BEFORE THE ENVIRONMENTAL APPEALS BOARD
UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C.

In re:	)
Taotao USA, Inc. Taotao Group Co., Ltd., and Jinyun County Xiangyuan Industry Co., Ltd.	)
Dkt. No. CAA-HQ-2015-8065	)

NOTICE OF APPEAL

Taotao USA, Inc. ("Taotao USA"), seeks review of a decision of Administrative Law Judge Susan L. Biro, issued August 7, 2018, assessing a joint and several civil penalty of $1,601,149.95[1] for violations of sections 203 and 213 of the Clean Air Act, 42 U.S.C. §§ 7522, 7547, and implementing regulations codified at 40 C.F.R. Part 86, Subpart E and 40 C.F.R. §§ 1051, 1068. An appeal brief is attached.

Respectfully Submitted,

/s/William Chu
William Chu
Texas State Bar No. 04241000
The Law Offices of William Chu
4455 LBJ Freeway, Suite 1008
Dallas, Texas 75244
Telephone: (972) 392-9888
Facsimile: (972) 392-9889
wmchulaw@aol.com

Date: September 6, 2018

Attorney for Appellants

[1] Of the total joint and several penalty amount of $1,601,149.95 assessed against Taotao USA, Taotao Group is jointly and severally liable for $247,982.55 and JCXI is jointly and severally liable for $1,353,167.40.

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APPEAL BRIEF

INTRODUCTION

This is an appeal of the Initial Decision of the Administrative Law Judge ("ALJ") assessing a civil penalty of $1,601,149.95[1] for 109,964 alleged violations of sections 203 and 213 (to the extent section 213 permits EPA to enforce emission standards for nonroad vehicles in the same manner as the motor vehicles regulated under section 203 of the CAA), of the Clean Air Act (CAA), 42 U.S.C. §§ 7522, 7547, and implementing regulations codified in 40 C.F.R. Part 86, Subpart E and 40 C.F.R. §§ 1051, 1068.

Judge Biro found that Taotao USA Inc. ("Taotao USA") had violated section 203 of the CAA by importing 67,527 on-road motorcycles manufactured by Taotao Group Co. Ltd. ("Taotao Group"), and violated 40 C.F.R. § 1068 by importing 42,437 nonroad recreational vehicles manufactured by Jinyun County Xiangyuan Industry Co., Ltd. ("JCXI"), none of which were covered by an EPA-issued certificate of conformity (COC). Even though Taotao USA had imported all 109,964 vehicles after securing EPA-issued COCs for those vehicles, the ALJ found that the subject vehicles were not covered by those COCs because they were equipped with catalytic converters containing precious metal concentrations that were not identical to the concentrations stated in their respective COC applications. The ALJ based its decision on the regulations codified in 40 C.F.R. Part 86, Subpart E (regarding on-road vehicles) and 40 C.F.R. §§ 1051, 1068 (regarding recreational vehicles). *See* Initial Decision at 2; Amended Complaint ¶ 23 (a), (b).

For the reasons stated in this brief, the ALJ erred both her liability determination, and her penalty assessment.

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[1] Of the total joint and several penalty amount of $1,601,149.95 assessed against Taotao USA, Taotao Group is jointly and severally liable for $247,982.55 and JCXI is jointly and severally liable for $1,353,167.40.

ISSUES PRESENTED FOR REVIEW

1. Did the ALJ erroneously conclude that all 109,964 on-road and nonroad vehicles were not covered by their respective EPA-issued COCs because they did not conform, in all material respects, to the design specifications in their COC applications, regardless of whether they were identical to their respective engine family's emission data vehicles, which passed end of useful life emission tests?

2. In spite of the DOJ's express condition on the jurisdictional waiver stating that the waiver does not extend to violations do not go beyond mere harm to the regulatory scheme and those that cause excess emissions, did the ALJ erroneously conclude that because harm to the regulatory scheme ultimately leads to potential harm to the environment, the administrative court had jurisdiction over this complaint even though Complainant clearly sought a penalty for harm from actual or potential emissions?

4. Although liability was determined solely based on (i) a finding that the catalytic converters in the imported vehicles did not match the catalytic converters described in their respective COC applications, and (ii) a finding that all 109,964 subject vehicles were uncertified because they contained the same catalytic converters as the emission data vehicles tested for each respective engine families and were therefore all the same, did the ALJ then erroneously conclude at the penalty stage that the imported vehicles had a potential for excess emission because all useful life emission tests were conducted on emission data vehicles that were ***not the same*** as the imported vehicles?

5. Did the ALJ erroneously make a penalty determination based on the Complainant's upward biased penalty calculation without regard to the statutory factors, the language of the Penalty Policy or the DOJ's conditional waiver?

FACTUAL AND PROCEDURAL BACKGROUND

The CAA prohibits manufacturers from selling or offering for sale, introducing or delivering for introduction into commerce, or importing into the United States a vehicle and/or vehicle engine unless it is covered by a certificate of conformity (COC) issued under applicable regulations. 42 U.S.C.§ 7522(a)(1).

To obtain a COC, a manufacturer submits a COC application, along with emissions data collected by conducting emissions tests on an emission data vehicle (EDV) until reaching the end of the engine's "useful life." 40 C.F.R. § 86.437; Initial Decision at 7-9. Once full useful life compliance has been determined, the manufacturer is able to calculate a "deterioration factor" for the engine. Initial Decision at 7-9. A deterioration factor "is a ratio of end-of-life performance to low-hour life emissions performance" that allows a manufacturer "to demonstrate compliance over the products full useful life. *Id.* An emission data vehicle, from which a deterioration factor is determined, must be materially similar to the product that the manufacturer will produce. *Id.* Because an emission data vehicle is tested in conjunction with an original COC application, it is produced in the year preceding the COC. *Id.* However, in case of carry-over applications, which differ from original applications because they seek recertification or renewed certifications, the manufacturer can continue to use the same emissions data from the original EDV, regardless of when it was tested or produced, so long as the vehicles seeking recertification will be materially similar to those EDVs.

The Agency requires both a COC application, to assess whether design specifications meet design and performance standards,[2] and emissions data from a concurrently or previously tested

[2] The her Initial Decision, the ALJ misstates that that regulations set performance limits but not design specifications. Initial Decision at 8. Whereas the regulations in fact do not set any design standards or specifications for catalytic converters, they do set design specifications or standards for other emission-related components. *See e.g.* 40 C.F.R.

EDV, to assess whether the product will meet applicable emission standards throughout its useful life. However, in case of catalytic converters, the Agency has no design standards, nor is it possible to assess a catalytic converters design by simply looking at it. *See* CX176 ("Studies to date have not provided a reliable method or model for determining what emission rate a given catalytic converter with a specified precious metals ratio will achieve in a given application . . . [r]eliable results can only be obtained by testing a catalytic converter's performance. . .")[3] In fact, the only way to test a catalytic converter's performance is to test it for emissions to the end of its useful life. *Id.* Therefore, whereas the Agency may typically rely on a manufacturer's COC application in deciding whether or not a product will remain complaint throughout its useful life, in case of catalytic converters the agency does not, and cannot, assess a catalytic converter's performance based on the "stated" design specifications.

At the liability stage, Judge Biro held that all subject on-road and non-road vehicles were not covered by their COCs because they did not conform in all material respects to the design specifications described in their COC applications, regardless of the stipulated fact[4] that these vehicles conformed to their emission data vehicles. *See* Order on Partial Accelerated Decision and

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1051.245 (a)(2); (e)(1)(i) (setting design specifications that a manufacturer must comply with in certain circumstances).

[3] Agency's expert witness, Dr. Heck's report, which Complainant submitted and the ALJ relied upon in determining liability. *See* Liability Order at 8, 14, 24.

[4] *See* Complainant's Second Motion to Supplement the Prehearing Exchange and Combined Response Opposing Respondents' Motion to Dismiss for Failure to State a Claim and Motion for Accelerated Decision ("Combined Response") at 14-15 (Jan. 3, 2017) (requesting the Presiding Officer treat Respondents' claim that the tested catalytic converters for each engine family were the same as the catalytic converters on the respective imported vehicle as a judicial admission and remove the factual matter from controversy) (citing Respondents' Motion to Dismiss for Failure to State a Claim ("Motion to Dismiss") at 9 (Nov. 28, 2016) (asserting that each catalytic converter relevant to this matter, including the one tested for emissions pursuant to the [pre-import] certification procedure, was the same, and that Complainant does not allege that the catalytic converters that were tested and passed [useful life] emission tests are not the same as the catalytic converters in the imported vehicles); *see also* Liability Order at 30-31 (agreeing with Complainant's position and holding that because Respondents state that "the EDV that passed the emissions standards contained a catalytic converter which conformed to the catalytic converter on imported vehicles… I find there is sufficient evidence to conclude that none of the 109,964 imported vehicles conform to the design specifications of their COC applications.

Related Motions at 29, 31 (May, 3, 2017) (hereinafter "Liability Order"). The ALJ found liability in spite of the stipulated fact that the test emission data vehicles for each engine family, tested for useful life emissions for the purpose of certification, from which the deterioration factors were calculated and results were submitted, were the same as their respective imported vehicles.[5] Yet, after agreeing with Complainant's foregoing position at the liability stage of the proceedings, the ALJ thereafter once again agreed with Complainant at the penalty stage, although this time Complainant took a directly conflicting position and claimed that the emission data vehicles tested by the manufacturer for initial certification, and the deterioration factors calculated therefrom, were not the same as their respective imported vehicles. *See* Initial Decision at 12-13; *see also* Complainant's Post Hearing Brief ("C's Br.") at 8, 9 (arguing that Appellants' vehicles were not covered by "certificates of conformity because they were built using untested catalytic converters..." and the "deterioration factors derived from full-useful life testing [that were] conducted on vehicles other than those identified in the Amended Complaint).

ARGUMENT AND AUTHORITIES

The Agency brought this action against Appellant alleging that based on certain inspections on Taotao USA's imported highway motorcycles and recreational vehicles, the Agency determined that the catalytic converters in those vehicles, and all other imported vehicles belonging to those engine families, did not conform, in terms of precious metal concentrations, to the catalytic converters described in those vehicles' relevant COC applications. *See* Amended Complaint ("Am. Comp.") ¶¶ 33-36. But in order to bring this penalty action, Taotao USA's actions must have been in violation of one or more specific sections of the Clean Air Act. *See* id. ¶ 23; *see also* 40 C.F.R. 22.1.

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[5] *Id.*

The CAA prohibits manufacturers from selling or offering for sale, introducing or delivering for introduction into commerce, or importing into the United States a vehicle and/or vehicle engine unless it is covered by a certificate of conformity (COC) issued under applicable regulations. 42 U.S.C.§ 7522(a)(1). However, because Taotao USA holds EPA-granted COCs for every engine family identified in [the Complaint],[6] in order to establish liability the Agency had the burden to prove that the highway motorcycles and recreational vehicles imported by Appellant were not covered by those EPA-granted COCs for every engine family and class of vehicles. *See* 40 C.F.R. § 22.24.

I. EPA did not meet its burden of proof in demonstrating that Taotao USA imported vehicles in violation of the Clean Air Act, therefore the ALJ erroneously denied Appellants' Motion to Dismiss.

To show that the 67,527 highway motorcycles, and the 42,437 recreational vehicles were not covered under their corresponding EPA-granted COCs, the Complaint alleges that "[b]ecause the catalytic converters do not conform to the ***design specifications*** described in the relevant applications for COCs, the vehicles do not conform in all material respects to the specifications in the COC applications and are therefore not covered by those COCs. Am. Compl. ¶ 37 (emphasis added). In making the foregoing allegation, the Agency relies on the following regulations: 40 C.F.R. §§ 85.2305(b)(l) and 86.437-78(a)(2)(iii), (b)(4) (highway motorcycles), and 40 C.F.R. §§ 1068.101(a)(1)(i) and 1068.103(a) (recreational vehicles).

Although the Complaint clearly refers to the above-mentioned regulations to establish that Appellant violated the CAA, the ALJ's liability order made no reference to these regulations in denying Appellant's Motion to Dismiss and granting Appellee's Motion for Accelerated Decision on Liability. *See generally* Liability Order.

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[6] Am. Compl. ¶ 31.

A. ***Appellant's 67,527 highway motorcycles were covered by their respective EPA-granted COCs in accordance with the governing regulations.***

In regards to the highway motorcycles, for which, according to the Complaint, 40 C.F.R. Part 86 sets emission standards and section 203 or the CAA, 42 U.S.C. *§* 7522, sets compliance provisions,[7] the Agency alleges that subject highway vehicles are not covered by their COCs pursuant to the following regulations: 40 C.F.R. *§§* 85.2305(b)(l) and 86.437-78(a)(2)(iii), (b)(4). Am. Compl. ¶¶ 48, 58, 68, 78. Appellant will go through each of these regulations to show that the error in Complaint and the ALJ's liability determination.

The first regulation cited by the Agency in the Complaint states:

> "Section 203 of the Clean Air Act prohibits the sale, offering for sale, delivery for introduction into commerce, and introduction into commerce, of any new vehicle or engine not covered by a certificate of conformity unless it is an imported vehicle exempted by the Administrator or otherwise authorized jointly by EPA and U.S. Customs Service regulations. However, the Act does not prohibit the production of vehicles or engines without a certificate of conformity. ***Vehicles or engines produced prior to the effective date of a certificate of conformity***, as defined in paragraph (a) of this section, ***may also be covered by the certificate if the following conditions are*** met . . .The vehicles or engines conform in all material respects to the vehicles or engines described in the application for the certificate of conformity"

40 C.F.R. § 85.2305(b)(1) (emphasis added). Section 85.2305(b)(1) provides an exception to 40 C.F.R. § 85.2304 only if the vehicles are produced prior to the effective date of the COC. *Id.* § 85.2305(a) ("***Except as provided in paragraph (b)*** of this section, a certificate of conformity is deemed to be effective and cover the vehicles or engines named in such certificate and produced during the annual production period, as defined in § 85.2304.") (emphasis added). Given that the ALJ made her decision, as stated in her Initial Decision, based on the legal contention that "only after the Agency has evaluated the application and issued a COC for a product model year does the manufacturer begin to build their products consistent with the certificate of conformity they

[7] *Id.* ¶ 23(a)

receive, it is evident that the exception identified in section 85.2305(b)(1) does not apply to these proceedings. The general rule stated in 40 C.F.R. § 85.2304 says nothing about which vehicles are or aren't covered by a COC and rather defines certain terms, such as "annual production period." *See* id. § 85.2304.

The only other regulation cited in the Complaint to show that Appellant's highway motorcycles must conform to the design specifications stated in the relevant COC application states:

> "(a) New motorcycles produced by a manufacturer whose projected sales in the United States is 10,000 or more . . . are covered by the following . . . (2). . . (iii) The certificate will cover all vehicles represented by the test vehicle and will certify compliance with no more than one set of applicable standards."

40 C.F.R. 86.437-78 (a)(ii)(iii).

The foregoing regulation unambiguously states that a certificate will cover all vehicles represented by the test vehicle, not the manufacturer's description. *See* id.; *c.f.* § 86.437-78(b)(4) (in case of small manufacturers, because they are not required to submit test reports and test data,[8] "the certificate will cover all vehicles described by the manufacturer." Furthermore, by providing that the COC only sets one set of standards, a phrase that immediately follows the statement that a certificate covers all vehicle represented by the test vehicle, the regulation implicitly states that in case of differences between the test vehicle or the manufacturer's description, the certified vehicle must comply with the test vehicle.

Although the Complaint also cites 40 C.F.R. § 86.437-78(b)(4), subpart (b)(4) is not applicable to Appellant because it pertains only to small manufacturers, who sell less than 10,000 units in the model year for which certification is sought. *See* Initial Decision at 10; *see also* Am. Compl. ¶¶ 38, 39; CX001-CX010; CX213 (showing that Appellant imported 21,275 highway motorcycles in model year 2012, 28,587 highway motorcycles, in model year 2013, and 17,665 highway motorcycles in model year 2014.

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[8] 40 C.F.R. §§ 86.437-78(b), 86.431-78 (a) ("Data from all tests (including voided tests) performed by a manufacturer with total projected sales in excess of 10,000 vehicles shall be included in the application.

Given that the regulations applicable to highway motorcycles and certification draw clear distinctions between certificates that require test data and those that do not, it is clear that the only instance in which a vehicle must comply with the manufacturer's description to retain its certification is where no test reports or data from emission tests conducted on a test vehicle (EDV) are submitted to the Agency for certification purposes. Otherwise, these distinction would be meaningless.

Because the Agency stipulated, and the ALJ determined liability for all 109,964 vehicles on the finding, that all imported vehicles conformed, in all material respects, to their respective emission data vehicles, there is no dispute that all highway motorcycles (and recreational vehicles) identified in the Complaint conformed to their relevant test vehicles, i.e. EDVs. *See* Complainant's Second Motion to Supplement the Prehearing Exchange and Combined Response Opposing Respondents' Motion to Dismiss for Failure to State a Claim and Motion for Accelerated Decision ("Compl. AD Resp.") at 14-15 (Jan. 3, 2017) (requesting the Presiding Officer treat Appellant's statements on page 9 of their Motion to Dismiss that "the EDVs[9] [Appellants] used to certify each engine family contained catalytic converters which conformed to the catalytic converters equipped on [their] imported vehicles[10]. . . as a judicial admission and remove the factual matter from controversy."); *see also* Liability Order at 30-31 (agreeing with Complainant's position and holding that because Respondents state that "the EDV that passed the emissions standards contained a catalytic converter which conformed to the catalytic converter on imported vehicles… I find there is sufficient evidence to conclude that none of the 109,964 imported vehicles conform to the design specifications of their COC applications."). Because all 67,547 highway motorcycles imported by Appellant had catalytic converters that conformed to the catalytic converters on their

[9] The EDVs referenced are the prototype test vehicles for each engine family used to gather emissions data for certification; the data is submitted with each COC application. *See* Compl. AD Resp. at 13; Respondents' Motion to Dismiss for Failure to State a Claim ("Motion to Dismiss") at 9.

[10] Appellee agreed that the "imported vehicles" Appellant refers to include the 109,964 vehicles identified in the Amended Complaint. Compl. AD Resp. at 14.

respective test vehicles, and test reports and test data for said representative test vehicles were submitted to the Agency prior to the production of these subject vehicles, they are covered by their EPA-granted COCs.

The ALJ's liability determinations in this case were based not on the language of the regulatory authority cited in the Complaint, Liability Order at 25-29, but on the language on the face of the COC. As such, said language is not a regulation, not mandated by statute, in fact it conflicts with the language of the applicable regulation, i.e. the one that forms the basis of the Complaint. *See* 40 C.F.R. 437-78(a)(2)(iii). The language on each of the COCs issued for the highway motorcycles is as follows:

> . . . this Certificate is hereby issued with respect to test vehicles which have been found to conform to the applicable requirements of 40 CFR Part 86 and which represent the motor vehicle models listed above by engine family and permeation/evaporative family, more fully described in the manufacturer/importer's application for certification. Vehicles covered by this Certificate have demonstrated compliance with the applicable emission standards, ***as more fully described in the manufacturer/importer's application***. This Certificate covers the above models, which are designed to meet the applicable emission standards specified in 40 CFR Part 86 as specified in the manufacturer/importer's application . . . This Certificate covers only those vehicles which conform, in all material respects, to the design ***specifications that applied to those vehicles described in the documentation*** required by 40 CFR Part 86 and are produced during the model year production period stated on the Certificate as defined in 40 CFR Part 86…

CX043-CX046.

Although the ALJ made her decision based solely on the last sentence quoted above, a closer look at the language shows that the COC only requires that each vehicle conform to the design specifications that applied to those vehicles in the "documentation" required by 40 CFR Part 86. However, as previously explained, when a COC is issued with respect to test vehicles and test data, the vehicles must comply with the test vehicle, and only when the COC is issued without such test data, the vehicle must comply with the COC application. Furthermore, nowhere does 40

C.F.R. Part 86 require that the manufacturer describe the precious metal concentrations of the catalytic converter, only that members of an engine family "must be identical" in "[t]he number of catalytic converters, location, volume, and composition." 40 C.F.R. § 86.420-78(b)(7). Here the catalytic converters on all imported highway motorcycles were identical to their test vehicles, and therefore they were all the same. *See* Compl. AD Resp. at 14-15; Liability Order at 31. Finally, the regulation that required that specific language on the face of each COC has since been deleted. *See* Respondents' Response to Complainant's AD Motion at 10-14.

B. ***Appellant's recreational vehicles were covered by their respective EPA-granted COCs in accordance with the governing regulations.***

In case of recreational vehicles, for which, according to the Complaint, 40 C.F.R. Part 1051 sets emission standards and 40 C.F.R. Part 1068 sets compliance provisions,[11] the Agency alleges that subject highway vehicles are not covered by their COCs pursuant to the following regulations: 40 C.F.R. §§ 1068.101(a)(1)(i) and 1068.103(a). Am. Compl. ¶¶ 87, 97, 107, 117, 125, 133.

The Complaint is premised on the allegation, and regulation, that " Engines/equipment covered by a certificate of conformity are limited to those that . . . conform to the specifications described in the certificate and the associated application for certification." 40 C.F.R. 1068.103(a). Yet, the Agency ignores the very next sentence that precedes the above-quoted language, which defines the term "specifications." *Id.* ("For the purposes of this paragraph (a), 'specifications' includes the emission control information label and any conditions or limitations identified by the manufacturer or EPA.).[12] Nowhere in all the emission control information ("ECI") specified

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[11] Id. ¶ 23(b)

[12] The ALJ took the position that the applicable regulation is not the one that is current now, or was current at the time of her liability decision, but rather one that existed prior to December 2016, which did not include "the emission control information label" but was otherwise the same.

on each ECI label attached to all the vehicles identified in the Complaint, is there any mention of the precious metal concentrations, nor is such "mention" required. See e.g. CX006 at EPA-000196. Furthermore, none of the conditions or limitations identified by the manufacturer make any mention the catalytic converter's precious metal concentrations. See e.g. id at EPA-000205. Finally, that EPA does not have any catalytic converter design standards or specifications. Initial Decision at 8.

Therefore, unlike cases where certain design specifications are required, i.e. EPA standards such as those required in order to demonstrate compliance with evaporative emission standards,[10] and information that must be included; or cases where the parts equipped onto the EDV were different from the parts on the production vehicles, *see e.g. United States v. Chrysler Corp.*, 591 F.2d at 960, n.3., the present matter involves no such facts. Because the recreational vehicles involved materially conformed to all "specifications" described in the COC application, as the term is defined in the relevant regulation, and it is undisputed that the recreational vehicles conformed to their respective test vehicles, *see* Compl. AD Resp. at 14-15, all recreational vehicles imported by Appellant into the U.S. were covered by a valid COC.

II. The ALJ erred by making liability determinations based upon findings that the subject vehicles did not conform to the vehicles described in the COC applications, even though they confirmed to their certification EDVs, and making penalty determinations based on conflicting findings.

As more fully discussed above, there is no allegation in the Complaint that the catalytic converters in the subject vehicles did not conform to the catalytic converters of the relevant emission data vehicles of each engine family the vehicles belonged to. *See generally* id.; *see also* Liability Order at 29 (the issue is "whether the catalyst levels in Respondents' vehicles matched what was claimed on their COC applications, not whether they matched the catalyst levels of their emissions-data vehicles … ." Even if such an allegation were made, which it clearly wasn't, the

Agency stipulated that all imported vehicles conformed, in all material respects, to their respective emission data vehicles. *See* Complainant's Second Motion to Supplement the Prehearing Exchange and Combined Response Opposing Respondents' Motion to Dismiss for Failure to State a Claim and Motion for Accelerated Decision ("Compl. AD Resp.") at 14-15 (Jan. 3, 2017) (requesting the Presiding Officer treat Appellant's statements on page 9 of their Motion to Dismiss that "the EDVs[13] [Appellants] used to certify each engine family contained catalytic converters which conformed to the catalytic converters equipped on [their] imported vehicles[14]. . . as a judicial admission and remove the factual matter from controversy.").

Because the Complainant has the burdens of presentation and persuasion that the violation occurred ***as set forth in the Complaint*** and that the relief sought is appropriate, 40 C.F.R. § 22.24 (emphasis added), and the only violation set forth in the Complaint is that the catalytic converters in the subject vehicles do not match the design specifications described in the relevant COC applications, any liability, and consequently the penalty, determinations shall be based solely on the violation as set forth above. Because the Complaint never alleges that the subject vehicles did not match their certification EDVs, and any controversy as to the fact that the subject vehicles did conform to their certification EDVs was expressly removed from controversy, therefore the Agency could not make penalty determinations, and the ALJ could not accept those determinations, based on unalleged violations, and which are contradicted by uncontroverted (stipulated) facts. Therefore any penalty arguments and determinations, premised upon the an allegation that the emissions data submitted to the Agency with each COC applications was

[13] The EDVs referenced are the prototype test vehicles for each engine family used to gather emissions data for certification; the data is submitted with each COC application. *See* Compl. AD Resp. at 13; Respondents' Motion to Dismiss for Failure to State a Claim ("Motion to Dismiss") at 9.

[14] Appellee agreed that the "imported vehicles" Appellant refers to include the 109,964 vehicles identified in the Amended Complaint. Compl. AD Resp. at 14.

acquired from the testing of a different catalytic converter is clearly erroneous. *See* 40 C.F.R. § 22.24 (Each ***matter of controversy*** shall be decided by the Presiding Officer upon a preponderance of the evidence) (emphasis added); *see also* Complainant's Post-Hearing Brief ("Compl. Br.") at 8 ("[Appellants imported or sold 109,964 vehicles that were not covered by Certificates of Conformity because they built using ***untested catalytic converters***...No emission tests were conducted on vehicles belonging to Counts 9 and 10. . . [Appellants caused the program significant harm by circumventing the pre-import, pre-sale certification process. . . [a]s a consequence 109,964 vehicles with ***untested useful life emissions*** are operating in the United States.") (emphasis added); *c.f.* Compl. AD Rep. at 13-15.

Even though the ALJ clearly stated in her Liability Order that the issue is "whether the catalyst levels in [Appellants'] vehicles matched what was claimed on their COC applications, not whether they matched the catalyst levels of their emissions-data vehicles...," the ALJ in her Initial Decision took a different stance. Liability Order at 29; *see also* Initial Decision at 12, 25 (finding that Appellant harmed the regulatory scheme by causing a risk of potential emissions because even though all subject vehicles passed low-hour emissions tests, their deterioration factors were based on EDVs that had different catalytic converters than those on the imported vehicles, and the useful life emissions tests were unreliable because they were performed on a vehicle built in a different model year).

The ALJ found that the useful life emissions were unreliable because "the Agency correctly points out, "all of the engine families named in the Amended Complaint relied on an EDV from a previous model year for certification, meaning the EDVs were not manufactured at the same time as the production vehicles... thus, performance characteristics of the EDVs cannot

be presumed to apply to vehicles in this case based on a shared production process." Initial Decision at 32. Such a finding makes no sense given that all test vehicles are tested in the previous year because a COC application and test data is submitted prior to the beginning of the model year. *See* CX001-CX010; *see also* Initial Decision at 9 ("only *after* the Agency has evaluated the application *and* issued a COC for a product model year does the manufacturer "begin to build their products consistent with the certificate of conformity they receive.").

III. The penalty exceeds the Clean Air Act's jurisdictional limitations, and in this case there was no potential for excess emissions.

The $1,601,149.95 proposed penalty sought is larger than statutory maximum permitted in administrative proceedings, and exceeds the bounds of the waiver of the statutory limits in this case.

The Clean Air Act ("CAA or the "Act") unambiguously limits the amount of penalty that may be sought against a violator in a penalty assessment proceeding. CAA § 205(c)(1). The language of the Act makes clear that the limitation is not only on the amount recovered, but the amount "sought" in an administrative proceeding. *Id.* Here Complainant sought a penalty of $1,601,149.95, which was the penalty assesses in the Initial Decision. The Agency could only bring this action against Respondents if the Administrator and the Attorney General jointly determined that larger penalty amount in this matter was appropriate for administrative penalty assessment. CAA § 205(c)(1). During the prehearing stage of this action, Complainant presented evidence to show that the DOJ had agreed to waive the CAA jurisdictional limits. *See* CX028 at EPA-000546-47. However, said waiver of the CAA's jurisdictional limitations is not unconditional. *Id.* In fact, the DOJ waiver expressly limits the penalty assessment in this matter to violations "that harm the regulatory scheme, but do not cause excess emissions;" and

violations of "provisions on certification, labeling, incorrect information in manuals, or warranty information violations." *See* CX028 at EPA-000546-47. The DOJ waiver explicitly excluded violations:

> "***--that go beyond mere harm to the regulatory scheme***; ***--that cause excess emissions***; -- that are other than violations of provisions on certification, labeling, incorrect information in manuals, or warranty information violations; or ***--that are willful, knowing***, or otherwise potentially criminal; or --that increase the aggregate number of waived vehicles in the matter to over 125,000 total."

Id. (emphasis added). The statute governing administrative assessment of penalties does not use the term "regulatory scheme", instead the foregoing language likely comes from the Clean Air Act Mobile Source Civil Penalty Policy ("Penalty Policy"). *See* Complainant's Ex. 22 at EPA-000465.

At the evidentiary hearing, Complainant presented Ms. Isin, who calculated the proposed penalty in this matter. *See* Transcript of Proceedings (Tr.) at 556-57. Complainant attempted to satisfy the agency's burden of proving the reasonableness of the proposed penalty through Ms. Isin's testimony on how she applied the Penalty Policy to come up with the relief sought. *Id.* Ms. Isin's testimony, however, entirely defeats Complainant's claim that the penalty sought is appropriate. Ms. Isin admitted at the hearing that the proposed penalty is not solely based on harm to the regulatory scheme, but instead includes amounts attributable to actual or potential harm to the environment. *See* Tr. at 841. Ms. Isin further testified that the proposed penalty includes amounts attributable to willfulness and negligence. *See* Tr. at 601 ("We adjusted the penalty by 20 percent upward for willfulness *and* negligence.") (emphasis added). Ms. Isin testified that when she speaks of "willfulness or negligence" she is "describing something that could have been prevented…something the Respondent knew or should have known to prevent." *See* Tr. at 706.

Because the proposed penalty is based on harm to the environment, in addition to any harm to the regulatory scheme, and makes adjustments for conduct that Complainant deems willful and "knowing," it directly violates the express conditions of the DOJ's waiver. *See* CX28 at EPA-000546-47. Yet, the ALJ determined that the penalty does not exceed the statutory waiver because the risk of excess emissions created by the failure to have valid COCs also harmed the regulatory scheme as the scheme was designed to prevent such risks; and because "it is clear from the context of the DOJ authorization and use of the phrase "or otherwise potentially criminal" that the "willful" or "knowing" prohibition applies to enforcement actions arising in a criminal context, or to violations requiring a scienter element. *See* Initial Decision at 31, 38.

In support of the conclusion that regulatory scheme includes risk of emissions, the ALJ points to cases such as those which state preventing harm is part of a valid regulatory scheme. Initial Decision at 31. However, the cases cited in the Initial Decision are clearly distinguishable in light of the DOJ waiver, which does not only limit the penalty to violations that harm the regulatory scheme, but also expressly excludes any violations that go beyond "mere harm to the regulatory scheme.

Furthermore, even if the risk of excess emissions were covered by the DOJ waiver, in this case, the evidence shows that there is no risk of potential harm. All arguments made by the agency, which the ALJ relied upon, are based on allegations that the Agency had no way of determining how the subject vehicles would perform throughout their full useful life. However, those concerns are irrelevant because the catalytic converters installed on the imported vehicles were representative of their test vehicles, which passed full useful life emissions. The model year of the test vehicle is irrelevant because the regulations expressly permit the use of test vehicles built prior to certification, and in case of carry-over applications, the year preceding the original application.

Based on the foregoing, Appellant imported vehicles that were in fact covered by their EPA-granted COCs, the test reports and test data submitted to the Agency was accurate and based on a catalytic converter representative of the imported vehicles, and therefore the Agency's liability and penalty determinations are erroneous.

III. The Penalty does not accurately follow the Penalty Policy.

The Penalty Policy states that in case of violations that harm the regulatory program, but do not cause excess emissions, the importance of the requirement to the regulatory scheme should be considered in determining egregiousness, *see* CX022 at EPA-000469; because egregiousness is the second step in the gravity calculations, s*ee* C's Br. at 10, the Penalty Policy appears to eliminate the first step entirely for said violations. It makes sense to eliminate this step, given that base gravity calculations in the Penalty Policy rely on harm from potential emissions. *See* CX022 at EPA-000466. Here, Complainant incorrectly calculated the base gravity, first, by relying on horsepower, and then, by failing to limit the base gravity to $500. *See* CX213, EPA-002808–11 (the base-per-vehicle gravity for counts 2, 9 and 10 is $589.60, count 6 is $552, and counts 5 and 8 is $669.60).

Next, Complainant adjusted the base-per-vehicle penalty for egregiousness, categorizing the violations in Counts 9 and 10 as "Major", and applying a 6.5 multiplier, on the ground that there is no information about the emissions from the vehicles in counts 9 and 10. *Id.* at 10-11. At the same time, Complainant admits that there is no allegation in this action, nor evidence, that the violations caused excess emissions, and that an increase in penalty on the basis of excess emissions is not, and cannot be, sought. *See* id. at 11 n.1. Complainant also states that violations are "Moderate" (multiplier of 3.25) if they involve uncertified vehicles, and "the emissions from the vehicles . . . are likely to be similar to emissions from certified vehicles." *Id.* at 10-11. Given that there is no allegation or evidence of excess emissions, and penalty cannot be increased for

emissions, Complainant's claim that a lack of information on emissions justifies a two-fold increase in adjusted base gravity then strains logic. What's even more bewildering is that Complainant has previously stipulated that the useful life emission test results submitted with each of the ten COC applications in this case had the same catalytic converters as those on the 109,964 imported vehicles, therefore, there is information on emissions from counts 9 and 10, which shows that these vehicles do not exceed emissions. *See infra* 9-12; *see also* Complainant's Second Motion to Supplement the Prehearing Exchange and Combined Response Opposing Respondents' Motion to Dismiss for Failure to State a Claim and Motion for Accelerated Decision ("Combined Response") at 14-15 (Jan. 3, 2017). Complainant therefore should have used "Moderate" egregiousness for all counts, if an increase based on potential emissions was permitted. However, because excess emissions cannot be considered and Complainant has failed to show how the harm to the regulatory scheme is egregious, all violations should be characterized as "Minor." *See* Rs' Br. at 12.

Setting aside the EPA-DOJ waiver for a moment, had Complainant simply followed the Penalty Policy by grouping all counts together for scaling purposes, *see* id. at 12-15, capping base-per-vehicle gravity at $500, and categorizing counts 9 and 10 at "Moderate" egregiousness, the gravity component of the proposed penalty would go down from $1,381,850.95 to approximately $693,455.20.[2] *See* CX213 at EPA-002808–11; CX022 at EPA-000467, EPA-000469-72.

Additionally, if Complainant had followed the EPA-DOJ waiver, at least to the extent that it prohibits an assessment for willful and knowing conduct, and removed that portion of the proposed penalty that Complainant admits is attributable to Respondents' willfulness ***and*** negligence, see Tr. at 106, CX213 at EPA-002808–11, Complainant's gravity component would further go down to approximately $594,390.16 (more vehicles would be scaled at 0.0016 and

000.32). As for the economic benefit portion of the proposed penalty, Complainant admits that "[t]he Penalty Policy states that where violations arise from missing or nonconforming catalysts, as in this case, 'the cost of purchasing and installing the catalytic converter' is an appropriate measure of the violator's economic benefit, and stipulates that the net present value of the cost of purchasing the certified catalytic converters in $114,338. See C's Br. at 6 (emphasis added); CX022 at EPA-000462; Respondents' Exhibit ("RX") 1 at 19, 31 (Addendum). Yet, Complainant seeks an economic benefit of $219,299 on the ground that "additional staffing would be a necessary component for measuring Respondents' economic benefit as the avoided cost of using catalytic converters that conformed to the certified specifications." See C's Br. at 6-7 (referring to Jonathan Shefftz report). However, had Respondents used catalytic converters with the certified specifications, there would be no avoided costs, and the economic benefit would be $114,338; not to mention, Mr. Shefftz admits that by adding the additional staffing component to scenarios two through four, he took a "more aggressive approach or a more upwardly-biased approach..." See Tr. at 898. On the other hand, Respondents could have simply listed the correct catalytic converter concentrations on the COC applications, and given that the EDVs with the uncertified catalytic converters passed the useful life emissions and the Agency's decision to approve the design specifications could have only been based on those tests, see infra 9-12; see also 40 CFR § 86.435-78, the only economic benefit would then be the cost of additional staffing alone. See RX1 at 1; Tr. at 866-7.

Therefore, the facts show that Respondents, by spending $104,961 on additional staffing could have listed the correct specifications and avoided the violations; while the Penalty Policy suggests that the economic benefit in this case should be $114,338. *See* RX1 at 1, 14; CX022 at EPA-000462. Complainant cannot seek an economic benefit that is not supported by the facts, nor

prescribed by the Penalty Policy, simply because it's a possible economic benefit provided by an expert. Had Complainant accurately calculated the economic benefit component pursuant to the Penalty Policy, the total proposed penalty would go from $1,601,149.95 to either $699,351.16 or 708,728.16.

However, as mentioned above, even the reduced penalty, resulting from an accurate calculation of the Penalty Policy framework, would still be inappropriate because Complainant cannot assess a penalty based on harm from excess emissions. *See* CX028 at EPA-000546-47; C's Br. at 11 n.1. Therefore, because the penalty cannot be increased on the basis of excess emissions, it makes no sense to calculate the penalty by relying on methods provided to calculate harm from potential emissions. *See* C's Br. at 7-11. It is important to note that the Penalty Policy only provides the method for calculating potential harm from excess emissions because "the amount of excess emissions attributable to the violation(s)- may not be known with certainty." *See* CX022 at EPA-000466. The calculations for potential harm, in the Penalty Policy, are not provided to distinguish between situations where there are actual excess emissions, and situations where there are no emission-related violations; rather calculations of potential harm are provided as an alternative to determining actual emissions "because precise quantification would require emissions testing of the uncertified engines which is time-consuming, resource-intensive, and may not be possible if the subject engines are not in EPA's or the violator's possession." *Id.* Potential harm is therefore calculated when the violations do cause excess emissions, but there is no evidence, or reliable evidence, of said excess emissions. There is no such thing as potential harm in the absence of excess emissions, only potential harm in the absence of ***evidence*** of excess emissions. *Id.*

Contradicting its own claim that penalty was not increased on the basis of excess emissions (C's Br. at 11, n.1), Complainant admits that violations for which the proposed penalty is assessed

[purportedly] caused harm to the Act's certification program ***and*** created the potential for environmental harm in the form of excess emissions of pollutants. *See* C's Br. at 8 (emphasis added). On one hand, Complainant argues that the proposed penalty calculation fits within the bounds of the DOJ waiver because the chosen egregiousness multiplier is not based on excess emissions, *see* id. at 11, n. 11, while on the other hand, Complainant justifies the substantial gravity component of the proposed penalty on the grounds that Respondents' violations caused actual or potential emissions which harmed, or could have harmed, human health and the environment. *Id.* at 7-8. Complainant therefore fails to understand the difference between harm to the program and harm to the environment, a distinction that is clearly understood and drawn by the DOJ in granting the waiver, as well as in the Penalty Policy. *See* CX028 at EPA-000546–47; CX022 at EPA-000465. Complainant is under the misguided impression that the EPA-DOJ waiver permits penalty assessment for violations that cause potential excess emissions (or potentially harm the environment from excess emissions), so long as the penalty is not based on actual excess emissions. *See* C's Br. at 8-9, 11, n. 1. By doing so, Complainant considers only some of the language in the DOJ waiver, while ignoring the rest. *See* CX028 at EPA-000546-47; *see also* Order Denying Respondents' Motion to Dismiss for Lack of Subject Matter Jurisdiction at 19 n. 21; Tr. at 138. The DOJ waiver clearly says that the waiver is limited to violations "that harm the regulatory scheme, but that do not cause excess emissions." *See* CX028 at EPA-000546. The DOJ waiver further explains that the violations that are not covered by the waiver are those that "go beyond *mere* harm to the regulatory scheme." *Id.* at EPA-000546-7 (emphasis added). The use of the word "mere" clearly shows that the scope of the DOJ waiver is limited to only harm to the regulatory program, i.e. the certification program. It cannot include harm from anything that does not constitute harm to the regulatory scheme. Stated differently, Complainant cannot assess a

penalty, or increase the penalty, on the basis that the violations cause, or potentially cause, harm from excess emissions, and that the violations were a result of willful or knowing conduct. *Id.*

Complainant is attempting to unilaterally expand the scope of the waiver by insinuating that "harm to the regulatory scheme" inherently includes harm to human health or to the environment from excess emissions because the function of the regulatory program is to protect human health and the environment. *See* C's Br. at 8. But under that logic, the conditions set in the EPA-DOJ waiver, and in turn the statutory waiver requirements, would be rendered meaningless because Complainant could, as it has, calculate the penalty in this case for harm from excess emissions, as an extension to harm to the regulatory scheme, and disregard the very basis of the DOJ's determination to waive CAA limitations. Perhaps, foreseeing such a possible blatant disregard of the DOJ's conditions on this administrative action, the EPA-DOJ waiver, not only includes the word "mere", but goes further and broadly prohibits harm from excess emissions, without drawing a distinction between actual and potential emissions. *See* CX028 at EPA-000546-7 (limiting the waiver to violations that "harm the regulatory scheme, but that do not cause [actual or potential] excess emissions.").

Respectfully Submitted,

/s/William Chu
William Chu
Texas State Bar No. 04241000
The Law Offices of William Chu
4455 LBJ Freeway, Suite 1008
Dallas, Texas 75244
Telephone: (972) 392-9888
Facsimile: (972) 392-9889
wmchulaw@aol.com

Date: September 6, 2018

Attorney for Appellants

CERTIFICATE OF SERVICE

I certify that a copy of the foregoing instrument was sent this day via electronic mail to the following e-mail addresses for service on Complainant's counsel: Edward Kulschinsky at Kulschinsky.Edward@epa.gov, Robert Klepp at Klepp.Robert@epa.gov, and Mark Palermo at Palermo.Mark@epa.gov.

Date:09/06/2018

/s/William Chu
William Chu