

Compliance Lessons From Toyota's Clean Air Act Settlement

By **Jeffrey Corey** (February 23, 2021)

On Jan. 14, the U.S. Department of Justice and the U.S. Environmental Protection Agency announced a \$180 million settlement with Toyota Motor Corp. and related entities.[1]

On the same day, the DOJ filed a proposed consent decree in the U.S. District Court for the Southern District of New York that, if judicially approved, will resolve a decade of Clean Air Act violations stemming from Toyota's failure to report emission-related defects.[2]

As part of the settlement, Toyota admitted that, between approximately 2005 and 2015, it routinely filed late emission defect reports "and, in many cases, failed to file such reports at all." [3]



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Toyota's settlement is small in comparison to the emissions-cheating scandals that resulted in Volkswagen AG and Mercedes-Benz paying, respectively, \$1.5 billion and \$14.7 billion in fines and other penalties. But the case is another example of a major auto manufacturer failing to abide by basic Clean Air Act requirements.

The settlement also provides several lessons that extend well beyond the specific compliance issue involved in the case.

If you tell the EPA you will adhere to certain compliance standards, you should adhere to those standards.

The government's case against Toyota was made much easier by Toyota's violation of a prior agreement with the EPA. In 2002, Toyota and the EPA engaged in a series of meetings regarding when Toyota would file EPA emission defect information reports, or EDIRs.[4]

Clean Air Act regulations require that automobile manufacturers file EDIRs so that, in turn, the EPA may determine whether to demand a recall or take other action related to a manufacturer's emission control defects. The 2002 meetings culminated in an agreement between Toyota and the agency that Toyota would file EDIRs based on certain volumes of warranty claims and other specified metrics.[5]

Toyota adhered to its agreement with the EPA for several years. In 2005, however, Toyota simply stopped following the agreed-upon reporting process — and it never notified the EPA of its effective withdrawal from the agreement.[6] Its noncompliance continued until 2015, when it self-disclosed to the EPA and the DOJ that it had failed to abide by its agreement for nearly a decade.[7]

Toyota's noncompliance was exacerbated by its failure to listen to its own employees. As part of its recently announced settlement, Toyota admitted that multiple times, personnel charged with filing EDIRs called for the company to submit the reports to the EPA, in accordance with Clean Air Act requirements.[8]

These internal warnings, however, did not cause Toyota to come into compliance with its 2002 agreement with the EPA, or otherwise change its practices with respect to EDIR reporting.[9] Toyota's violation of its 2002 agreement effectively handed the government an enforcement case on a silver platter.

In enforcement cases, the government bears the burden of establishing that a defendant had the requisite intent or mental state to commit the violation at issue. In environmental cases, that burden is often complicated by the fact that many regulatory requirements are less than clear.

Defendants in environmental enforcement cases can reasonably argue that perceived violations were unintentional or not violations at all, given regulatory standards that can be difficult to apply in real world operations. In Toyota's case, however, the EPA went out of its way to meet with Toyota in 2002, to remove any regulatory uncertainty as to when the company should file EDIRs and other emission-related reports.

Given that history, it should have been fairly easy for Toyota to achieve compliance. It is hard to understand why Toyota's internal controls were so deficient that the company effectively ignored its 2002 agreement a few years after carefully negotiating it with the EPA.

Toyota's \$180 million penalty should serve as a reminder to companies both big and small that the EPA has a long memory — and those who disregard their agreements with the agency do so at their own peril.

Environmental compliance failures may give rise to criminal liability — or at least motivate the EPA to consider a criminal referral.

Shortly after the settlement was announced, Evan Belser, deputy director of the EPA's Air Enforcement Division, publicly praised the outcome, and warned that the EPA takes "so-called 'paperwork' violations seriously."^[10] Belser's characterization of the case as involving mere paperwork violations may have been generous.

The DOJ's public filings suggest that the case involved more troublesome conduct. Simultaneously with the filing of the proposed consent decree, the DOJ filed a complaint alleging conduct that goes far beyond paperwork violations.

The complaint alleges an intentional effort on Toyota's part to avoid compliance, including a combination of ignoring knowledgeable employees and failing to provide adequate training to other employees.^[11] For example, the DOJ's complaint alleges that a Toyota employee repeatedly flagged EDIR reporting issues in correspondence with the company's audit staff, including a 2014 email in which the employee stated "[as] long as EPA is not asking about EDIR then I do not want to change."^[12]

The complaint also alleges that Toyota's audit department personnel "often had a weak understanding of EPA regulations and weak English language skills," and that the company failed to provide adequate training or oversight to ensure it complied with Clean Air Act reporting requirements.^[13]

Given these allegations, Toyota may have been fortunate to avoid criminal charges against it or its employees. The DOJ's press release suggests that it and the EPA considered referring the case for criminal prosecution, as it specifically thanks "the agents at EPA's Criminal Investigative Division for their critical work on this case."

It is highly unlikely that the DOJ would have gone out of their way to thank the EPA's Criminal Investigative Division agents if the EPA had not devoted resources to investigating Toyota's criminal liability. The undisputed facts of the case — including knowing violation of an agreed-upon compliance standard, and ignoring internal calls for compliance — certainly make it a potential candidate for criminal charges.

Notably, Toyota has a prior criminal record that typically would make charges more likely. In 2014, the company entered into a deferred prosecution agreement to resolve criminal charges related to allegations that it defrauded consumers by issuing misleading statements about safety issues.[14]

It is impossible to know, of course, how close Toyota may have come to criminal charges. Among other nonpublic aspects of the case, there may be undisclosed mitigating facts that ultimately justified the government's apparent decision not to pursue criminal sanction.

Moreover, Toyota's self-disclosure of its noncompliance — even if it did come after ten years of misconduct — would justify some degree of leniency from the government. The company has also stated publicly that it put a new reporting and compliance process in place within months of its self-disclosure, so it may be that Toyota's remedial actions earned it credibility with the EPA and the DOJ.[15]

Although the details of the parties' negotiations and government's internal decision-making process are not publicly available, this much seems clear: Toyota's conduct appears to have placed the company — and potentially some of its officers — in serious legal jeopardy, so much so that they may have been the targets of a criminal investigation.

One lesson from Toyota's \$180 penalty and its potential close call with criminal liability is that compliance costs are not costs at all. Rather, they are prudent investments that help companies avoid the far more damaging costs associated with civil or criminal enforcement.

Indeed, Toyota likely could have paid for employee training and implemented proper compliance controls for a fraction of the \$180 million penalty it will pay to settle the matter, assuming its settlement is approved by the court. Whatever short-term benefits Toyota gained from not submitting defect reports likely are insignificant compared to the nonmonetary costs stemming from the company's compliance failure — such as damage to the company's reputation, and having employee time focused on after-the-fact internal and government investigations.

A basic lesson for Toyota, and any other company operating in a heavily regulated industry, is that paying for a robust and well-funded compliance program is far better than having your employees face the immense pressure of a government investigation — especially one that could expose them to criminal liability.

Automakers and others in the mobile source industry should expect more scrutiny in the Biden administration.

A final lesson from Toyota's settlement is that a \$180 million civil penalty may soon be a small price to pay for intentional Clean Air Act violations involving mobile sources.

The EPA and the DOJ announced Toyota's settlement just six days before the start of the Biden administration. The settlement was years in the making, given that Toyota voluntarily disclosed its violations in 2015.

Consistent with typical practice in large environmental enforcement matters, the government and Toyota likely engaged in extensive negotiations for many months before publicly announcing their settlement. Although Toyota could not have planned for finalization of the settlement to coincide with the end of the Trump administration, it nevertheless may have been fortunate to resolve the case when it did.

The Biden administration is expected to take a much more aggressive stance on environmental issues — including enforcement of environmental laws — than the Trump

administration. Indeed, on his first day in office, President Joe Biden issued an executive order directing all federal agencies to review decisions made during the Trump administration, to ensure consistency with his environmental agenda.[16]

The executive order also instructed federal agencies to consider suspending, revising or rescinding agency actions inconsistent with that agenda.[17] Consistent with this executive order, on Feb. 4, the DOJ announced it was withdrawing numerous Trump-era policies that were seen as impediments to environmental enforcement — the first of what likely will be multiple steps toward a more aggressive approach to enforcement during the Biden administration.[18]

At least in theory, the Biden administration could move to withdraw the proposed consent decree with Toyota, which was negotiated and approved by the prior administration. In light of Biden's day one executive order and recent changes in DOJ policy, the district court could also, *sua sponte*, ask the government to address whether the proposed settlement is consistent with the administration's position on climate change and other emission-related issues relevant to Clean Air Act settlements.

Fortunately for Toyota, such developments are not likely. Biden's executive order and changes in EPA and DOJ leadership likely will not alter the government's position in Toyota's case. The EPA probably approved the key terms of the deal many months ago, and even if the deal had not been finalized prior to Biden's inauguration, the new administration may be reluctant to derail a settlement that was nearly finalized before its tenure began.

If, however, Toyota's case had begun, and been negotiated, during the Biden administration, the company may not have fared as well. The administration has made it clear that confronting climate change is a high priority.

Pollution from mobile sources will be a focus of the administration's climate change efforts. This being the case, companies with any connection to mobile source emissions, whether they be original manufacturers or makers of after-market parts, should prepare for enhanced scrutiny.

Although high-profile policy issues such as emissions standards may grab the spotlight in the near term, the automotive industry should also expect Biden's EPA to devote significant resources to enforcing standards related to mobile sources. The new administration's priorities are yet another reason why companies like Toyota should place a premium on compliance.

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[1] See U.S. Department of Justice, Press Release, Toyota Motor Company to Pay \$180 Million in Settlement for Decade-Long Noncompliance with Clean Air Act Reporting Requirements (January 14, 2021) ("DOJ Press Release"), available at <https://www.justice.gov/opa/pr/toyota-motor-company-pay-180-million-settlement-decade-long-noncompliance-clean-air-act>.

[2] Consistent with Clean Air Act requirements, the DOJ filed the settlement as a proposed

consent decree that was subject to a 30-day public comment and judicial review before being considered final. The proposed consent decree was filed with the court on Jan. 14, meaning that the public had until on or about Feb. 15 to file comments on the settlement; even after such a comment period closes, it may take the court some time to review and approve the settlement. See U.S. v. Toyota Motor Corporation et al., S.D.N.Y. Case. No. 1:21-cv-323, Docket No. 3-1, Proposed Consent Decree ("Consent Decree").

[3] Consent Decree ¶ 8(a).

[4] Id. ¶ 8(h)-(m).

[5] Id. ¶ 8(l).

[6] Id. ¶ 8(o).

[7] Id. ¶ 8(s).

[8] Id. ¶ 8(r).

[9] Id.

[10] Evan Belser, LinkedIn posting regarding DOJ Press Release (Jan. 16, 2021), available at <https://www.linkedin.com/feed/update/urn:li:activity:6755530123396608001/>.

[11] See U.S. v. Toyota Motor Corporation et al., S.D.N.Y. Case. No. 1:21-cv-323, Docket No. 1, Complaint.

[12] Id. ¶ 63.

[13] Id. ¶ 39.

[14] U.S. Department of Justice, Press Release, Manhattan U.S. Attorney Announces Criminal Charge Against Toyota Motor Corporation and Deferred Prosecution Agreement with \$1.2 Billion Financial Penalty (March 19, 2014), available at www.justice.gov/usao-sdny/pr/manhattan-us-attorney-announces-criminal-charge-against-toyota-motor-corporation-and.

[15] Reenat Sinay, Toyota to Pay \$180M Penalty For Clean Air Act Violations (Law360 article published on Jan. 14, 2021), available at <https://www.law360.com/articles/1345113/toyota-to-pay-180m-penalty-for-clean-air-act-violations>.

[16] Protecting Public Health and the Environment and Restoring Science to Tackle the Climate Crisis, Executive Order 13,990 (Jan. 20, 2021).

[17] Id.

[18] The memorandum announcing the DOJ's policy changes can be accessed here: <https://www.justice.gov/enrd/page/file/1364716/download>.