NACAA
national association of clean air agencies

The National Association of Clean Air Agencies' Recommendations for the Distribution of Funds for Environmental Mitigation and Supplemental Environmental Projects Related to Alleged Volkswagen Violations

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Background

On September 18, 2015, the U.S. Environmental Protection Agency[1] (EPA) and the California Air Resources Board[2] (CARB) initiated enforcement actions against automakers Volkswagen AG, Audi AG (a subsidiary of Volkswagen) and Volkswagen Group of America (collectively referred to as VW) for allegedly equipping approximately 500,000 light-duty diesel vehicles with 2.0-liter (2.0L) engines in the U.S., from model years (MY) 2009 through 2015, with software intended to impede, or "defeat," emission control devices during normal driving situations. These devices are designed to sense when a vehicle is undergoing the Federal Test Procedure and, at that time, turn on full emission controls. The use of such "defeat devices" is illegal under the Clean Air Act.

At that time, CARB recounted in its compliance letter to VW that the state and EPA were alerted to the alleged violations in 2014 by the International Council for Clean Transportation Technology and West Virginia University, which, through their test program, discovered elevated levels of nitrogen oxides (NO_x) under real-world driving conditions. CARB detailed in its letter the events that had taken place over the course of many months since the discovery of elevated emissions – discussions with VW, testing, a recall of the software by VW that affected nearly 500,000 vehicles, more testing and a determination by CARB that the recall had failed to remediate the increased real-world driving emissions. CARB then stated in its compliance letter that after all these efforts,

> During a meeting on September 3, 2015, VW admitted to CARB and EPA staff that these vehicles were designed and manufactured with a defeat device to bypass, defeat, or render inoperative elements of the vehicles' emission control system. This defeat device was neither described nor justified in the certification applications submitted to EPA and CARB. Therefore, each vehicle so equipped would not be covered by a valid federal Certificate of Conformity or CARB Executive Order and would be in violation of federal and state law.

[1] U.S. EPA Notice of Violation issued to VW related to 2.0L diesel vehicles (September 18, 2015), http://4cleanair.org/sites/default/files/resources/EPA_NOV_to_VW-09.18.15.pdf.
[2] CARB In-Use Compliance Letter issued to VW related to 2.0L diesel vehicles (September 18, 2015), http://4cleanair.org/sites/default/files/resources/CARB_InUseComplianceLetter_to_VW-09.18.15.pdf.

According to researchers at the Massachusetts Institute of Technology, as of September 28, 2015, excess NO_x emissions that had occurred to date from the alleged illegal use of defeat devices on these 2.0L diesel vehicles were estimated to be about 46,000 tons.

On November 2, 2015, EPA[3] and CARB[4] initiated additional enforcement actions against VW (this time also including Porsche, a subsidiary of VW) for allegedly equipping diesel vehicles with 3.0-liter (3.0L) engines from MYs 2014 through 2016 with illegal defeat devices. On November 20, 2015, CARB announced that during a meeting on November 19, 2015, VW admitted to EPA and CARB that the company had, in fact, equipped *all* of its 3.0L U.S. diesel vehicles with illegal defeat devices since MY 2009 (through MY 2016). EPA has indicated that this amounts to approximately 80,000 vehicles nationwide. CARB issued a third in-use compliance letter to VW on November 25, 2015 for all 3.0L diesels from MYs 2009 through 2016.[5]

On January 4, 2016, the U.S. Department of Justice, on behalf of EPA, filed a civil complaint in the U.S. District Court for the Eastern District of Michigan against Volkswagen AG and its subsidiaries, including Audi and Porsche, alleging the use of illegal defeat devices on approximately 500,000 2.0L and 80,000 3.0L diesel-fueled vehicles beginning with MY 2009.[6]

In addition, a number of states have filed suit against VW for violations of state air quality laws and many states have initiated legal actions against VW for violation of consumer protection laws.

As state and local air pollution control agencies continue the work of reducing emissions that pose risks to our citizens, it is troubling that, allegedly, VW purposely, and over a sustained period of time, violated federal and state laws and regulations not only frustrating our clean air efforts but, moreover, jeopardizing public health. The excess NO_x emissions that have resulted from VW's alleged violations – emissions that EPA says are as high as 40 times the federal standard for 2.0L diesel vehicles and nine times the federal standard for 3.0L diesel vehicles – contribute to ozone (smog), particle pollution, haze, toxic air pollution, global warming, acid rain and the eutrophication of water bodies. NO_x emissions are linked with a large number of adverse impacts on the respiratory system, as well as with the many ill effects associated with all of the pollution problems to which they contribute, including premature death. Each day the defeat-device-equipped vehicles remain in use excess emissions continue to accrue.

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[3] U.S. EPA Notice of Violation issued to VW related to 3.0L diesel vehicles (November 2, 2015), http://4cleanair.org/sites/default/files/resources/EPA_NOV_to_VW-11.02.15.pdf.

[4] CARB In-Use Compliance Letter issued to VW related to 3.0L diesel vehicles (November 2, 2015), http://4cleanair.org/sites/default/files/resources/CARB-InUseComplianceLetter_to_VW-11.02.15_1.pdf.

[5] CARB second In-Use Compliance Letter issued to VW related to 3.0L diesel vehicles (November 26, 2015), http://4cleanair.org/sites/default/files/resources/CARB-InUseComplianceLetter_to_VW-11.25.15.pdf.

[6] U.S. EPA Civil Complaint against VW filed in the U.S. District Court for the Eastern District of Michigan (January 4, 2016), http://4cleanair.org/sites/default/files/resources/EPA_Civil_Complaint_VW-01.04.16.pdf.

Financial Payments or Penalties for Mitigation Efforts and Environmental Projects

Since the VW case is ongoing at the federal level and with individual states, it is as yet unknown how it will be resolved. However, there are multiple possible outcomes, including a full trial or a settlement that is negotiated among the parties. Regardless of which direction the legal process takes to resolve the matter, the government may require certain actions from VW as part of injunctive relief (i.e., obligations to ensure that a violator is brought into and remains in compliance). This could include, for example, recalling and repairing the vehicles and/or offering to buy them back from consumers. Additionally, VW may be required to take measures that address the excess emissions that have already occurred, as well as emissions that may continue in the future if the recall/buyback options do not fully address the problem.

Some of the measures that the government may require under injunctive relief in this case may call for significant expenditures on VW's part. These could include:

- *Mitigation of Environmental Harm* – The government may seek mitigation of the environmental harm the alleged violations caused. According to EPA, "[m]itigation is injunctive relief sought by the government to remedy, reduce or offset past (and in some cases ongoing) harm caused by the alleged violations in a particular case."[7] In order to address the excess emissions from this matter (both past and future), VW could be required to purchase offsets, for example, or provide resources for other programs to reduce air pollution.

- *Civil Penalties* – According to EPA, "civil penalties are monetary assessments paid by a person or regulated entity due to a violation or noncompliance. Penalties act as an incentive for coming into compliance and staying in compliance with the environmental statutes and regulations. Penalties are designed to recover the economic benefit of noncompliance and to compensate for the seriousness of the violation." By their nature, civil penalties are intended to serve as a deterrent to future violations.[8]

- *Supplemental Environmental Projects (SEPs)* – In lieu of some of the civil penalties, VW may be permitted to set aside funds for SEPs. EPA describes a SEP as "an environmentally beneficial project or activity that is not required by law, but that a defendant agrees to undertake as part of the settlement of an enforcement action. SEPs are projects or activities that go beyond what could legally be required in order for the defendant to return to compliance, and secure

[7] U.S. EPA Memorandum, *Securing Mitigation as Injunctive Relief in Certain Civil Enforcement Settlements – 2nd Edition* (November 14, 2014), https://www.epa.gov/sites/production/files/2013-10/documents/2ndeditionsecuringmitigationmemo.pdf.

[8] U.S. EPA Webpage, *Enforcement Basic Information,* https://www.epa.gov/enforcement/enforcement-basic-information.

environmental and/or public health benefits in addition to those achieved by compliance with applicable laws."[9]

Under the Clean Air Act (Sections 203(a)(1), 203(a)(3)(A), 203(a)(3)B) and 203(a)(2)), VW could be held liable for injunctive relief and civil penalties of 1) up to $37,500 per subject vehicle due to the lack of a valid Certificate of Conformity, 2) up to $37,500 per subject vehicle because vehicle devices or elements of design needed for compliance were removed or rendered inoperative, 3) up to $3,750 per "defeat device" per subject vehicle and 4) up to $3,750 per day of violation for failure to make test data or other information available under statutory information collection requirements.

Under any settlement, VW should be required to provide resources sufficient to not only offset, but also achieve reductions to surpass, all excess emissions that have already occurred and that will occur in the future as a result of the alleged violations.

Role of State and Local Air Pollution Control Agencies

Under Section 101(a)(3) of the Clean Air Act, state and local air pollution control agencies are granted the primary responsibility for preventing and controlling air pollution. Among other things, they are required to develop plans for meeting the National Ambient Air Quality Standards for NO_2 (the indicator for the larger group of NO_x), as well as for ozone and particulate matter, both of which can be created as a result of NO_x emissions.

State and local air agencies are expending tremendous capital – financial and political – to identify and implement effective air pollution control strategies, particularly for NO_x. Now state and local air pollution control agencies will share in the responsibility of mitigating the environmental damage and public health harm caused by the violating VW vehicles, including the excess emissions that have already occurred and any additional future releases from vehicles that are not adequately repaired or removed from service.

In addition, state and local air pollution control agencies have extensive experience implementing a host of sophisticated and comprehensive air quality programs, as well as special projects designed to address specific issues. These efforts focus on all manner of emission sources and activities and range from, among many others, regulating power plants to retrofitting trucks and buses with diesel control devices to replacing older wood-burning devices.

Accordingly, state and local air pollution control agencies should be provided with significant resources from funds earmarked for mitigation activities and SEPs under the legal settlement of the VW case, to be used to advance clean air efforts. The paramount goal of the resources provided to state and local air agencies would be to fund activities to ensure that every ounce of excess emissions – past, present and

[9] U.S. EPA Memorandum, *Supplemental Environmental Projects Policy 2015 Update*, (March 10, 2015), https://www.epa.gov/sites/production/files/2015-04/documents/sepupdatedpolicy15.pdf.

future – from VW's alleged violations is mitigated. To achieve this goal, each state and local agency should be able to retain a portion of its allotted funds to administer and implement its program. Additionally, the receipt of funds by a state or local agency under this program should not result in decreases in other funds provided to the agency.

Towards this end, the National Association of Clean Air Agencies (NACAA) recommends the following approach for the distribution of such funds to, and use of such funds by, state and local air pollution control agencies.

Criteria for Distribution of Funds from Mitigation Efforts or SEPs to State and Local Air Agencies

There are various approaches for distributing mitigation and/or SEP funds resulting from the VW case that are earmarked for state and local air pollution control agencies.[10] Under NACAA's recommended approach, each state or local air agency would receive funding in proportion to the extent of the problem the VW case caused in its jurisdiction. Among the criteria that could be considered when disseminating funds under the VW settlement are the following:

- the number of affected VW vehicles in the jurisdiction;
- the number of excess tons of NO_x;
- the size of the affected population; or
- some combination of the above.

In any case, every state and local agency that wishes to participate in this program would receive some minimum level of funding in recognition of the interstate transport of excess emissions and the operation of affected vehicles in jurisdictions other than the ones in which they were sold and/or are registered.

Further, it is imperative that any mitigation or SEP funds distributed to a state or local air agency not be comingled with other state or local funds.

Structure of State and Local Programs Using VW-Related Funds

NACAA's recommended approach is similar in structure to, but more expansive than, the final consent decree resolving the Deepwater Horizon BP spill in the Gulf of Mexico in 2010.[11] Under the NACAA model, a state or local air agency would have substantial flexibility in how it structures its program. Accordingly, an agency may use

[10] These recommendations pertain only to funds negotiated by the federal government and do not apply to settlements, penalties, SEPs or mitigation funds that individual state or local governments may negotiate as part of their own legal actions against VW.

[11] Consent Decree Among Defendant BP Exploration & Production Inc. ("BPXP"), the United States of America, and the States of Alabama, Florida, Louisiana, Mississippi, and Texas (April 4, 2016), https://www.justice.gov/enrd/file/838066/download. In addition to civil penalties, BP will be required to pay $8.1 billion in natural resources damages related to the spill. The funds will be allocated among five restoration goals and restoration types and distributed among the five states along the Gulf of Mexico (with each state receiving a different amount based on the restoration goals and types).

all the funds it receives on specific projects consistent with the criteria identified below. The agency may also choose to pattern its program similar to the highly successful Diesel Emission Reduction Act (DERA) program,[12] but without some of the inherent limitations, using some (or all) of its funds to develop a competitive grant program under which it solicits funding requests for and selects and awards grants to projects to mitigate adverse health and environmental impacts in its jurisdiction.

Criteria for Funding Projects

There are many types of projects and programs that would be beneficial to public health and the environment. Ideally, a project supported by VW funds should address as much as possible the same pollutants, types of sources and geographic areas that were involved in the violations while garnering emission reductions that are significantly greater than the excess emissions that occurred and will continue to occur from the VW vehicles.

While priority could be given to projects that address these elements, there may be other ways of accomplishing similar goals. Therefore, the criteria for determining appropriate activities must allow for broader options and greater creativity. Additionally, state and local programs should be held accountable to ensure that the funds are used for their intended goals. For instance, the program could require a commitment from state and local recipients to review and publicize the environmental results of each grant on a regular basis (e.g., every two years) to provide assurance to the public that the funds are achieving meaningful results.

The following are important criteria to consider when approving projects for funding:

- A project should generate emission reductions.
- Emission reductions should be quantifiable and verifiable.
- Emission reductions should occur in the same geographic area in which the excess emissions occurred.
- Priority should be given to projects that provide near-term emission reductions.
- While projects should focus on NO_x reductions, priority should be given to efforts that also provide co-benefits (e.g., reduction of diesel particulate matter).
- While transportation sector projects are preferable, stationary source projects that provide significant reductions should also be considered (e.g., credits for reductions from power plants).

[12] U.S. EPA Webpage, *Learn About Clean Diesel,* https://www.epa.gov/cleandiesel/learn-about-clean-diesel.

- Priority should be given to projects that are highly cost-effective, with the clear understanding that cost effectiveness will vary from area to area.

- Buyback or accelerated turnover programs must ensure that the violating vehicles are taken out of circulation.

While it is unlikely that any recommended projects will have all of the characteristics included in the list above, projects that meet multiple criteria should be given a higher priority when activities to be funded with resources resulting from the VW matter are selected.

Sample Projects

There are many specific kinds of projects that may be appropriate to fund under the criteria listed above. Following are just some of the options that may be considered, among others:

- Replacement or retrofit of older engines with cleaner technology (e.g., retirement of older diesels or rebuild of heavy-duty engines)

- Electric- or hydrogen-vehicle infrastructure development (e.g., charging stations)

- Zero Emission Vehicle and electric vehicle projects, including those that accelerate purchase for commercial applications

- Funds for equipment and operation of mobile source emissions testing programs

- Truck stop electrification

- Investment in the development of advanced vehicle technology

- Other projects that comport with the criteria listed above