

Science and Technology Committee Newsletter

Vol. 3, No. 2

August 2003

MESSAGE FROM THE CHAIR

Terry F. Quill
Duane Morris LLP

On behalf of the Special Committee on Science and Technology leadership, I am pleased to present our final Committee Newsletter for 2002-2003. We have had a very successful year and look forward to the new year, which starts in August. You will note that the Newsletter now is available only in electronic format – the Section has moved away from printed Committee Newsletters. We hope you are finding the electronic publication convenient.

Of note, beginning in September 2003, we will no longer a “Special” environmental committee. We will become a regular committee and will be designated as a “cross-practice” committee serving members practicing in the energy and resources areas as well as the environmental area. We believe that this new committee status is a recognition that science underlies environment, energy and resources law, and that our committee provides utility to all three aspects of the Section. We will make a renewed effort to address cutting-edge science and technology issues that are important in the practice of energy and resource law, as well as environmental law.

We are busy planning our activities for the new ABA year. We would like to build upon the successes our Committee has had this past year. In that regard, we need your input to ensure that we continue to serve the interests of our Committee members. We have identified a number of substantive issues for the new year that we hope to address through conferences, teleconferences or our newsletter. Those issues include toxicogenomics, science and technology trends affecting litigation and regulatory practices, EPA’s new cancer assessment guidelines, biomonitoring, bias in scientific peer review, EPA’s implementation of an endocrine disruptor screening program, and modeling cumulative risks and assessing mixture toxicity. We welcome additional ideas.

With a new ABA year upon us, now is a good time to become more involved in the Committee (actually, there has never been a bad time to become involved). We will be successful only to the extent you get involved. If you are not yet a member, please join us. If you wish to become more active in our Committee or just want to share your ideas, please give us a call. We will list the new Committee chairs and vice-chairs in our next Newsletter. Also, please visit our Committee’s Web page at <http://www.abanet.org/environ/committees/sciencetech/home.html>.

**Science and Technology
Committee Newsletter
Vol. 3, No. 2, August 2003
Elliot Eder and Sarah Brozena, Editors**

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This newsletter is a publication of the ABA Section of Environment, Energy, and Resources, and reports on the activities of the committee. All persons interested in joining the Section or one of its committees should contact the Section of Environment, Energy, and Resources, American Bar Association, 750 N. Lake Shore Drive, Chicago, IL 60611.



In closing, I would like to repeat our theme for the past year: this is your Committee – please participate. The Committee leadership will continue to do what it can to respond to your information needs, provide a forum for you to share your expertise in the area of science and technology, and accommodate your desire to become more involved in the Committee. We look forward to working with you.

The 2002-03 Committee leadership is delighted to have had the opportunity to assist and work with you on matters involving science and technology in the practice of law. Indeed, those matters form the basis of our practices and we have appreciated the opportunity to share our expertise and learn from you. We have found our work with the Committee fun and professionally enriching.

Again, it has been a pleasure to serve you this past year. I hope to see you at the ABA Annual Meeting in San Francisco or at the 11th Section Fall Meeting in Washington D.C. (October 8-12). Please enjoy your Newsletter.

EDITOR'S INTRODUCTION

**Elliot Eder
Eder, LLC**

With this edition, your Science and Technology Committee Newsletter concludes its year under the ABA calendar. In this issue, we focus on several policy, regulatory and legislative developments, as opposed to the litigation and security themes that prior Newsletters have covered. Our three authors cover interesting ground:

Sunil Garg discusses implications of the Sarbanes-Oxley legislation, with a focus on the methodologies used when statements are made regarding contingent environmental liabilities. In addition, his discussion is

informed by expert testimony issues that may have special relevance in light of factors announced by the Supreme Court in the *Daubert* and *Kumho Tire* cases.

William Vincent evaluates “The Law of Unintended Consequences” that he finds operative in environmental aspects of mass transit projects. Bill offers suggestions for counsel, particularly given the impact of the New Starts Program in recent transportation legislation, as well as NEPA and the environmental impact statement process.

In “A Tale of Two Sites,” Michael Hill compares the fate of two New England cleanup sites, one pursued under a fixed-price insurance umbrella, and the other largely remaining to be resolved. In the process, Mike raises policy concerns that may merit attention at SEC and EPA, particularly in light of the Sarbanes-Oxley legislation and Congressional objectives announced for the Superfund program.

Sarah Brozena and I have endeavored to bring you interesting perspectives in Newsletters organized around various themes throughout the year. Plans for upcoming Newsletters should make for an interesting read, and we hope you will continue to offer your input regarding articles and themes. Meanwhile, best wishes for the summer.

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**ENVIRONMENTAL LAWYERING AND
VALUATION OF CONTINGENT
ENVIRONMENTAL OBLIGATIONS AFTER
THE SARBANES-OXLEY ACT: THE NEED
FOR A “SCIENTIFIC” APPROACH**

Sunil K. Garg, Ph.D., Esq.
The EcoShelf Group Inc

Introduction

There is little doubt that the passage of Sarbanes-Oxley Act of 2002, Pub. L. 107-204, 116 Stat.745 (2002) (Sarbanes-Oxley or the Act) had a direct effect on the “standard of professional conduct” and the judgment in-house and retained counsel must exercise when reviewing, accepting and reporting estimates of contingent environmental obligations in documents filed with the Securities and Exchange Commission (SEC or the Commission). The significance of the effect, and what the environmental legal, accounting, technical and engineering communities must do to deal with attendant changes are, however, in flux at this time. This article raises some issues that affect the reporting of contingent environmental obligations under the Act, and it proposes potential approaches to resolve them.

Principal Requirements of Sarbanes-Oxley Act that Affect Environmental Reporting

The Act requires the SEC to complete a number of regulatory actions in a rather short period of time. These actions have a potential impact on the current practices used in developing and reporting known and contingent environmental obligations in SEC filings. The principal mandates, for the purpose of this note, are briefly summarized below.

Section 401(a) of the Act requires the issuance of rules to ensure the periodic disclosure of

“all material off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships of the issuer with unconsolidated entities or other persons, that may have a material current or future effect on the financial condition, results of operations, liquidity, capital expenditures, capital resources, or significant components of revenues or expenses.”

Section 307 of the Act (entitled “Rules of Professional Responsibility for Attorneys”) directs the SEC to:

“issue rules, in the public interest and for the protection of investors for the professional conduct of attorneys appearing and practicing before the [SEC] in any way in the representation of issuers, including a rule – (1) requiring an attorney to report evidence of a material violation of securities laws or breach of fiduciary duty or similar violation by the company or any agent thereof to the chief legal counsel or the chief executive officer of the company (or the equivalent thereof);....”

Sections 302 and 906 of the Act direct all CEOs and CFOs to file two separate certifications with their company’s periodic SEC reports, certifying, *inter alia*, that

“the signing officers – (A) are responsible for establishing and maintaining internal controls; (B) have designed such internal controls to ensure that material information relating to the issuer ... is made known to such officers by others within those entities, particularly during the period in which the periodic reports are being prepared; (C) have evaluated the effectiveness of the issuer’s internal controls as of a date within 90 days prior to the [periodic] report; and (D) have presented in the report their conclusions about the effectiveness of their internal

controls based on their evaluation as of that date....”

Recently, SEC published a final rule required by Section 401(a), see SEC Release No. 33-8182 (Jan. 28, 2003), concerning disclosure of off-balance sheet arrangements and contractual obligations. The rule is silent on standards for disclosure of environmental contingencies. A coalition of charitable foundations and “socially responsible” investment funds, however, recently has submitted a petition for rulemaking urging SEC to adopt standards for estimating and disclosing environmental costs and liabilities. It is perhaps a matter of time before SEC addresses this issue.

SEC Release No. 33-8185: Implementation of Standards of Professional Conduct for Attorneys

SEC recently also finalized the rule required under Section 307 for the implementation of standards of professional conduct for attorneys who appear and practice before the Commission, see SEC Release No. 33-8185 (Jan. 29, 2003), 68 Fed. Reg. 6296 (Feb. 6, 2003) (to be codified at 17 C.F.R. Part 205) (Professional Conduct Rule). This rule, which is effective on Aug. 5, 2003, should be of particular interest to environmental attorneys, and technical and engineering experts and cost estimation professionals who advise them.

Attorneys who “appear and practice” before the Commission are subject to sanctions and discipline for violations of the Professional Conduct Rules, 17 C.F.R. Sec. 205.6. Sanctions include civil penalties and administrative disciplinary proceedings that may lead to censure and denial of the privilege of appearing or practicing before the Commission. 17 C.F.R. Sec. 205.6 (a) and (b). The only “safe harbor” seems to be a good faith attempt to comply with the Rule, see 17 CFR Sec. 205.6(c). However, the preamble to

the final adoption of the Rule indicates that this “safe harbor” is available only in limited circumstances since 17 CFR Sec. 205.6(c) “has been drafted to apply only to an attorney’s liability for violating inconsistent standards of a state or other U.S. jurisdiction. Thus, it is not available where the state or other jurisdiction imposes additional requirements on the attorney that are consistent with the Commission’s rules.” 68 Fed. Reg. at 6314.

The Rule, at 17 C.F.R. Sec. 205.1, “sets forth the minimum standards of professional conduct for attorneys *appearing and practicing* before the Commission” (emphasis added) and “supplement applicable standards of any jurisdiction where an attorney is admitted or practices.” In the event of a conflict between the standards of SEC and of a state or other U.S. jurisdiction where an attorney is admitted or practices and SEC, SEC Professional Conduct Rules govern. Accordingly, all attorneys appearing and practicing before the SEC are subject to discipline under 17 C.F.R. Part 205.

The all-important term *appearing and practicing* before the Commission is broadly defined at 17 C.F.R. Sec. 205. 2(a) to include:

(iii) Providing advice in respect of the United States securities laws or the Commission rules or regulations thereunder regarding any document that the attorney has notice will be filed with or submitted to the commission, or incorporated into any document that will be filed with or submitted to, the Commission, including the provision of such advice in the context of preparing, or participating in the preparation of, any such document, or

(iv) Advising an issuer as to whether information or a statement, opinion, or other writing is required under the United States securities laws or the Commission

rules or regulations thereunder to be filed with or submitted to, or incorporated into any document that will be filed with or submitted to, the Commission....

The Commission clarified in the preamble accompanying adoption of the Professional Conduct Rules that “attorneys who advise that, under the federal securities laws, a particular document need not be incorporated into a filing, registration statement or other submission to the Commission will be covered by the revised definition. In addition, an attorney must have notice that a document he or she is preparing or assisting in preparing will be submitted to the Commission to be deemed to be ‘appearing and practicing’ under the revised definition.” See 68 Fed. Reg. at 6298.

Reporting of environmental contingencies is required under various regulations adopted by the Commission; see particularly Regulation S-K, 17 C.F.R. Part 229, as clarified by SAB 92 and other guidance from the Commission. Accordingly, attorneys who participate in the preparation of statements of environmental contingencies for annual reports (Form 10-K), quarterly reports (Form 10-Q), and other required reports, such as Form 8-K, are “appearing and practicing” before the Commission, whether or not such attorneys consider themselves securities lawyers. Environmental attorneys who evaluate and provide advice on whether and what to report concerning the nature and extent of the contingent environmental obligations of their clients are now “appearing and practicing” in front of SEC, and have the affirmative duty to report evidence of a “material violation” to senior management, see Sec. 307 of the Act and 17 C.F.R. Sec. 205.3.

The definition of “material violation” includes a “material breach of fiduciary duty” under U.S. or state law. 17 C.F.R. Sec. 205.2(i). The Commission has stated that the term

“material” has a “well-established meaning under federal securities laws and the Commission intends that same meaning to apply here (footnote with citations omitted).” 68 Fed. Reg. at 6303. The omitted footnote refers to *Basic, Inc. v. Levinson*, 485 U.S. 224, 231-36 (1988) and *TSC Indus. v. Northway, Inc.*, 426 U.S. 438 (1976), which adopt the standard that an omitted fact is material if there is substantial likelihood that its disclosure would have been considered significant by a reasonable investor.

Issues for Environmental Lawyers Raised by These Requirements

SEC recently released a report entitled “Summary by the Division of Corporate Finance of Significant Issues Addressed in the Review of the Periodic Reports of the Fortune 500 Companies” (Review). The Review, SEC periodic assessment of Form 10-K filings by Fortune 500 companies, is dated Feb. 27, 2003 and is available at www.sec.gov/divisions/corpfm/fortune500rep.htm. The Review includes

“environmental liabilities” among the areas that “could have been made more transparent as a result of a more thoughtful discussions of assumptions and estimates. We found that we asked many companies to enhance their disclosure of critical accounting policies in one or more of the[se] areas. . . .”

The Review further notes:

In these comments, we pointed the companies to the guidance in SFAS 5, FIN 14, SOP 96-1 and SAB 92, which generally provide that companies with environmental and product liabilities must disclose:

- The nature of a loss contingency;
- The amount accrued;
- An estimate of the range of

- reasonably possible loss;
- Significant assumptions underlying the accrual; and
- The cost of litigation.

In addition to finding that many companies did not provide adequate disclosure relating to those items, we also found that companies could improve their disclosures required by SAB 92. SAB 92 provides interpretation of SFAS 5, but also includes additional specific disclosure requirements. We urged companies with material contingent liabilities to carefully review their disclosures and ensure that they include all required information. We also urged companies to provide in their MD&A a meaningful analysis as to why the amounts charged each period were recorded and how the amounts were determined.

The current environmental loss contingency reporting practice basically relies on FASB SFAS 5, as interpreted in FASB FIN 14. Both were adopted well before any significant developments in environmental laws as we know them today, and then only to account for contingent liabilities in general. Although there have been subsequent clarifications in SEC SAB 92 and AICPA SOP 96-1, among others, these “standards” have engendered limited due diligence as to the specific cost estimates on the part of the reporting lawyer(s) and technical professionals. Moreover, these reporting “standards” deal primarily with the mechanics of what to report and when to recognize a particular loss contingency. They do not deal with how the underlying cost estimates or estimate ranges, which are the subject of the report, are obtained.

The standard under Sarbanes-Oxley, due to the Professional Conduct Rule, is more rigorous than what has been the practice in the past. It is a reasonable interpretation of the Act that environmental reporting counsel, as an initial matter, need to review all known

and contingent environmental obligations of a company's, not simply those for which a regulatory action or litigation has commenced. The test for "materiality" can then be applied more meaningfully in deciding "up-the-ladder" reporting obligations of the attorney(s). This is a particular concern in light of the rise of the "socially conscious" investor in recent years. There are reasonable investors who consider a company environmental performance a material factor in deciding whether or not to invest, or to maintain the investment. See, e.g., the petition for rulemaking filed by the Rose Foundation for Communities and the Environment with the SEC, SEC File # 4-463 (Sept. 20, 2002).

Significance of Sarbanes-Oxley for In-House or Outside Environmental Counsel

These developments create enhanced obligations for the lawyer, usually an environmental lawyer, who reviews environmental cost estimates and makes recommendations for reporting environmental contingencies in documents filed with the Commission. Due to the "up-the-ladder" reporting character of the Rule, the initial burden of determining what is or is not "material" will fall on the reporting lawyer. The issue is: "material" with respect to what aggregate environmental obligations, or the aggregate financial position of the company? Environmental lawyers generally are not privy to the company aggregate financial status when a decision about the materiality of a specific environmental cost estimate must be made. In such a case, determination of what is material or not must be made in the context of the aggregate environmental obligations, whether contingent or not, for reporting "up-the-ladder" so that the CFO/CEO can decide how to treat the environmental attorney report in documents submitted by the company to the Commission.

The certification requirement for CFOs and

CEOs, contained in Sections 302 and 906 of the Act, is also of critical importance to the environmental reporting lawyer. The CFO/CEO must now certify, on a routine basis, that adequate internal controls exist in their company to allow surfacing of material information concerning contingent obligations, including environmental obligations, to them. Such internal controls would encompass the activities of the environmental lawyers and other technical professionals involved in the process of managing environmental responsibilities and reporting on the obligations and liabilities of the company. In preparing their individual certifications, CFOs and CEOs would be justified in relying on certifications from the law department, the chief environmental counsel and the chief environment, health and safety officer that an adequate internal control system exists.

Environmental lawyers have relied on the environmental engineers and consultants to develop estimates of costs for potential, and contingent, environmental liabilities. These lawyers seldom, if ever, independently verify either the methodology by which the estimates are obtained or whether these methodologies are reasonable in the context in which they are applied. Engineering cost estimating techniques lend themselves more readily to situations where an engineering solution can be designed based on an identifiable engineering process. This is so because an engineering design of the equipment needed to accomplish the desired result can be developed, and a cost for the project, including the necessary and inevitable contingencies, can reasonably be determined and applied.

Due to the inherent uncertainty that such estimates involve, these techniques generally are less useful in the important area involving remediation of contaminated sites such as

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New from ABA Publishing and The Section of Environment, Energy, and Resources

Issues of Legal Ethics in the Practice of Environmental Law by Irma S. Russell

This new book is an essential guide for every environmental lawyer on representing industrial clients, government agencies, individuals, and public interest groups. It focuses primarily on the rules of ethics that raise significant concerns for the environmental practitioner. A proactive approach to ethics helps lawyers avoid problems by making reasoned decisions before ethical problems arise in urgent or complicated context. This book helps you anticipate and analyze these difficult ethics issues. It also examines the American Bar Association's Model Rules of Professional Conduct (Model Rules), judicial decisions, formal and informal ABA Opinions, and opinions of state boards of professional responsibility. Contents include:



- Regulation of Lawyers
- The Duty of Competence and the Lawyer's Duty of Diligence
- The Lawyer-Client Relationship
- Confidentiality
- Conflicts Concerns in Environmental Law
- Imputed Conflicts
- Duty of Candor
- The Lawyer's Duties to Non-Clients
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- The Anti-Contact Rule
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- The Lawyer's Role in Working with Consultants
- The Lawyer Role in Working in Use of the Media
- Termination and Withdrawal from Representation

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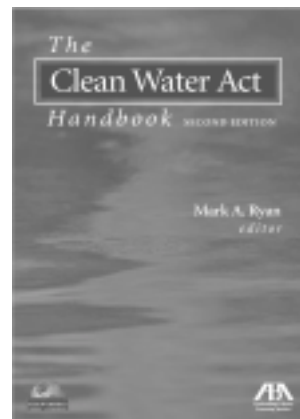
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Price: Section of Environment, Energy, and Resources members \$64.95; Regular \$79.95

The Clean Water Act Handbook, Second Edition

Mark A. Ryan, editor

This updated guide is the definitive resource to the provisions and complexities of the federal Clean Water Act and how it continues to evolve. Recent court rulings and the change of administration have resulted in significant changes that dramatically affect practitioners working in the area. This new edition provides detailed explanations of these changes and considers the impact of recent court decisions, including the Supreme Court's decision in *SWANCC* and the Court of Appeals decisions in *American Mining Assoc.*, *Talent Irrigation*, and *Forsgren*, among others.



Beginning with an overview of the law's provisions and pertinent regulation and enforcement issues, the subsequent chapters address specific issues, such as:

- NPDES permits
- Control of publicly owned treatment works
- Requirements applicable to indirect discharges
- The regulation of wetlands and the impact of recent judicial decisions
- Oil and hazardous substance spills
- Enforcement options under Section 309
- Judicial review

Chapters begin with a section on applicability and scope. Within each fully annotated chapter, clear explanations of specific statutory and regulatory provisions and court decisions applicable to the issue are presented in the order needed for full and accurate analysis – a virtual checklist of requirements and considerations. Making this new edition more useful than ever, the authors reference URL addresses for quick, up-to-the-minute information on government documents that are often difficult to locate.

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Superfund and RCRA corrective action sites and environmental incidents that involve allegations of natural resource damages. Despite over 20 years of experience with Superfund, RCRA, Clean Water Act and Clean Air Act, among others, there are few, if any, meaningful standards or standard practices on how to estimate costs associated with remediation related environmental matters. Everyone seems to do it differently, and one can easily get significantly different estimates for the same site based on the same information from different “experts.”

In 2001, ASTM published E 2137-01 entitled “Standard Guide for Estimating Monetary Costs and Liabilities for Environmental Matters.” Despite the title, this “standard guide” simply provides a blueprint of some of the issues one must consider when developing a cost estimate. Among the more salient aspects of E 2137-01 are that the “standard” (1) defines the term “studies,” at Sec. 3.1.9, to include more events and investigations than have historically been considered in reporting of environmental contingencies; (2) recommends inclusion of “actual or potential risk to human health and the environment” in developing the estimate; (3) recommends inclusion of damages arising from resources damages, ecological damages and the like; and (4) recommends selection of an “appropriate estimator or group of estimators,” stating that “[I]t is the responsibility of the entity sponsoring the cost and liability estimates to select an estimator with the appropriate level of knowledge, training, and experience for the parts of the estimation effort for which the estimator is responsible.” E 2137-01, Sec. 4.2.6. Accordingly, all major details are left to the judgment of the “entity sponsoring the estimate.” Indeed, the “standard guide” does not even reference a single source from which unit cost data can be obtained for use in preparing the initial cost estimate.

Proposal for Managing Environmental Counsel Responsibilities Under the Professional Conduct Rule

It seems clear that, in light of Sarbanes-Oxley Act and the Professional Conduct Rule, estimation and reporting of environmental obligations has become more complicated than they have been. To meet the intent of the Act and the Rule, counsel should pay attention to what is included within the broad term “contingent environmental obligations” and the procedures used to develop initial cost estimates to which the required “materiality” analysis will be applied. An appropriate system would, for example, document what counsel did to (1) identify most, if not all, contingent environmental obligations of the company, (2) estimate the costs, or range of costs, associated with the identified contingencies, (3) evaluate the materiality of any individual estimate as compared with aggregate estimate for all contingent environmental obligations, and (4) prepare and forward appropriate reports of the estimates, with appropriate explanations, “up-the-ladder” for evaluation in relation to the company aggregate financial position by the CFO and staff.

Here are a few suggestions for reporting counsel as they review and evaluate an existing, or develop and implement a new, internal control system in their companies (or their clients) to discharge the responsibilities under Sec. 307 and the Professional Conduct Rule:

1. Initiate a review of current practices and procedures used in their companies for identification of environmental obligations and liabilities. In addition to information in the law department, it would be helpful to review the company capital projects, including history and projected expenditures.
2. Compile cost estimates historically

produced by the company for the various projects to determine the trends, if any. Often, historical data is routinely reported year after year without an updating effort – often without even adjustments for inflation or the current status of the site.

3. Compile the identity of the relevant corporate entity, firms and individuals, including in-house engineering department, or retained engineering firm, etc., that produced the estimates. Counsel should obtain and review the qualifications of individuals and firms involved in past cost estimating scenarios, and should document the amount of time expended by the estimator(s) in developing the estimate. This is often an indicator of the rigorousness of the effort undertaken.

4. Review, with suitable independent assistance, the procedures and practices followed by the company in determining the cost estimate(s) in the past. Counsel should specifically determine the assumptions used to develop and/or modify the estimates, and why certain items are either included or excluded from consideration. For example, even though potentially responsible parties have actively participated in remedial studies and efforts under Superfund and RCRA for many years, the potential for natural resources damages and costs associated with the restoration of the damage are generally neither considered nor estimated in determining the contingent environmental liability of the company. This practice probably should be reviewed in light of the emerging aggressive trend in pursuing claims for natural resources damages by various states, such as in New Jersey.

5. Evaluate, with suitable independent assistance, whether the entities and individuals involved have employed relevant and reliable protocols in conducting the cost estimating exercise.

6. Evaluate the “materiality” of the contingent and identified environmental liabilities and decide what to report “up-the-ladder” for consideration for inclusion in documents to be filed with the SEC.

7. Document the process from identification to estimation and reporting.

As part of the internal controls of the company, counsel should consider conducting an evaluation based on the principles articulated by the U.S. Supreme Court in *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993), concerning the opinions of environmental cost estimators retained by their company. Senior management, shareholders and investors in a company should be confident that information they are receiving was developed with suitable attention to the non-exhaustive list of criteria for determining the admissibility of scientific and technical evidence in a litigation context.

Moreover, *Daubert* and its Supreme Court case progeny enunciate crucial considerations as to the standard for assessing the relevance and reliability of opinion testimony by “experts,” such as the cost estimators in the present context. The four criteria enunciated in *Daubert* for this assessment are whether the techniques used for generating the estimates (i) have been peer reviewed; (ii) have a known or potential rate of error; (iii) are generally accepted in the field; and (iv) can be and have been tested? These criteria have relevance in the present context because they provide a “scientific” basis for the cost estimate, including documentation of the range of uncertainty and the assumptions used in arriving at the estimates. As stated in the ASTM standard guide E-2137-01:

5.10 Documentation – Documentation should include the identity of the estimator and a description of their relevant knowledge, training and experience. The

estimation documentation should be sufficient for a user to evaluate the estimates. For example, it may be useful to identify the purpose and objective, the estimation approach(es), the major uncertainties considered, and the sources of information used in making estimates of *costs and liabilities* for environmental matters. This documentation may be prepared to cover a single event or multiple events estimated in a similar manner, and may consist solely or in part of existing work papers.

Environmental counsel, and others who advise them, need to be particularly circumspect in evaluating and reporting on environmental contingencies in light of the Sarbanes-Oxley Act and the Professional Conduct Rule, because of the many uncertainties that accompany environmental matters. There probably is no substitute for increased diligence throughout the process by which the relevant contingencies are identified, evaluated, quantified and reported. There is absolutely no substitute for the need to selecting skilled estimators and to document the process followed by them, and the internal controls used by counsel, in determining what counsel must report “up-the-ladder” to senior management for incorporation in periodic SEC filings.

Dr. Sunil Garg (sgarg@ecoshelf.com) is president of The EcoShelf Group Inc, a consulting firm specializing in environmental law, science and policy, project management and environmental strategy. His recent work has included expert testimony on a variety of environmental remediation and compliance issues, advice on economic benefit analysis, environmental management systems development and assessment of supplemental environmental projects in penalty settlements, and serving as a consulting expert in litigation.

THE LAW OF UNINTENDED CONSEQUENCES: HOW PUBLIC TRANSPORTATION FUNDING LAWS FAIL TO MAXIMIZE ENVIRONMENTAL AND OTHER BENEFITS FOR COMMUNITIES

William Vincent

Investing in public transportation is an important strategy for enhancing mobility, improving air quality and reducing our dependence on foreign oil.

Yet, despite decades of massive investment, fewer people commute to work by public transportation today than did 40 years ago. Roughly 12.9 percent of workers used public transportation to get to work in 1960. In 2000, that number had declined to 4.7 percent.

There are many reasons for this. We have invested far more to enable transportation by single occupant vehicles than we have to provide mobility through public transportation. We also have adopted land use policies that encourage sprawl and provide few alternatives to automobile transportation.

This article explores a third potential explanation: that the legal and regulatory structure for selecting transit projects discourages innovation. New technologies offer great potential to provide mobility and environmental benefits, but these technologies often are overlooked.

This article describes the complex and arcane requirements for transit funding and explains how that process, despite clear intent to ensure rigorous analysis and cost-effectiveness, too often leads to irrational decision-making. As a case study, it explores a proposed rail project in the northern Virginia suburbs of Washington, D.C.

History of Transit Planning and Development Law

Historically, transportation was a state and local issue. That changed in the 1950's, when the federal government began paying for the vast majority of highway projects, enabling the construction of the interstate highway system. In the 1970's, federal support for highways was seen as skewing transportation investment in favor of too many roads. Communities could receive 90 percent of the cost of building highways, but very few federal dollars were available for transit.

To remedy this imbalance, President Ford authorized transit funding from highway spending accounts, and states were given significant flexibility to choose how to allocate available resources between highway and transit.

Major transit projects began sprouting like flowers in the spring. Regions that previously could not afford transit suddenly found the federal government paying most of the tab.

Although federal support enabled important systems to be built, it also provided local governments with little incentive to propose cost-effective projects. After all, it was not their money.

In 1976, the U.S. Department of Transportation (DOT) required that projects be "cost-effective" and required analysis of alternatives for new capital investment in transit. See 41 Fed. Reg. 41512. Two years later, DOT followed up with a specific "Policy on Rail Transit" that added requirements for local governments to demonstrate financial commitment to the project and to adopt supportive land use policies. See 43 Fed. Reg. 9428.

In 1980, DOT linked these requirements to the Environmental Impact Statement (EIS)

process required under the National Environmental Policy Act (NEPA) (see 42 U.S.C. 4321-4347, 45 Fed. Reg. 71986). In 1984, DOT added a rating system to evaluate competing projects on the basis of their relative cost-effectiveness. Congress formally adopted DOT's process through the Surface Transportation and Uniform Relocation Assistance Act of 1987 (STURAA) (Pub. L.100-17).

In 1991, President Bush enacted the landmark Intermodal Surface Transportation Efficiency Act (ISTEA). ISTEA expanded the cost-effectiveness requirements, requiring that a project be "justified, based on a comprehensive review of its mobility improvements, environmental benefits, cost-effectiveness, and operating efficiencies." Three years later, President Clinton issued Executive Order 12893, which requires that all federal infrastructure investments, including transportation, undergo a rigorous cost/benefit analysis.

In 1998, Congress reauthorized ISTEA with the Transportation Equity Act for the 21st Century (TEA-21) (Pub. L. 105-178). TEA-21 kept many ISTEA requirements and added, among other things, requirements to consider the cost of sprawl and cost savings due to compact land use.

Despite the clear intent to ensure cost-effective transit investments, the reality too often is quite different. As a result, innovative and cost-effective mass transit technologies often are left on the cutting room floor – if they ever are seriously considered – in a process that somehow manages to keep serving up "light rail" technology sausage, regardless of what other technologies are available. All too often the decision to proceed with light rail is made without adequate regard for the financial, environmental and social impact inputs that are supposed to be addressed through the EIS process.

A central problem is the statute that defines the eligibility for federal funding of transit capital projects. Under this statute, known as “New Starts,” funding is limited to “fixed guideway” systems. See 49 U.S.C. § 5309. As the term implies, “fixed guideway” means that the system must operate on a permanent track or route, which usually means a rail system.

Fixed guideway systems, however, are very expensive, in some cases costing hundreds of millions of dollars per mile to build, then requiring perpetual government subsidies to continue operating. Innovative technologies that do not require fixed guideways have difficulty qualifying for this funding, even though they can perform as well or better at a fraction of the cost.

A separate problem is the complexity of the process to obtain New Starts funding. The process involves many agencies at various levels of government. Few people understand it, and there are very limited opportunities for public involvement, making it difficult for all but industry insiders to have meaningful input.

In regions that are “non-attainment” areas under the Clean Air Act (CAA), projects proceed on several tracks. For example, a project must be included in a long-range transportation plan and a transportation improvement program (TIP) developed by the region’s metropolitan planning organization (MPO). There must be a public involvement process, and the plan and TIP must conform with the state’s air quality plan.

Second, a project must go through a multi-phase planning and development process. This process begins with the alternatives analysis discussed above, which itself has several components, including major investment studies (MIS), public involvement requirements, and financial plans. It also may include an environmental impact statement as

required under NEPA.

Once alternatives analysis is complete, a locally preferred alternative (LPA) is selected. Then, a project must go through preliminary engineering, final design, and construction. Between each of these stages, the Federal Transit Administration reviews the project and approves its advancement to the next stage. Ultimately, though, FTA is empowered only to make recommendations, which Congress must approve.

Unfortunately, the discrepancy between theory and practice is wide when this process is put to the test. An example follows.

The Northern Virginia Story

Since the 1960’s, a right-of way in the Dulles International Airport access road was reserved for a future rail connection. In the mid-1990’s, the Virginia Department of Rail and Public Transportation (DRPT) began planning to use this right-of-way to extend the Washington subway system, known as MetroRail. Metrorail is by far the most expensive option available, costing hundreds of millions of dollars per mile.

DRPT initiated the “alternatives analysis” process in the mid-1990’s. Despite the requirements to objectively examine alternatives, many public officials endorsed extending Metrorail, even though the alternatives analysis process was not complete.

During the same period, a number of organizations formed to lobby for Metrorail. The Dulles Corridor Rail Association (DCRA) was created to “advocate rail in the Dulles corridor by 2010, sooner if feasible.” Similarly, the Landowners Economic Alliance for Dulles Extension of Rail (LEADER) was formed to raise funds for the local costs of extending Metrorail.

In 1997, DRPT completed a study that examined rail and recommended building rail. It also concluded, however, that “substantial congestion would remain” after completion of the project, and that “substantial risks exist that the ridership and effectiveness of the rail alternatives will be less than projected....” (Dulles Corridor Transportation Study, Final Report, June 1997, at 6-8.)

Shortly thereafter, an unsolicited proposal to build rail was received from some of DCRA’s founding members. The proposal was submitted under the Virginia Public Private Transportation Act, which allows the Commonwealth to negotiate sole source contracts for transportation projects. In this case, the contract is potentially worth at least \$4 billion, all of which can be awarded without competition.

Also shortly thereafter, Congressional leaders demanded a revised study examining bus rapid transit (BRT). In July 1999, DRPT released a supplemental study, but this study examined BRT merely as an interim solution to rail, not as a substitute for rail. To justify this, the study used strained logic, arguing that BRT could not substitute for rail because, in part, “BRT would not help expedite rail....” (Supplement to the Dulles Corridor Transportation Study, July 1999, at 8.)

DRPT next hired the Washington Metropolitan Area Transit Authority (WMATA) to prepare the Draft Environmental Impact Statement (DEIS) required under NEPA. WMATA built and operates the Metrorail system. WMATA is exempt from various public accountability requirements, including the freedom of information act (FOIA), thus arguably shielding the process from public scrutiny.

WMATA, in turn, used a long-standing contract to sole source the DEIS to a partnership of engineering companies. This partnership expressly stated that at least one of its

members anticipated being involved in future phases of the project. Thus, there was an apparent incentive to recommend a more expensive solution.

Unlike the previous studies, WMATA now purported to include BRT as a stand-alone option. The BRT options, however, appeared to be nothing more than straw proposals designed to make Metrorail attractive, rather than true, objective alternatives. For example:

- BRT was allocated a maximum of 5 stations, MetroRail had 13;
- BRT was designed to bypass Tyson’s Corner, the 12th largest central business district in the nation. Metrorail was proposed to serve the heart of Tyson’s with four stations;
- BRT was given low capacity diesel vehicles, even though high capacity, low-emission vehicles are now widely available, and zero emission fuel cell buses are on the horizon; and
- The study assumed that no emissions would result from operating Metrorail, even though extending the Metrorail inevitably would add to the burden – with its attendant pollution emissions – presented by coal-fired electric power plants that produce the juice, the life-blood of electrically powered rail.

Although the flaws and conflicts were pointed out in comments, Virginia used the DEIS to select Metrorail as the locally preferred alternative. At this point, the Federal Transit Administration (FTA) intervened, raising serious doubts about the legality of the project. See The Washington Post, Dec. 4, 2002. Nevertheless, Virginia officials returned to Richmond and, less than three weeks later, approved the entire project, at an estimated cost of \$4 billion, more than ten times the projected cost of available alternatives that could provide equal or better service.

So What Does All This Mean?

As shown in the Northern Virginia example, the process can be used to justify a particular technology that otherwise would never meet objective standards for cost-effectiveness. But why should we care?

Transit resources are extremely limited. By overspending on particular projects, we limit the amount of new transit capacity that can be built. We also ensure that some communities who want new or improved transit will not get it, because the money is being used elsewhere.

Moreover, to maximize the environmental and other benefits of transit, we need to invest in the most appropriate technologies available, given the particular circumstances for the project. Thanks to a skewed process, however, we lose the benefit of competition on a level-playing field, which was the intent of Congress and DOT in the first place.

Situations like this create ample opportunities for lawyers. For example:

- Providing particular communities with expensive transit service, without providing comparable service in other communities, can create an actionable claim. A case against the Los Angeles County Metropolitan Transportation Authority on this issue recently was settled by consent decree (*See Labor/Community Strategy Center v. Los Angeles County Metropolitan Transp. Authority* (9th Cir. Aug. 31, 2001, No. 99-56581)).
- To raise money, local governments may use a variety of tactics, including special tax districts, debt financing, sales and property tax increases, and increases on highway tolls. Businesses, property owners, and

others in the community who are expected to pay these bills may desire representation.

- NEPA requires that reasonable alternatives be adequately considered and that the EIS be used to inform the decision-making process, not to justify previously made decisions. Although agencies have some discretion, NEPA is being used in support of a claim where, as the Northern Virginia case suggests, it appears that (1) decisions were made long before the process was complete, (2) a significant source of pollution was ignored in the EIS, and (3) a substantial reduction in the massive traffic congestion confronting Northern Virginia is not even present as a justification for a mass transit proposal of such enormous cost and scope.
- Federal transportation laws, including the New Starts requirements, are due to be reauthorized this year. Significant discussions are underway about reforming New Starts so that federal capital dollars are technology neutral, rather than expressly biased in favor of rail technologies. Interests on various sides of this issue may desire representation.

Transit funding is a scarce resource that must be used wisely. We must be faithful to Congressional and DOT intent to ensure rigorous analysis and cost-effective investments. Lawyers can play a key role in making this happen.

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**A TALE OF TWO SITES:
HOW INSURED FIXED-PRICE CLEANUPS
EXPEDITE PROTECTIONS, REDUCE
COSTS, AND HELP EPA, THE SEC
AND THE PUBLIC**

Michael O. Hill

This article compares two waste oil Superfund Sites virtually identical in size and character but vastly different in policy approach and cleanup results. The first Site employed an Insured Fixed-Price Cleanup (IFC) and, as a result, was cleaned up in 19 months, at 40 percent below estimated costs and with no litigation. At the second, where an IFC has not been used, cleanup has been stalled for years, more has already been spent on attorneys' fees and other transaction costs than was required to clean up the IFC Site in its entirety, and estimates of future cleanup costs rise yearly as the Site contamination spreads. The IFC Site now is being used as public fields and open space; at the non-IFC Site, no beneficial use is foreseeable for years. At the IFC Site, the cleanup was funded solely by the Potentially Responsible Parties (PRPs) who sent the waste to the Site; at the non-IFC Site, the public has footed the lion's share of the bill. Finally, at the IFC Site, the PRPs identified and set aside from the start funding for more than twice the estimated cleanup costs; at the non-IFC Site, the Securities & Exchange Commission (SEC) and public have virtually no assurance that the PRPs have even identified much less set aside even a fraction of the government-estimated cleanup costs. This article urges

policymakers in general – at EPA, the SEC, and Congress – to consider IFCs as a way past existing obstacles to Superfund cleanups. It urges policymakers to enact guidance, regulations, and/or statutes to encourage the use of IFCs as an environmental tool. Three specific regulatory suggestions are outlined at the end.

IFCs are a relatively new tool and any of several reasons might discourage or even prevent their use at a particular site. Still, at sites where IFCs are well-suited they offer enormous public and private benefits. When an IFC first was proposed five years ago for the IFC Site that is the focus of this article – the *Portland Bangor Waste Oil (PBWO)* Superfund Site in Wells, Maine – the Wall Street Journal foresaw the use of IFCs as holding the potential to “end the tangle of Superfund litigation” and otherwise provide public benefits (*Maine Experiment May End The Tangle Of Superfund Litigation*, Wall St. J., Apr. 29, 1998). In 2000, immediately following judicial entry of the *PBWO* settlement, officials from the State of Maine hailed the settlement as “revolutionary” (*BNA Daily Environment Reporter*, June 8, 2000, at A-6). Finally, in 2002, following the completion of the *PBWO* cleanup, the Boston Globe revealed that the Wall Street Journal and the State of Maine's prognoses were on the mark: “The Portland-Bangor Waste Oil site was once one of Maine's most polluted and poisonous eyesores. . . . today it is a grassy field where the community will host games for children and choose a name for the site from a school contest” (*Speedy Dump Site Cleanup Celebrated*, Boston Globe, Oct. 26, 2002).

Five years into their history, IFCs are no longer an experiment. They have proven to be important environmental tools by the results at the *PBWO* Site and at over 50 other sites. To date, however, federal-lead sites generally have not emerged as IFC sites. For example, the *PBWO* Site cleanup was directed by the

State of Maine. The non-IFC Site, by contrast, is being led by EPA.

The Two Sites

PBWO

The Site where an IFC achieved a timely and cost-effective cleanup – with adequate funds segregated up front – is the Portland Bangor Waste Oil (*PBWO*) Superfund Site in Wells, Maine. A cleanup consent decree was entered on May 30, 2000, with government-estimated future cleanup costs at \$25M. Approximately 60 percent of the 3000 PRPs that allegedly sent waste oil to the site contributed about \$15M, an amount that the Cleanup Contractor (TRC Companies, Inc.) believed was sufficient under an IFC model to complete the cleanup *and* to purchase enough insurance and bonding to cover potential costs increases up to \$30M. Nineteen months later – less than one-fifth the average federal cleanup time – the cleanup was done, and less than a year after that, a Site-naming contest was held by the local elementary school and a community celebration held on the Site's new fields. Nowhere else in Superfund's 22-year history has a cleanup of this size and complexity been accomplished with such speed and obvious public benefits.

Beede

By contrast, roughly 50 miles to the west of the *PBWO* cleanup, progress at the Beede Waste Oil Superfund Site (*Beede*) cleanup has languished for years. The majority of the *Beede* Site PRPs (as measured by their respective waste volumes) collectively asked EPA to allow the same Cleanup Contractor and Insurer that accomplished the *PBWO* IFC to try an IFC at *Beede*. Whether consciously or not, EPA has discouraged the IFC effort, through refusals to meet, imposition of changing conditions, and in other ways. In the interim, EPA's mostly-administrative costs

have grown to over \$20M, the plumes have spread, and the PRPs have spent millions of dollars on attorney's fees and other non-cleanup costs, precisely the transactional costs that Congress and presidents have long identified as perhaps the most critical problem in the Superfund Program. Decades after regulators were first put on notice of the *Beede* Site's problems, cleanup still remains years away, and there are no clear plans for any beneficial re-use. Whereas an IFC allows all PRPs to settle from the outset, EPA has allowed only the smallest of the *Beede* PRPs to settle (less than 10 percent of the total by waste volume). Moreover, those PRPs who were allowed to settle were required to do so at a price roughly 20 percent more than they could have under an IFC, because EPA's approach does not reflect any of the cost advantages presented by an IFC (discussed below). The purpose here is not to "bash" the specific regulators involved at the *Beede* Site. Indeed, two EPA regions (Regions 2 and 9) have been very receptive to, and have in fact implemented or are about to implement IFCs (though the Region 9 model is somewhat different from that which is discussed here). The point of this article is to encourage policymakers in general to consider IFCs where appropriate as a cost-effective and environmentally sound solution.

The Mechanics of an Insured Fixed-Price Cleanup (IFC)

The mechanics of an IFC are probably best explained through the use of a hypothetical. Assume a Site (Site X) that has an EPA-estimated cleanup cost of \$100M and where the waste came from 55 PRPs, 50 of whom each sent 1 percent of the waste (and therefore likely qualify as "De Minimis" PRPs under EPA's Policies), and 5 of whom each sent 10 percent of the waste (and therefore are considered "Major" PRPs).

In a nutshell, the PRPs transfer into a

“Cleanup Account” sufficient funds to accomplish the entire cleanup. The sufficiency of the funds is first triple-checked by three independent entities – the Contractor, the Insurer, and the government – each of which has a vested interest in ensuring their adequacy. (The separate motivations of these three entities to ensure adequacy of funding is explained below). Simultaneously, the PRPs collectively purchase an insurance policy that provides at least twice the estimated costs of the cleanup. Thus, at the \$100M Site X, the PRPs might put \$100M into the Cleanup Account plus pay the Insurer \$20M in order to obtain another \$100M in cleanup costs through insurance. In this way, for \$120M, the PRPs have assured the government that \$200M in cleanup costs will be available.

In return for the \$20M premium, the Insurer is obligated to EPA to: (1) hold the estimated cleanup costs in the Cleanup Account and pay those funds to the Contractor only as the cleanup is accomplished; and (2) provide another \$100M in cleanup costs if the costs exceed the amount held in the Cleanup Account. The Insurer has every motivation to limit the amount paid to the Contractor (*i.e.*, to pay only those costs that are reasonably incurred), because if the \$100M in the Cleanup Account is used up before the cleanup is complete, the Insurer must provide up to another \$100M to complete the cleanup. If the Insurer fails in this, EPA can look to the Major PRPs for completion of the cleanup.

The government gives up nothing under an IFC . . . it loses no rights with respect to any PRP, and it gains rights with respect to a new and voluntary PRP . . . the Contractor. As happened at the PBWO Site, the Contractor voluntarily becomes a PRP and thus remains entirely subject to the government’s control, forever, with respect to the type and adequacy of the cleanup. If the Contractor becomes bankrupt or fails in other respects, the government still has the balance of the \$100M

in the Cleanup Account *plus* another \$100M in Insurance Proceeds. Finally, if the Cleanup Account and Policy are exceeded, then just as the government can do under today’s settlement policies, the government can still pursue the Major PRPs. The *only* PRPs who get a full release are the De Minimis PRPs . . . the same ones that get full releases under today’s policies. Bottom line: the government merely gains a new and voluntary PRP and gives up none of its authority with respect to the historical PRPs.

Public and Private Cost Savings

Under an IFC, cost savings are achieved in at least 4 significant ways.

1. Lower Premium for Equal Coverage. Continuing with the \$100M Site X hypothetical, under EPA’s Settlement Policy, each individual Major PRP who settled under EPA’s current Settlement Policies would need \$15M to settle with EPA. This number is reached by taking the PRP’s 10 percent share of \$100M to get \$10M, and then adding to that number a 50 percent premium to protect EPA in case of cost overruns up to \$200M. (See, *e.g.*, EPA Guidance, Standardizing The De Minimis Premium (July 7, 1995) (noting “presumptive premium figures” of “100 percent for a settlement without a cost reopener and 50 percent for a settlement with a cost reopener”). De Minimis PRPs – who today are eligible to obtain complete releases from EPA with no chance of re-openers – typically must pay a 100 percent premium, thus increasing their 1 percent contribution of \$1M to a total contribution of \$2M. By contrast, through the private insurance market, the PRPs could buy insurance that similarly covered cost increases of up to 100 percent (*i.e.*, up to \$200M) but only pay a 15-25 percent premium for that coverage (See *supra* Section II). The government would still have the \$200M in available cleanup funds, but for an overall cost reduction of 20 percent for the

Majors and 40 percent for the De Minimis PRPs.

2. *Increased Efficiencies in the Cleanup.*

The next saving – which can be expected to be 15-40 percent – comes from the increased efficiencies of a cleanup done by a single PRP instead of a collective effort by tens, hundreds, or even thousands of PRPs. The IFC model – where the cleanup is done by a single-PRP – enables both the Contractor and the EPA to operate far more efficiently than multiple PRPs can under the traditional approach, and the Contractor/PRP remains fully under EPA's direction and must perform the cleanup just as (and as long as) EPA dictates. At the *PBWO* Site, the cleanup Contractor accomplished a government-estimated \$25M cleanup for less than \$15M. At the *Beede* Site, the same Contractor promised to perform the government-estimated \$46M cleanup for \$40M, while providing insurance coverage for costs up to \$92M.

3. *Private Transactions Costs Avoided.* The General Accounting Office (GAO) has estimated that PRPs spend as much as \$1 in litigation and other transaction costs for every \$2 they spend on the actual cleanup (GAO, *Superfund Legal Expenses for Cleanup-Related Activities of Major U.S. Corporations*, GAO/RCED-95-46, Dec. 1994, at 1)). Although some Superfund program improvements have been made since this GAO report issued, the problem remains. IFCs can be accomplished with *no* litigation, as happened at the *PBWO* Site. While some legal fees will still be incurred (e.g., to negotiate and enter the settlement), they are only a small fraction of what they could be otherwise.

4. *Public Transactions Costs Avoided.* At the *Beede* Site, EPA has already spent over \$20M, most of it in the form of transaction costs such as organizing the PRPs. EPA's own cost model estimates that, region by

region, EPA spends 29 percent to 54 percent just in indirect costs (e.g., rent, administration, etc.). See EPA Guidance, *Accounting for Indirect Costs Associated With Superfund Site-Specific Activities*, May 26, 2000. At *PBWO*, these costs were almost entirely avoided, since the government obtained an early settlement for full relief and left it to the Contractor to organize the PRPs and then carry on their work. Interacting with one Contractor under EPA control, of course, is far less costly and far more efficient than interacting with hundreds or thousands of PRPs.

IFCs Promote the Policies of EPA and the SEC

IFCs not only are legal – as evidenced by judicial entry of the *PBWO* consent decree – but they promote existing EPA and SEC policies and goals.

EPA Policies and Goals

The ways in which IFCs meet EPA's policies and goals of expediting cleanups the saving costs were discussed above. This section provides a summary of the goals, the EPA Guidance documents that state them, and the manner in which IFCs meet them.

- EPA has an identified goal of preserving the Superfund and encouraging private party cleanups. See October 1999 Interview of EPA Assistant Administrator Tim Fields, *Inside EPA's Superfund Report*, at 27, Oct. 27, 1999 (trust fund balance expected to expire in the year 2001); EPA, *Interim CERCLA Settlement Policy*, OSWER Dir. 9835.0, at *5, Dec. 5, 1984, and EPA, "Addendum To The *Interim CERCLA Settlement Policy*" Issued On December 5, 1984," at *3, Sept. 30, 1997). Because IFCs use only private funds (from PRPs), and because IFC cleanups are done by

PRPs or by the Contractor as their agent, IFCs advance these two government goals.

- EPA seeks to minimize its own legal and administrative costs and to focus instead on achieving prompt cleanups. See *Interim CERCLA Settlement Policy*, at *7. IFCs expedite settlements and enable the EPA to interact with just one PRP (*i.e.*, the Contractor) instead of the many historical PRPs.
- Perhaps in recognition of the fact that most Superfund PRPs did not break the law or act irresponsibly in any other way, EPA has a stated policy goal of reducing PRPs' legal and other transaction costs (*e.g.*, 63 Fed. Reg. 24784, 24792 (May 5, 1998)). IFCs advance this goal because they avoid litigation and promote early settlements, and because through an IFC the PRP contractor – not the myriad historical PRPs – is fully responsible for interacting with the EPA during the cleanup.

SEC Policies And Goals

Scholars and others have long urged the SEC to do more to require publicly-traded companies to disclose their environmental liabilities (*e.g.*, Theodore Sonde and Harvey Pitt, *Utilizing Federal Securities Laws To "Clear The Air! Clean The Sky! Wash The Wind!"*, 16 How. L. J. 906 (1971); National Research Council, *Innovative Technologies In Toxic Waste Cleanup Need Federal Boost* (1997)). Nevertheless, 74 percent of companies in a recent study failed to comply with SEC reporting requirements with respect to environmental liabilities. (See EPA Office of Enforcement and Compliance Assurance, Enforcement Alert, Vol. 4, No. 3 (Oct. 2001); see also The Rose Report, *The Environmental Fiduciary: The Case For Incorporating*

Environmental Factors Into Investment Management (Fall 2002)).

The use of IFCs help to correct this problem. As noted in Section II, before an IFC is implemented, the PRPs must collectively identify how much it will cost to clean up the site and insure it against cost overruns. They then collectively set aside those funds by placing the anticipated cleanup costs in a Cleanup Account (formally called a "commutation" or "experience" account) and also pay the premium for an insurance policy to protect against cost overruns. Thus, under the hypothetical Site X discussed above, the PRPs would at the outset put \$100M into the Cleanup Account and also pay a premium (*e.g.*, \$20M) to obtain insurance to cover costs of up to \$200M. Because the funds required for the Cleanup Account and the policy premium are both funded up front, necessarily the PRPs are identifying and setting aside adequate cleanup funds from the outset.

IFCs also offer an improved method for ensuring that the amount needed for the Cleanup Account is adequately estimated. The amount is not determined solely by the PRPs. As noted above, it is triple-checked by at least three outside entities that each has a vested interest in ensuring that the amount is adequate. First, the Contractor will not agree to take over the cleanup obligations unless it has independently determined that the Cleanup Account has enough funds to pay for it. Second, the Insurer will not agree to insure against cost overruns unless the Insurer is reasonably confident that overruns will not occur. In short, market incentives drive both the Contractor and the Insurer to independently ensure the adequacy of the Cleanup Account. Finally, before an IFC is allowed to proceed, it requires the government's (and often a court's) approval. That approval will not be given unless the government has independently satisfied itself that the Cleanup Account is adequately funded.

Further, the SEC and public are given still greater assurance because, in addition to the Cleanup Account, IFCs have access to insured funding of twice the amount of the Cleanup Account.

Finally, in most cases, the SEC and public are given a third layer of protection, which is a full indemnity from the Cleanup Contractor. The degree of protection this third layer offers will depend, of course, on the assets of the Contractor. This article is not suggesting that this third layer of protection is sufficient in itself. The indemnity does, however, add to the protections offered by the separate Cleanup Account and the Insurance, and for this reason it is a net plus for the SEC and the public.

IFCs Address Government Critiques of the Superfund Program

Findings by the GAO and other government entities over the years show that the problems experienced at the *Beede* Site are neither new nor unique. Many of the problems can be blamed on the structure of the Superfund statute, which was passed hurriedly during the last months of the Carter administration in late 1980. IFCs are an important tool for overcoming many of the problems.

Transactions Costs. IFCs can vastly reduce the inordinate transaction costs that GAO's report (*supra*) documented, because they are accomplished from the outset without litigation, and the settlement is offered to *all* PRPs – small *and* large – from the outset.

Delay In Cleanup. In 1998, the GAO found that EPA took an average of 9.4 years from the discovery of the contamination to get a site added to the National Priorities List, and another 8 to 10 years to complete the cleanup (GAO, *Superfund, Times To Complete Site Listing And Cleanup*, GAO/RCED-98-74 (Feb. 4, 1998)). The *PBWO* remedy was completed

in less than a quarter of that time. There are two reasons for this expedition: (1) a single Contractor-PRP can work far more efficiently than a multi-party PRP group; and (2) the Contractor-PRP has a vested interest in expediting the cleanup in order to expedite its payments, which are held in a "Cleanup Account" and paid out only as the cleanup is accomplished. It is important to remember, however, that since the Contractor becomes a statutory PRP, EPA will always retain control over the speed and scope of the cleanup.

A common misconception is that EPA might have to sue the Insurer, or step back in and pay for the entire cleanup if the Insurer and the Contractor were to become insolvent. It would not, at least not under the type of IFC advocated in this article. That is because all but De Minimis PRPs would remain potentially liable, and thus EPA could look to non-De Minimis PRPS if the Insurer and the Contractor were to become insolvent or failed in their obligations in any other respect. In fact, because IFCs accelerate settlements – largely because the PRPs get a better deal for less money – EPA is in a better position with respect to the PRPs because EPA will not need to sue them: the PRPs will already have settled and be bound by a Consent Decree.

Measurable Improvement In Reform: In 2000, the GAO reviewed 62 EPA administrative reforms and found that 42 "did not have a fundamental effect," another 6 "did not have measures to demonstrate [results]," and another 7 had no demonstrated achievements. In all, only 7 of the 62 reforms had fundamental and measurable effects (GAO, *Superfund: Extent To Which Most Reforms Have Improved The Program Is Unknown*, GAO/RCED-00-118 (May 2000)). IFCs have fundamental and measurable effects (*e.g.*, lower costs, faster cleanups, better accounting).

Promoting The "Polluter Pays" Principle. IFCs do not rely on the Superfund, but instead use only private funds, thus promoting EPA's goal of having the "polluter" pay, rather than the taxpaying public. Furthermore, and related to the "delay in cleanup" principle above, by collecting private funds around a settlement structure that encourages the expedition of cleanup, IFCs expedite cleanups. The problem of delays through lack of public funding became even more acute last year, when the Superfund ran out of virtually all of its funds. EPA's Inspector General found that shortages in the public funding had led EPA to "slow[] the cleanup of 33 highly contaminated hazardous waste sites because of funding shortfalls." Washington Post, at A2 (June 2, 2002). A Knight Ridder analysis issued in April of this year found that the number of Superfund cleanups completed in fiscal years 2001 and 2002 fell 41 percent compared with the annual average for the previous eight years. While not a panacea, the private-funding mechanism used in IFCs helps to mitigate this situation.

Regulatory Suggestions

As noted above, IFCs tend to promote public policy goals, both environmental and financial. What's needed is something to encourage their broader use, particularly at federal sites. Three possible tools are (1) presumptions favoring the use of IFCs; (2) specific numeric goals to encourage the use of IFCs; and (3) the creation and implementation of EPA guidance regarding use of IFCs.

Policy Presumption. Under EPA's current settlement policies, EPA regional offices are guided to use specific settlement premiums as *presumptive* starting points: 100 percent premium when the PRPs obtain a full release, and 50 percent when the PRPs obtain a release that is subject to "re-openers" (e.g., if the remedy fails), as noted above. While the regions are not firmly bound by these

presumptions, where the presumptions are departed from, the regions are directed to explain the departure in writing (see, e.g., EPA Guidance, *Standardizing The De Minimis Premium* (July 7, 1995)).

The same approach could be used for IFCs. While they should not be required at every site, policymakers could reasonably demand an explanation for why they were not used at a particular site, given the many public benefits that IFCs can bring.

Numeric Goals. In the mid-1990's, when EPA began implementing its Brownfield initiative – designed to convert contaminated and abandoned, idled, or underused industrial and commercial sites to productive use – it set specific numeric goals, with deadlines. Specifically, EPA challenged itself to implement 50 Brownfield cleanups within the first two years. (See Office Of Technology Assessment, Congress of the United States, *State of the State on Brownfields: Programs for Cleanup and Reuse of Contaminated Properties*, OTA-BP-ETI-153, at 25 (June 1995); EPA Guidance, *The Brownfield Economic Redevelopment Initiative*, 9230.0-30, at 13 (Sept. 1995)).

Policymakers should set similar goals in the IFC context. To start, even a far more modest goal would be an enormous help. Specifically, EPA Headquarters and the SEC could challenge each EPA region to implement at least one IFC within the next 18 months (*i.e.*, by the end of 2004). In case some regions miss this target, EPA Headquarters could challenge itself to ensure that a missed IFC in one region is made up by an additional IFC elsewhere, so the public is assured of at least 10 IFCs nationwide by the end of 2004. If EPA does not take up this challenge itself, Congress could require it by legislation.

Creation and Implementation of Guidance. Finally, when EPA began implementing its

Brownfield initiative in the mid-1990s, it expressly identified as a goal for the year 1995 the development of new guidance (OTA Assessment (*supra*), at 25). The danger of identifying this regulatory step is that the Guidance could take months or even years to create, and so this step, taken alone, could actually postpone the use of IFCs. However, as it did with Brownfields, EPA should combine this identified goal with a concurrent step of identifying a numeric goal. In the long run this step will likely facilitate the widespread use of IFCs where they are appropriate.

Conclusion

With five years of hindsight, the 1998 Wall Street Journal has been proven right: IFCs do help to end the tangle of Superfund litigation; they can reduce costs to the public and the PRPs; they can expedite cleanups; and they can provide unique and presently unavailable assurances to the SEC. Given the enormous and demonstrated policy benefits, EPA and the SEC should take active steps to promote the use of IFCs.

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AMERICAN BAR ASSOCIATION SECTION OF ENVIRONMENT, ENERGY, AND RESOURCES

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Moderator: David Fischer, Chlorine Chemistry Council, Arlington, VA,

Speakers: Dr. Gio Batta Gori, Health Policy Center, Bethesda, MD; James Conrad, Jr., American Chemistry Council, Arlington, VA; Terry F. Quill, Duane Morris LLP, Washington, DC; Rena Steinzor, University of Maryland School of Law, Baltimore, MD

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