acceptable SEPs, procedures for calculation of the final penalty, liability for nonperformance, oversight and drafting of enforceable SEPs, stipulated penalties, community input, approval procedures, profitable SEPs, aggregation of funds and the use of third parties to manage or implement SEPs.

To ensure that the Agency's enforcement discretion is used appropriately and in compliance with federal law, a US EPA SEP must:

- Be related to—that is, have a "nexus" to—the underlying violation;
- Provide significant environmental and public health benefits;
- Benefit the community affected by the violation; and
- Secure public health and/or environmental improvements beyond what is achievable under applicable environmental law.

Although the SEP policies of the United States Environmental Protection Agency (US EPA) have shaped state practices, neither federal law nor policy require states to conform to federal SEP policies. In general, federal SEP policies are more restrictive than state policies.

Highlights of State SEP Policies and Programs

According to a survey conducted by Hastings Law School, 32 states have formal, published SEP policies and 16 states (and the District of Columbia) have informal practices or internal, unpublished policies.[4] Only two states—North Carolina and South Carolina—have rejected SEPs. State SEP policies vary with respect to (1) legal requirements such as nexus, agency authority to manage funds, contributions to third parties, eligibility of willfull or repeat violators, percentage of the penalty that can be mitigated, (2) types of allowable projects, (3) public accessibility of SEP-related information, and (4) degree of community involvement.

Best Practices from Federal and State SEP programs

The Public Accessibility Principle

It is axiomatic that publicly accessible information makes it more likely that an enforcement action will conclude with a SEP. For this reason, EPA provides a link to its SEP policies on its webpage and EPA's Office of Enforcement and Compliance Assurance (OECA) routinely updates its webpage directory of significant cases with SEP settlements. OECA also collects project ideas from interested parties to include in the Agency's *Potential Supplemental Environmental Projects Guidance*.[5]

Some states also have publicly accessible SEP information, but practices vary widely. Thirteen states provide a link to their SEP policies and eleven of these provide one or more of the following:

- A link to the US EPA's ECHO database, which allows for a SEP search;
- Guidelines and access to a SEP Idea Bank, allowing the public to post and/or view suggested project ideas for SEPs; and
- The ability for penalties to be placed into a community fund (SEP Fund Bank) for an environmentally beneficial project.

The SEP "Idea Bank"

A "SEP Idea Bank" is a pre-approved list of proposed SEPs contributed by various sources. It allows violators to choose a project that has already been vetted by the agency and is of interest to the non-agency proponent. Some states provide public access to submitted proposals while others only provide publicly accessible instructions and/or mechanisms (*e.g.*, a web-based form) for submission. One example is the website for the Illinois Environmental Protection Agency which includes an explanation of each SEP category (*e.g.*, public health, pollution prevention, pollution reduction) and instructions about how to post suggestions onto the agency's publicly accessible SEP Idea Bank. Proposed projects are posted for two years.

Project ideas in a publicly accessible SEP Idea Bank can be catalogued by location, cost, or category. Upon the request of a violator, the agency enforcement case team may consult the Idea Bank for relevant SEP ideas, or refer violators to do so. Providing guidance—and technical assistance—during the initial stages of project submission helps prevent misunderstandings about cost expectations, increases long-term efficiency, and makes it more likely that beneficial community projects will be undertaken as SEPs. For example, US EPA Region 1 has adopted a Best Practice that fosters community involvement in identifying potential projects. The Region screens project ideas, and in consultation with the proponent, develops a proposal that includes realistic cost estimates for the project.

Idea Banks appear to be helpful in

creating interest in SEPs. One state website with SEP Guidance and an "Idea Bank" of pre-approved SEPs concludes 11.8% of enforcement cases with a SEP, representing 42.5% of the total penalty dollars. Another comparable state website concludes 6.4% of all enforcement cases with a SEP, representing 63.4% of total penalty dollars. Where a SEP Fund was available, 28.8% of all enforcement actions concluded with a SEP. In contrast, state websites with little or no mention of SEPs conclude less than 3% of their enforcement with a SEP, representing only about 3% of the total penalty dollars.

The SEP "Library"

A "SEP Library" is a database of approved or successful SEPs that provides a frame of reference for those developing SEPs. Thus, new SEP proposals benefit from past lessons learned, increasing the overall efficiency of the SEP process and reducing transactional costs. The Massachusetts Department of Environmental Protection (MassDEP) provides a publicly accessible SEP Library containing the following information: case names, the budget for SEPs (including credit in penalties), short descriptions of the SEP activities, and the violations that prompted enforcement action. The SEPs are arranged alphabetically and by category.

One problem with the SEP Library is the concern that a project's inclusion will be perceived as an assurance that it will be accepted by the agency. Clearly articulated caveats may be used to overcome this barrier to having a SEP Library. Alternatively, access to the SEP Library can be limited to "in house" staff until parties understand the library's limits. The Washington Department of Ecology's (Ecology) Water Quality Program maintains an "in house" SEP Library. Along with the SEP description and project title, the site provides a link to each project's settlement agreement, enabling Ecology's enforcement staff to access approved past projects and serving as a resource for evaluating future project proposals.

The SEP "Fund Bank"

A "SEP Fund Bank" aggregates smaller amounts of SEP funds for use on larger projects. SEP funds are set aside into escrow accounts and managed for SEP implementation by state enforcement agencies or private entities.[6] Both New York and Delaware have versions of a SEP Fund Bank.

The New York Department of Environmental Conservation has an Environmental Benefit Projects Policy that authorizes escrow accounts for SEP funds. Violators settling under this policy may place the penalty funds into an escrow account to fund unspecified future projects. The escrow is held either by the violator or by an approved independent escrow agent and the interest and remaining account balance is given over to the state at the conclusion of the SEP.

Delaware's Department of Natural Resources and Environmental Control manages the state's Community Environmental Protection Fund. According to the Fund's authorizing statute, the Fund will consist of 25% of the civil and administrative penalties collected by the agency, pursuant to its general enforcement authority, as well as penalties collected pursuant to specific statutory authority relating to sediment and erosion control, wetlands protection, coastal zone protection, chronic violators, and hazardous substance clean up. While the Fund does not receive funds from SEPs, it has many of the same qualities of an SEP Fund Bank. Delaware's website provides a publicly accessible application with guidelines and examples of suggested projects. The DNREC website also provides PDF downloads of Fund account statements that provide fund balances for public review.

Conclusions

- SEPs are generally underutilized, and government could benefit by examining SEP policies as well as practices that enhance opportunities for SEPs.
- Government should consider developing publicly available SEP Libraries, Idea Banks, and Fund Banks to expand the opportunities for SEPs and make the process more efficient and accessible.
- Information is key to an authentically transparent and inclusive process with the potential for community involvement and investment.

Endnotes

1 Excerpted from *National Policy Consensus Center, Environmental Enforcement Solutions: How Collaborative SEPs Enhance Community Benefits,* available at http://www.policyconsensus.org/publications/reports/index.html.

2 Currently on temporary assignment to US EPA Office of Environmental Justice in Washington, D.C.

3 See http://cfpub.epa.gov/compliance/resources/policies/civil/seps.

4 The Public Law Research Institute, Hastings College of the Law, Univ. California, *Supplemental Environmental Projects: A Fifty State Survey with Model Practices* (S. Bonorris, ed.), available at www.uchastings.edu/site_files/plri/ABAHastingsSEPreport.pdf, (written in association with the American Bar Association's Section of Individual Rights and Responsibilities; co-Sponsored by the Section of Environment, Energy, and Natural Resources and Section of State and Local Government Law).

5 See http://www.epa.gov/compliance/resources/policies/civil/seps/projectsideas42004.pdf

6 In contrast with some state programs, US EPA's SEP policy allows aggregation of separate SEP funds only where (1) separate violators pool resources to hire a contractor to manage and/or implement a consolidated SEP or where (2) separate violators perform discrete and segregable projects within a larger SEP. Under either scenario, violators remain liable in the same manner as they would under a typical settlement, including the implementation and completion of the SEP. US EPA, *Guidance Concerning the Use of Third Parties in the Performance of Supplemental Environmental Projects (SEPs) and the Aggregation of SEP Funds* (December 15, 2003), available at http://www.epa.gov/compliance/resources/policies/civil/seps/seps-thirdparties.pdf.

Pacific Shrimp Co.'s Supplemental Environmental Project with the MidCoast Watersheds Council

By Diane Henkels, Associate Attorney General for the Confederated Tribes of the Umatilla Indian Reservation[1]

The story of Pacific Shrimp Co.'s SEP started with a casual reading of Newport, Oregon News-Times on September 28, 2005. The Oregon Department of Environmental Quality (DEQ) had imposed a $14,235 fine on the shrimp plant for failing to monitor and report wastewater discharges from its facilities on Bay Boulevard on Yaquina Bay. The shrimp plant had been operating since 1999 under a DEQ National Pollutant Discharge Elimination System General Permit No. 900-J. The 900-J permits apply to fish plants which discharge into the waters of the state adequately treated wastewaters from specific discharge points and in conformance with conditions including monitoring and reporting. DEQ sent Pacific Shrimp Co. a Notice of Violation and Assessment of Civil Penalty for failure to comply with its permit.

The News-Times write up of the DEQ fine caught the attention of a MidCoast Watersheds Council (Council) member who brought the fine to the Council's attention. The Council's mission is to improve the health of the streams and watersheds of Oregon's central coast so they produce clean water, rebuild healthy salmon populations, and support a healthy ecosystem and economy. The Council works watersheds throughout Oregon's central coast, that is, the Salmon, Siletz, Yaquina, Alsea, and Yachats rivers, and more than 28 smaller ocean tributaries. Generally, in the Yaquina River watershed, most of the Council's on-the-ground restoration and education work had focused up river in the more rural sections of the Yaquina, above tide water, or in the several salt marshes lining the estuary.

The shrimp plant and the Council had already been in conversation about collaborating on various water conservation issues, and so the door was already open for the two to seriously contemplate an SEP in the Yaquina. Until that time, the Council had not worked with an industrial partner in Newport, nor with a SEP. Council members were concerned that the arrangement would allow the plant to "get off easy" and to get undue credit considering the allegations that the plant had violated its water quality permit. For its part, the plant saw an opportunity to keep a large share of the resources it expended on resolving this matter in the Yaquina River basin rather than sending it on to Salem to the state's General Fund. Also, plant management and staff expressed interest in protecting the health of the watershed and Yaquina Bay. DEQ was receptive to the SEP but made it clear that the agency had the discretion to reject the deal.

The Council's concerns were allayed by the required criteria for Oregon's SEPs. According to the Internal Management Directive on Supplemental Environmental Projects (Directive), the SEP cannot be used to supplant DEQ obligations, and it may not create a significant market advantage for the respondent. Indeed, to this author's knowledge, this article is the only publicity the plant has received on this issue.

The total amount of the civil penalty was $12,635, of which 80%, or $10,108, could be used to mitigate the fine by funding an SEP. The Council proposed a split to fund each of the goals it pursues: educating the public on watershed issues, assessing watershed conditions, and implementing scientifically-based projects to promote or restore watershed health. In addition, the Council decided to focus the benefits of the SEP in the Yaquina, the same watershed as the Pacific Shrimp Co. operations. An agreement was written up that allocated one-third of the SEP funds to funding a water quality monitoring project of the Yaquina River, one-third to the pre-purchase appraisal of 33 acres of salt marsh, and one-third to fund a Natural Resource crew program. The water quality program recently begun in Yaquina provides water quality monitoring data from several points along the river. Easements and property purchases protect the salt marshes and tidal flow that provide vital habitat to rearing salmon preparing their seaward migration. Natural resource crews operated by the Council's education staff are teams of selected local teenagers working on various watershed projects. The plant's payment of the SEP funds benefited the watershed and the Council by allowing projects which would not have occurred to this scale were it not for the impending penalty.

While interested in the SEP for this case, at first DEQ rejected the proposed expenditure plan, namely the education component as lacking accountability for the crew members' work. It was easier to make the case that the water quality monitoring and the salt marsh appraisal fit categories outlined in the Directive's preference criteria. However, there is no "environmental education" preference criteria so that component had to fit the "other projects" which are required to be fully consistent with all other provisions of the SEP Policy and approved by the Department. The Council provided DEQ staff with summaries of the

Continued on page 15

The Benefits of Collaborative Supplemental Environmental Projects[1]

By Langdon Marsh, National Policy Consensus Center and former Director of the Oregon Department of Environmental Quality

When faced with a significant violation of environmental law, environmental agencies often have to balance the need for sending strong enforcement signals with the opportunity to provide benefits to the community affected by the violation. Supplemental Environmental Projects (SEPs) developed with meaningful community involvement can provide significant benefits for the community, the violator, and the enforcement agency. SEPs are environmentally beneficial projects that are undertaken voluntarily by violators; in return, a state or US EPA may mitigate the penalty imposed. Two recent reports make the case for greater use of collaborative approaches involving the affected communities in developing and implementing SEPs.

Using SEPs to Leverage Additional Investments in Solving Community Problems

Imagine your agency has levied a big fine against a port authority for some air quality violations. The port is willing to do a SEP, in part to remedy its image, but also to deal with concerns of a neighboring community that sees itself affected by emissions from the port and the trucks, ships, and trains moving goods to and fro. Both you and the port see the opportunity to use the SEP to leverage other investments from businesses, the city, the state, and other organizations. You and the port ask the mayor to appoint a respected former public official to convene these and other stakeholders. A facilitated process managed by a local university center in a few meetings produces an agreement that everyone signs committing each entity or organization to a series of actions that will reduce diesel and other emissions. The actual SEP commits the port to subsidize the retrofit of single-owner drayage trucks using the port. Projects of others include agreements to retrofit public and private diesel-powered fleets that use the port, public health monitoring, and education and job training. The combination of these investments results in benefits far greater than the actual SEP project alone.

This is the kind of solutions-oriented outcome envisioned in a new report on SEPs from the National Policy Consensus Center (NPCC).[2] The report finds that combining model SEP practices that encourage community input and promote environmental justice with advanced collaborative problem solving techniques can produce larger and more satisfying outcomes from SEPs.

The NPCC report concludes that SEPs are underutilized generally and that newly developed collaborative governance processes can lead to greater community benefits by leveraging SEPs with other investments, actions, and commitments. It recommends that the states and U.S. EPA consider undertaking pilot collaborative SEPs to determine violator and community interest, and that they should develop "best practices" based on a collaborative governance process such as the Public Solutions System developed by NPCC.

What is Collaborative Governance?

Collaborative governance involves leaders in the state or the community engaging with all sectors—public, private, non-profit, citizens, and others—to develop effective, lasting solutions to public problems that go beyond what any sector could achieve on its own.

In a number of successful projects in Oregon, NPCC has employed a collaborative governance approach in which the governor appoints a legislator, local official, or respected civic leader to bring diverse parties together to work on a common problem. NPCC, as an impartial organization, performs an assessment of the probability of success and assists the convener in bringing together participants representing all interests to reach agreement on the issues. The key difference from other collaborative processes is the deliberate engagement of leaders in getting people to the table. The successful outcome in a typical Oregon Solutions project is that additional resources are committed by participants in amounts three to four times greater than the value of the original project.

More than 30 Oregon Solutions projects have used what NPCC calls the Public Solutions System. Several of the projects were similar to SEPs. For example, in North Portland, which has the highest levels of diesel emissions in the state, community groups, non-profit organizations, and private and public fleets reached an agreement to reduce diesel emissions through fuel and equipment upgrade projects. The parties incorporated a blend of public and private cost-sharing to support action on each party's voluntary commitments.

Collaborative SEPs

Some past SEPs illustrate aspects of collaborative SEPs. A good example is the *Detroit River SEP.* Demonstrating how an SEP can be integrated with other projects in support of a commu-

Continued next page

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SUPPLEMENTAL ENVIRONMENTAL POLICIES (SEP)

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Those wishing to follow up on topics addressed in *Outlook* should consider purchasing the 2006 Supplement to the Environmental and Natural Resources Law Deskbook. With 43 chapters of detailed information, the Deskbook and Supplement present discussions on national and Oregon environmental statutes, rules, and cases. Contact OSB CLE Publications or an ENR Executive Committee Member for more information.

Attorneys using *Outlook* should also research original and other sources.

nity objective, U.S. Steel, in coordination with companies, agencies, municipalities, foundations, and individuals, rehabilitated approximately 2,000 feet of shoreline to create the nation's only international wildlife refuge.

Similarly, in the *Neponset River/East Boston Greenways SEP,* negotiated by U.S. EPA Region 1 and the State of Massachusetts, a $2 million SEP was enhanced by an additional $1.2 million of funds that allowed the Trust for Public Land to acquire greenway sites.

Under another model of collaborative SEPs, the enforcement agency actively engages members of the community in identifying the projects to be funded through the SEP. The *Rocky Mountain Steel Mills SEP* resulted from concurrent federal and state enforcement actions by U.S. EPA Region 8 and the State of Colorado. The agencies succeeded in mobilizing a community of low-income, predominately Hispanic new immigrants and third-generation families and collaboratively selected nine public health projects, using funds contributed by the company.

Some community organizations have engaged in a process similar to the SEP process that results in a Community Benefits Agreement (CBA) mitigating unintended environmental, health, and economic consequences from new development. In one well-known case, a local organization successfully negotiated a CBA with the City of Los Angeles regarding the expansion of the LAX airport that included environmental mitigation and community benefits for nearby communities, while also ensuring good jobs for local residents.

ABA Report

A second recent report on SEPs was written by the Public Law Research Institute at Hastings College of the Law in association with the American Bar Association (ABA). The ABA survey summarizes the SEP practices of the states and reports that 28 states and the District of Columbia have instituted formal, published SEP policies.

The survey finds that, in designing their own policies, states are not strictly bound by the fairly rigid restrictions of U.S. EPA's SEP policy. For example, states need not strictly follow U.S. EPA policy requiring a nexus between the violation and the SEP, although some nexus requirement is desirable to ensure that the community where the violation occurred gets an appropriate benefit.

The ABA report concludes that SEPs have multiple benefits: *SEPs represent a real and practicable opportunity to provide significant benefits to all the stakeholders in the environment: the environment itself, affected communities, the regulated industry, and the regulators.*

Benefits of SEPs

There are potential additional benefits from collaborative SEPs. To the violator, these include building more effective relationships with the various communities they may wish to influence, including local jurisdictions, neighborhood or community-wide organizations, staff, workers and labor representatives, national business or environmental organizations, businesses to which they provide goods and services or are in their own supply chain, and, most importantly, their own customers.

The community will benefit from the additional investments in priority projects through the enhancing effect of a collaborative process. Individual organizations can see more of their objectives met and learn how to work better with the violator, community leaders, and the agency.

The state and federal enforcing agencies will find multiple objectives promoted by more robust SEPs, including reduction of environmental problems, enhancement of community sustainability, reduction of conflict inherent in enforcement, and greater visibility in communities they serve.

Conclusion

States and violators should weigh the pros and cons of implementing collab-

Continued on page 15

SEPs, Third Parties and Stipulated Penalties: Managing Outside Contractors for Environmental Benefit

By Steven Bonorris, Associate Director for Research at the Center for State and Local Government Law at UC Hastings College of the Law

As noted elsewhere in this issue, SEPs are environmentally beneficial projects that a violator agrees to perform, in consideration of which the regulator may mitigate the initially proposed penalty by an amount commensurate with the cost of the SEP. Successful SEPs can greatly benefit the community by returning environmental benefits directly to areas and populations affected by environmental violations, but SEPs can fail for a variety of reasons.

Most dramatically, a violator or its contractor can act in bad faith, and simply fail to expend the funds specified in the settlement agreement. In this case of noncompliance, regulators appropriately wield the stipulated penalty provisions in most settlement agreements. SEPs may also fail under good-faith circumstances: the project may not achieve its promised benefits; the project's actual cost may be substantially less than the estimate in the settlement agreement; the project may inadvertently cause harm to the environment; or the project may suffer other unforeseen circumstances that prevent the promised SEP from materializing.

These "good faith" failures can arise in SEPs that are performed by the violators directly. They can also occur with SEPs performed by third parties. A third party SEP is one in which a violator, recognizing that it might not have the expertise to conduct a SEP, outsources project implementation to a third party, possibly a nonprofit, community group or other environmental contractor. Some states encourage violators to use third party services for either project oversight or actual project implementation, partly in recognition that the interposition of a neutral third party can enhance the likelihood of successful projects. Both Cal/EPA and Oregon DEQ, for instance, may require the use of a competent third party implementer if a violator lacks the relevant technical expertise, and Oregon DEQ's revised policy described by Carlough elsewhere in this issue anticipates the use of third party implementers for SEPs used to settle violations caused with high mental state.

Understandably, due to differing priorities, violators and environmental agencies have disparate approaches to SEP enforcement. Violators would like to see outsourcing contracts (together with their timely payments to the contractor) deemed as their compliance with the settlement agreement. Violators argue that if all the funds have been disbursed to the third party implementer, then the punitive aims of the underlying environmental statute have been achieved and the enforcement matter should draw to a close. On the other hand, environmental agencies and prosecutors are hesitant to let go of the stick of further liability, out of a concern that without the threat of renewed enforcement actions (up to the originally assessed penalty in some states) SEPs will not be completed satisfactorily, or even worse, may beget further environmental degradation. Agencies commonly wield no legal authority over a violator's contractor, leaving the regulator with no recourse except to look to the violator. The use of a third party also makes agency oversight of the project itself more problematic because the regulator will likely only be aware of implementers' performance through reports from the violator. Moreover, the (favored) use of community groups as third party implementers complicates the liability question, as they may have limited wherewithal to remedy a SEP gone bad. That the violator may have the legal right to pursue damages against a community group may be of little value.[1]

The topic of this note – the problem of third party liability for SEPs that go wrong – is rather narrow, but its themes spread out to a wide variety of other SEP issues, including stipulated penalties, rigorous screening of acceptable SEPs, and SEP oversight practices. This note will briefly discuss the approaches of US EPA and the states to the problem of failed SEPs in general before it will touch on the two models for tapping the expertise of third party implementers – a regulatory model and a contractual model.

Liability for Nonperformance of a SEP and Stipulated Penalties

Federal system

Under U.S. EPA's *Final SEP Policy*, violators are responsible for ensuring that a SEP is completed satisfactorily, although they may use the services of third party contractors to perform the SEP. The policy requires that the settlement agreement spell out stipulated penalties for failing to satisfactorily perform a SEP: penalties should range between 75 and 150% of the mitigation value originally awarded to the project. However, a violator may avoid the stipulated penalty if good faith and

timely efforts were made to complete the work and at least 90% of the funds budgeted for the SEP was spent. Pursuant to the *Final SEP Policy,* overestimating the cost of a SEP should also be penalized, even if the SEP is successfully completed. If the final cost of a completed SEP is less than 90% of the projected cost, the violator should pay a stipulated penalty, between 10 and 25% of the mitigation amount originally conferred. This provision implies that good faith is a defense against stipulated penalties.

Stipulated penalties themselves are frequently observed in environmental enforcement: U.S. EPA defines them as "fixed sums of money that a defendant agrees to pay for violating the terms of a decree…. [to encourage] compliance with a consent decree." In some cases, federal as well as state law may require that consent decrees contain stipulated penalties. The federal policy on stipulated penalties and the U.S. EPA *Final SEP policy* both target violators that act in bad faith in not complying with the terms of a settlement agreement.

The states

Many state policies resemble the federal SEP policy regarding the severity of stipulated penalties included in settlements with SEPs. Alabama requires that violators should pay at least 100% of the original mitigated amount, although a violator may avoid paying a penalty if a good faith effort was made and at least 90% of the projected SEP funds were expended. Connecticut's policy requires that if a SEP isn't satisfactorily completed, then the violator is "liable for the amount by which the assessed penalty was reduced, with interest, plus an additional 10% charge to cover the administrative costs incurred by the Department in reviewing and approving the failed SEP." Under Connecticut's provisions, a violator could, in total, expend funds on a SEP as well as the full measure of mitigated penalty plus a fine. Some violators have suggested that the specter of this kind of financial outlay deters them from pursuing settlements with SEPs, and that they prefer the certainty of a determinate penalty.

This note does not suggest that stipulated penalties are draconian in all cases, but the threat of stipulated penalties can deter the use of SEPs, particularly when the violator might be inclined to use an outside implementer or when a SEP utilizes unproven yet promising technologies. Stipulated penalties are wholly suitable in situations where the violator is in bad faith and fails to expend the promised funds on a project. But in cases of full expenditures of funds by reliable third party contractors, states interested in promoting SEPs could relax or modify stipulated penalties provisions.

States could also specify lower stipulated penalties for innovative, risky SEPs, for instance, if regulators and violators are jointly interested in using SEPs to advance knowledge and implementations of newer environmental technologies. More aggressively, stipulated penalties could be waived for violators who use approved third party implementers and distribute funds to the implementer in a timely fashion, as shall be seen in the case of Texas, below. These forms of tailored stipulated penalty provisions would ensure that violators that implement SEPs in good faith will not be affected by the possibly heavy weight of conventional stipulated penalties (as seen in the Connecticut policy). Outside of Texas's example, the Hastings/ABA survey found no state experimentation with stipulated penalty provisions; many states (and U.S. EPA) may waive stipulated penalties even for failed projects as a discretionary matter, however, if the violator acted in good faith and the bulk of the promised expenditures actually occurred.

The "regulatory approach" – enhanced procedures for successful SEPs

At bottom, the problem of managing third party liability (*and* direct violator liability) is addressed by the same procedural tools that promote and maximize the likelihood of successful SEPs. Particularly effective techniques identified by the Hastings/ABA Fifty State Survey include safeguards such as: 1) careful pre-screening of projects at the settlement stage (*e.g.*, Connecticut's "worst case scenario" scrutiny); 2) defining projects with particularity and embedding performance measures to verify project success; and 3) consistent oversight, often by approved third party overseers (Colorado, Maine). Third party implementation also raises unique issues, as the regulator will not be in direct contract with the implementer. This fact explains the retention of the threat of stipulated penalties, as stipulated penalties are the only instrument regulators possess to encourage violators to select reliable third party implementers.

Many of these items reflect policies of U.S. EPA: for instance, federal enforcement personnel may decide not to approve SEPs when the likelihood of a successful SEP is sufficiently uncertain, or where the costs to EPA of reviewing and overseeing the SEP proposal are too great. Also, EPA requires a complete description of SEPs, and the means for assessing whether a project delivers its promised environmental benefits. Maryland's SEP policy requires that SEPs must be defined with particularity as to deadlines, and the agreement must specify "objective quantifiable deliverables with deadlines and consequences," facilitating oversight and enforcement.

Several state SEP policies place a premium on rigorous screening of projects, as well as imposing conditions to improve the likelihood of project success. Connecticut's Department of Environmental Protection examines the "worst case" scenario in determining whether a SEP poses too many risks if "done poorly or … left uncompleted at any time during implementation." Maine also scrutinizes a violator's capacity to conduct a successful SEP, conditioning its regulatory approval upon evidence of technical and economic resources

needed for implementation. Maine may "require a letter of credit, escrow agreement, or third-party oversight as part of this demonstration." By outsourcing the oversight of SEPs to the University of Maine or another branch of state government, and by charging those oversight costs back to the violator, Maine increases the possibility of successful outcomes through the project management expertise and neutrality of the third party.

The California Water Quality Board ("CWQB") expands upon this theme, specifying additional requirements for SEPs that are to be implemented by third parties. The CWQB states that when a violator submits a SEP proposal, "it should include draft provisions (*i.e.,* details of the specific activities that will be conducted, and of the estimated budget for activity in the SEP) for a contract to be executed between the discharger(s) who will be funding the project and the entity performing the SEP if different from the discharger." CWQB retains the right to impose stipulated penalties, as the final order must include either implementation schedules or milestones, and "if any SEP milestone is not completed to the satisfaction of the [agency] by the date of that milestone, the previously suspended liability associated with that milestone shall be immediately due and payable to the State." The violator/discharger remains liable for paying any supplemental fine, regardless of the contract between the violator and its third party contractor. CWQB suggests that the violator/discharger include a performance bond or penalty clause in the contract with the implementer.

As with the other enhanced regulatory mechanisms specified above, regulators increase the likelihood of successful project completion through better screening, articulation of milestones, and the early detection of a failing project. The price of these mechanisms, however, is a negotiation encumbered by additional delay, cost and procedural requirements, possibly deterring violators from pursuing settlements with SEPs. Regulators, too, can find the costs of increased oversight and project screening to be difficult burdens in times of scarce personnel and budgetary resources. Moreover, the building up of increasingly intricate centralized procedures cuts against one of the motivating forces behind the use of SEPs, that is, the emphasis upon localized control of projects and the return of environmental benefits to communities affected by environmental degradation.

A contractual model

While few states expressly release violators from the threat of stipulated penalties in exchange for their use of approved third party implementers, the Hastings/ABA survey shows that a few states have implemented novel measures that can ease the burden of the process-heavy model discussed in the preceding section. Colorado, for instance, relies upon the services of the StEPP Foundation ("StEPP"), which chooses implementers and oversees projects to their conclusion on behalf of violators funding the SEP. While the violator remains liable for failed projects, StEPP's environmental expertise and project management experience help vouchsafe against that possibility. StEPP itself is prompted to succeed by the force of the state agency's power to judge it ineligible to receive future contracts from violators.

Texas exemplifies the most promising balance of third party implementation and reduction of liability, having revamped its SEP practices to meet violator and regulator concerns about SEP transaction costs. The Texas Commission on Environmental Quality ("TCEQ") steers violators to fund pre-approved SEPs with third party implementers rather than "custom" SEPs, which involve additional reporting and procedural requirements. TCEQ negotiates master agreements with nonprofit organizations that agree to receive and use SEP funds from violators solely for pre-approved SEPs. These agreements include many of the provisions noted in the previous section, including scrutiny of the implementer's ability to conduct a project effectively, as well as the use of milestones and reporting requirements.

These "master" agreements directly connect regulator to third party implementer, so the regulator may specify the full range of performance safeguards, as well as hold the implementer accountable for performance shortfalls. Moreover, the regulator has the additional leverage of being able to reward good performance with additional projects from other SEP settlements, as well as holding the threat of terminating the multi-project contract for underperformance in any specific project.

Eligible third party organizations must have Section 501(c)(3) status as nonprofit organizations or be governmental organizations; have the ability to receive, manage, and report to TCEQ on the use of SEP funds; and have a history of implementing and managing environmental enhancement projects. To assure that a project is of broad public benefit, proposed SEPs must "meet agency criteria, as determined by the SEP Panel, [and] will be submitted to the commissioners for approval on an annual basis" and will be subjected to public comment, as well. The third party implementer also obligates itself to segregate SEP funds and use them solely for approved projects, accounting and reporting requirements (of contributions, progress, environmental benefits, expenditures and SEP account balances), and financial auditing.

Significantly, the violator is not subject to stipulated penalties for the failures of the third party implementer; any recourse must be pursued by the agency under its agreement with the implementer. As the master agreement specifies: if the agency "determines that SEP monies have been spent in a manner that has not resulted in adequate and timely work performed or purchases made in accordance" with the master agreement, the agency

can demand payment of the remaining amount of contributions, as well as repayment of funds spent on unapproved activities. However, violators that directly contract with third party implementers do not receive "safe harbor" from stipulated penalties for the third parties' failures.

Other states, such as New Hampshire, permit donations to nonprofits as SEPs, but this is distinct from the Texas system, which directly funds pre-approved projects and waives further violator liability. Pennsylvania, like Texas, requires that the donation be dedicated to a specified project, and not merely to the general accounts of the non-profit organization. But not all states permit these kinds of SEPs: the Delaware statute specifically prohibits payment to charities or other entities as SEPs, and prohibits performance by third parties in part because the state would have no direct legal leverage over third parties in cases of underperformance.

Further thoughts

A state interested in removing some of the disincentives to the expansion of the use of SEPs might consider following the Colorado/Texas model. While building relationships and negotiating contracts with third party implementers carry up-front costs to regulators, these would be one-off events and would greatly smooth the path for violators interested in providing environmental benefits to affected communities. Moreover, regulators are better positioned to negotiate meaningful service contracts than violators, which may only be executing an environmentally beneficial project contract for the first and only time.

A bolder (and untested) solution would be a licensing procedure, under which potential implementers would be duly certified and post performance bonds. Contracts executed with an approved implementer would be deemed as compliance with the settlement agreement, together with the full measure of SEP expenditures set out in the settlement agreement. This tactic would resemble and extend the Texas initiative, as the regulator would take on the burden of screening implementers and negotiating the parameters for their being eligible to receive SEP funds.

In the alternative, the California Water Quality Board's recommendation of the use of performance bonds/penalty clauses in violator/implementer contracts could also provide a measure of assurance to violators concerned about the risk of further liability. Even if a project should fail *and* result in stipulated penalties, a carefully drawn up contract with the implementer could protect the violator from further outlays. Performance bonds are commonly used in the construction industry and guarantee that work be completed according to approved plans and specifications; their relevance to the SEP context is evident.

A possible criticism of all the proposals and practices mentioned is that they would apparently sanction failed projects. The rebuttal to this criticism would note that, at worst, the expenditure of the full measure of promised funds would achieve the punitive aims of environmental enforcement; the threat of further penalties for failures in good faith only serves to deter the use of SEPs. The threat of stipulated penalties remains as a bulwark against violators that would egregiously refuse to comply with their obligations in settlement agreements.

Conclusion

This note attempted to sketch out ways that states and violators could harness the capabilities of expert and community third party implementers, while still satisfying the concerns for punishment that lie behind the use of stipulated penalties provisions. The Texas example provides the best case for balancing the competing concerns of environmental benefit, low transaction costs, and a preservation of the deterrent effect of environmental laws. In this way, Texas's model streamlines the adoption of SEP provisions in settlement agreements and reinforces the core purpose of SEPs, returning environmental benefit to communities affected by environmental violations. What has not been seen in practice is a model that would limit the risk of stipulated penalties for innovative projects advancing technology that cannot be justified on business grounds or agency programmatic grounds.

Endnotes

1 Community based SEPs have been problematic for some violators, who are obliged to provide completion reports back to regulators; at least one violator has noted that community implementers often lack the ability to keep records and produce timely reports for the violator to send up to the regulator, in satisfaction of its settlement obligations.

The Possibility of SEP Legislations and the Lessons that the Fifty Laboratories of Democracy Offer[1]

By Nicholas Targ, Senior Counsel, Holland & Knight, LLP; Steven Bonorris, Associate Director for Research at the Center for State and Local Government Law at UC Hastings College of the Law; and Chelsea Holloway, Associate, Holland & Knight, LLP.

The time may be ripe for legislation formally authorizing the Environmental Protection Agency's (EPA's) allowance of Supplemental Environmental Projects ("SEPs") in enforcement settlements. The convergence of congressional interest, environmental groups bringing perceived deficiencies to the attention of members of Congress, and a recent Internal Revenue Service Ruling (IRS) decision has set the stage. If SEP legislation proceeds, lessons may be gleaned from the use of SEPs at the state level.

Background on SEPs

SEPs are environmentally beneficial projects that a company or other environmental defendant voluntarily promises to undertake, in consideration of which, EPA may mitigate the penalty imposed. EPA has encouraged the use of SEPs for more than a decade. This past fiscal year, the agency environmental defendants agreed to include SEPs valued at $78,000,000 in 220 administrative and federal court settlements, according to EPA statistics. With all but two states using SEPs as an enforcement settlement tool, SEPs have become an integrated part of the enforcement process.

SEPs are popular with community members, regulators and environmental advocates because they involve actions that go beyond what is required by law and provide an environmental and/or public health benefit. In addition to the SEP itself, the process of negotiating a SEP can help restore frayed relationships that can result from a violation. Of major importance to environmental defendants, SEPs can substantially mitigate penalties, based on the cost of the SEP. To preserve the deterrence effect of environmental laws, however, EPA's SEP policy establishes minimum penalties.

The IRS Ruling and Its Implications for SEPs

A May 2007 IRS directive, affirming a year-old IRS Technical Advice Memorandum, may spur federal SEP legislation.[2] Both the IRS directive and decision hold that the portion of SEP costs used to mitigate the initially calculated penalty is analogous to a penalty and hence not deductable or depreciable. Further, the IRS directive requires IRS examination of all SEPs greater than $1 million, to ensure compliance with the directive. While the IRS directive does not directly address EPA's SEP policy, questions are raised about the nature of SEPs.

The IRS decision involved a facility with emissions in excess of those allowed under the Clean Air Act (CAA). Instead of paying a civil penalty and bringing its existing systems into compliance, the taxpayer/defendant proposed to undertake a state-SEP variant (referred to as "Beneficial Environmental Project" or "BEP"). Specifically, it agreed to perform a major project to convert its equipment to a design that would reduce emissions well below standards required under the CAA. The resulting emissions-reduction credits would be shared equally between the state and the facility. The state agreed to the proposal and included it in an enforceable settlement agreement.

The IRS concluded that the cost of the BEP should not be deductible because "the purpose of the civil penalty, *i.e.*, the portion of the [BEP] imposed in the settlement of those potential penalties…was to punish Taxpayer and to deter future violations." The IRS reasoned that

> if the Taxpayer had settled its civil penalty by making a cash payment to [the State], that payment would be a nondeductible fine or penalty…. The result should not change because the Taxpayer settled its penalty by agreeing to incur the costs of performing a project to benefit the environment instead of incurring a direct cash payment.

The IRS directive and decision's characterization of SEPs as comparable to a penalty implicates the nature of SEPs. In the IRS view, environmental settlement agreements are comprised of penalties (punitive or deterrent, and not deducible), injunctive relief (compensatory or remedial, and deductible) and SEPs (comparable to penalties, and not deductible). EPA's SEP Policy defines a SEP as an environmentally beneficial action voluntarily undertaken by an environmental defendant. Utilizing its enforcement discretion, EPA may reduce the penalty assessed in consideration of the defendant's legally binding commitment to perform the SEP. Under this rubric, EPA does not compel the defendant to undertake the SEP, and the SEP is not considered a "penalty."

Continued on page 16

Federal appropriations law necessitates this construction and, as implemented by EPA, requires further that SEPs have a nexus to the violation (*e.g.*, a SEP addressing air quality issues will likely have a nexus to a violation of the CAA). Nexus may be established by a SEP addressing the same pollutant, or the health effects, caused the violation. In addition, nexus is more readily established if the SEP has a has a geographic proximity to the violation.

Were SEPs characterized as penalties, they would be an amount "due and owing to the United States," under the Miscellaneous Receipts Act and required to be deposited into the into the General Treasury. 31 U.S.C. §3302(b). Moreover, if SEPs were characterized as penalties, additional concerns would be raised under the Anti-Deficiency Act (31 U.S.C. §1341(a) (prohibiting agency expenditure in excess of Congressional appropriations)).

These concerns were raised in U.S. General Accounting Office (GAO) opinions in the early 1990's, and were, in part, the impetus behind EPA's issuance of its 1998 SEP Policy, establishing the present construction of SEPs.

The IRS directive and decision made clear that the IRS will not allow the deductibility of the portion of the SEP costs used to mitigate the initially calculated penalty. A legislative response may be necessary to clarify the nature and authority of SEPs.

Lessons from the 50-states

The SEP policy arena has been fast evolving at the state level. Many states are not bound by appropriation laws analogous to those at the federal-level, and eleven states have legislation specifically authorizing the use of SEPs or similar practices. Consequently, if federal legislation is contemplated, lessons can be drawn from the states as to the desirability and contours of SEP practices that are shaped solely by enforcement and other policy objectives.

A new, authoritative study, *Supplemental Environmental Projects: A Fifty State Survey with Model Practices*, prepared by the American Bar Association's Section of Individual Rights & Responsibilities and the UC Hastings College of the Law, with the cosponsorship of the ABA Section of Environment, Energy, and Natural Resources, and the ABA Section of State & Local Government Law, details federal and state SEP laws, policies, and practices. This report demonstrates how SEP policies can be designed to improve conditions in communities faced with environmental violations. It guides policy-makers through the options that are available in designing effective SEP policies. The report was also designed to provide practicing attorneys and community advocates with the state-specific information they need to make effective use of SEPs. The report is available for download at no cost on the UC Hastings website at http://www.uchastings.edu/site_files/plri/ABAHastingsSEPreport.pdf.

The study makes a number of key findings and recommendations germane to those considering revisions to SEP laws and policies. These findings and recommendations are supportive of EPA's SEP Policy, but recommends increased flexibility in some aspect. They are summarized as:

Finding: *SEPs are a common and accepted part of the enforcement and compliance assurance process.* The report shows that most states have followed the EPA example in adopting some kind of SEP law, policy or practice. Twenty-seven and the District of Columbia have instituted formal, published polices through legislation, regulations, or guidelines, up more than 50 percent from ten years ago, when the only other fifty-state SEP study was conducted. The study further shows that another twenty-one states rely on informal policies or unwritten SEP practices. Only two states, North Carolina and South Carolina, have rejected the use of SEPs.

Finding: *While some state SEP policies closely track EPA's, many states have SEP policies that afford greater flexibility.* This flexibility can reduce the transaction cost of negotiating a SEP and allow settling parties to tailor projects that they, communities, and others want. By way of example, some state laws and policies allow donations of funds to nongovernmental organizations for the purpose of undertaking specific projects (*e.g.*, purchase and maintenance of ecologically important lands).

Recommendations: The Report identifies several key model practices drawn from the experience of states that could be considered in federal SEP legislation or its implementation:

1. Nexus: *SEP practices should include a mandatory connection between a violation and the negotiated SEP.* This element can help ensure that affected communities themselves benefit from the SEPs. However, the nexus requirement need not be as stringent as EPA's. The report also endorsed the nexus requirement to limit the possibility that the SEP will depart from the agency's core environmental mission.

2. Penalty: *SEP policies should recapture a significant portion of the economic benefit of noncompliance.* The report observes that, "SEPs may dramatically reduce the amount of cash penalty paid, therefore, regulators must ensure that the use of SEPs in settlements does not weaken the deterrent effect of environmental laws."

3. Community input: *SEP policies should include a mechanism for community input, which can lead to SEPs tailored to local needs and potentially heightened participation and oversight in project implementation.* The report notes that community input may also bring increased transparency to the enforcement process.

4. Environmental justice: *SEP policies provide a platform for furthering environmental justice and fostering a new environmental enforcement model.* The fifty-state survey found that nine states include environmental

justice as a factor in their SEP policies. It further concluded that, "[i]n view of the strong correlation between environmental violations and minority and/or low-income populations, SEP policies that do not require a relation back to the community miss a valuable opportunity to redress longstanding environmental inequities." Therefore, a geographic nexus is desirable.

Roadmap for federal legislation?

Whether the time is appropriate for SEP legislation is a matter left for Congress. The opportunity for clarification of the law and response to the lessons of the 50-states is, however, available. In expressly establishing EPA's authority to approve SEPs, Congress could pave the way for a revamped SEP policy that responds flexibly to business, environmental, and social justice priorities.

Endnotes

1 Reprinted from Trends July/August 2007

2 IRS Industry Director Directive on Govt. Settlements Directive #1 LMSB-04-0507-042 (May 30, 2007) (IRS directive): IRS Tech Adv. Mem. 2006-29030 (Mar. 31, 2006) (IRS decision).

Recent Revisions... *Continued from page 3*

effort DEQ would expend in reviewing and overseeing a SEP. The new directive allows smaller SEPs if handled by third parties and allows third parties to aggregate smaller SEPs into larger projects;

- Will allow some new types of costs to be used in valuing the SEP which makes the possible penalty reduction larger and more attractive to respondents. The proposed directive would allow inclusion of the costs of preparing the SEP proposal, some wages and overhead, and other costs of organizing and executing the SEP; and
- Would allow a respondent to conclude its enforcement action at the time it pays its SEP monies to a third party so long as the third party is required to complete the SEP and provide a Final Report to DEQ. Although some legal and procedural details of this process must still be evaluated, once that is done, violators may be able to shift financial liability for the work to the third party who accepted the money and is performing the work.[1]

The SEP program is designed to reverse noncompliance with environmental laws to create "beyond-compliance" benefits which could not have been attained through existing legal requirements. As other authors describe in this newsletter, SEPs can and should be used to encourage projects that benefit the public or environment at large, are innovative, address environmental justice concerns, incorporate community input, or have multimedia benefits. With the changes in the revised policy, the Department of Environmental Quality expects to see more and better SEPs that benefit the community and help the violator return to good community standing.

Endnotes

1 *See* Bonorris elsewhere in this issue for a thorough discussion of the issues involving third party SEPs.

Pacific Shrimp Co.'s... *Continued from page 6*

costs of each of the components, schedules of completion, a description of benefits and results, and how the benefits and results would be measured or assessed. The information included a fuller description of the Natural Resource crew member program and the program's evaluation process. In the end, the agency approved the three components, and the Council was able to represent all three of its goals in the process.

The SEP negotiation and execution process began in September 2005 and concluded around mid-July 2006. The funds were expended on their designated uses in mid-2007, due to the Council's fiscal schedule and the various other grants already funding the Council's education program, water quality monitoring, and the estuary restoration efforts. The experience proved to be a positive experience all around. The plant's settlement money went directly towards improving the Yaquina watershed, the SEP presented a new funding opportunity for the Council which funds the large share of its efforts from grants and donations, and the DEQ accomplished the purpose of the SEP program.

Endnotes

1 Ms. Henkels was previously in private practice in Newport, OR where she initiated and was the main negotiator of this SEP. The views of the author do not represent those of the Confederated Tribes of the Umatilla Indian Reservation, the MidCoast Watersheds Council, nor Pacific Shrimp Co.

The Benefits... *Continued from page 8*

orative SEPs where the circumstances are appropriate. Please contact the author at jlmarsh@pdx.edu if you would like to learn more or have a potential SEP that might produce additional benefits from a more collaborative approach.

Endnotes

1 Reprinted from ECOStates, Summer 2007

2 Environmental Enforcement Solutions: How Collaborative SEPs Enhance Community Benefits (M. Kirk and L.Marsh). http://www.policyconsensus.org/publications/reports/index.html.

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