**UNITED STATES**
**ENVIRONMENTAL PROTECTION AGENCY**
**BEFORE THE ADMINISTRATOR**



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| In the Matter of: | ) | |
| | ) | |
| Taotao USA, Inc., | ) | Docket No. CAA-HQ-2015-8065 |
| Taotao Group Co., Ltd., and | ) | |
| Jinyun County Xiangyuan Industry Co., Ltd. | ) | |
| | ) | |
| Respondents. | ) | |

**BUSINESS CONFIDENTIALITY ASSERTED**

The exhibits submitted with Complainant's Rebuttal Prehearing Exchange contain material claimed to be confidential business information ("CBI") pursuant to 40 C.F.R. § 2.203(b). The material claimed as CBI are Complainant's Exhibits CX161 to CX166. Exhibits CX161 to CX163 consist of unsigned federal tax returns submitted to the EPA by respondents Taotao USA, Inc., Taotao Group Co., Ltd., and Jinyun County Xiangyuan Industry Co., Ltd. (collectively, "Respondents"). Exhibit CX164 consists of an OBD-500C Form, Financial Statement of Corporate Debtor, completed by Taotao USA, Inc., and CX165 consists of unaudited financial statements for Taotao USA, Inc. Exhibit CX166 displays the volume and declared value of Taotao USA, Inc.'s imports from 2009 to 2015. These exhibits are therefore filed under seal pursuant to 40 C.F.R. § 22.5(d).

In addition, Exhibit CX167 consist of reference material subject to copyright and placed in the record under the fair use doctrine. To protect the commercial interest of the copyright holder this Exhibit is also filed under seal.

A complete set of the all exhibits, and a set in which the exhibits containing CBI and copyright material are omitted, have been filed with the Hearing Clerk. If you have any questions, please contact Edward Kulschinsky at (202) 564-4133, or at kulschinsky.edward@epa.gov.

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| Respondents. | ) | |

## COMPLAINANT'S REBUTTAL PREHEARING EXCHANGE

The Director of the Air Enforcement Division of the U.S. Environmental Protection Agency's Office of Civil Enforcement ("Complainant") files this Rebuttal Prehearing Exchange, consistent with section 22.19 of the Consolidated Rules of Practice Governing the Administrative Assessment of Civil Penalties and the Revocation/Termination or Suspension of Permits ("Consolidated Rules"), and with the Prehearing Order issued by this Tribunal on May 11, 2016, as amended. Complainant may amend or supplement this Rebuttal Prehearing Exchange as provided by sections 22.19(f) and 22.22(a)(1) of the Consolidated Rules.

Initially, Complainant notes that on October 6, 2016, Complainant filed a Notice of Discrepancy stating, in part, that the Respondents' Prehearing Exchange identified six potential witnesses, but only included a summary of one witness's expected testimony, in contravention of 40 C.F.R. § 22.19(a)(2)(1). Complainant identified other discrepancies having to do with exhibits that Respondents submitted with their Prehearing Exchange and served on Complainant's counsel, and requested that the Tribunal take action to resolve any ambiguity the discrepancies created in the record.

**A. Potential Witnesses**

In addition to the potential witnesses identified in Complainant's Initial Prehearing Exchange, Complainant may call any or all of the following witnesses at the evidentiary hearing in this matter. Complainant may supplement this list, upon adequate notice to the Tribunal and to Respondents, should information reveal the need for additional or alternative witnesses.

1. Emily Chen. Environmental Engineer, Gasoline Engine Compliance Center ("GECC"), Office of Transportation and Air Quality ("OTAQ"), Office of Air and Radiation ("OAR"), EPA. Ms. Chen is technical staff whose duties include review of applications for EPA Certificates of Conformity ("COCs") submitted for gasoline-powered engines like those at issue in this matter. Ms. Chen may testify as a fact witness about Respondents' COC applications, and about the confirmatory test orders her office issued to Respondent Taotao USA.

**B. Documents and Exhibits**

See Exhibit CX000-1, titled "Complainant's Prehearing Exhibits," for a list of the exhibits that Complainant may introduce at hearing, including those added by this Rebuttal Prehearing Exchange. Exhibits CX000 through CX160 were provided with Complainants Initial Prehearing Exchange. Exhibits CX161 through CX169 are added by this Rebuttal Prehearing Exchange. Copies of the exhibits added by this Rebuttal Prehearing Exchange are provided in tandem with this Rebuttal Prehearing Exchange. Each exhibit is labeled as prescribed by the Prehearing Order, and the pages of each exhibit are bates-stamped in sequential numerical order.

**C. Location of Hearing**

Complainant does not at this time oppose Respondents' request that Respondents' witnesses be allowed to appear via video conference or testify in a deposition, if the Tribunal chooses to hold the hearing in this matter in Washington, D.C. Complainant will work with Respondents to make appropriate arrangements for such alternate methods of testimony. If the hearing in this matter is not held in Washington, D.C., Complainant may request that certain of its witnesses be allowed to appear via video conference or testify in a deposition.

**D. Statement Concerning Respondents' Arguments in Support of Their Defenses**

Respondents make several arguments in support of their defense. Complainant contests these arguments, and will fully address them in forthcoming motions or briefs, and at hearing, as appropriate.

**E. Statement Concerning Respondents' Arguments Regarding Penalty**

Respondents make several arguments concerning the proposed penalty in this matter. Complainant contests these arguments, but in this Rebuttal Prehearing Exchange Complainant will limit its response to a few of the points Respondents raise. Complainant will fully address Respondents' arguments and defend its penalty calculation in forthcoming motions or briefs, and at hearing, as appropriate.

**1. Economic Benefit**

In calculating the proposed penalty, Complainant utilized the "rule of thumb" method of calculating the economic benefit Respondents obtained through their noncompliance, as described in the EPA's Clean Air Act Mobile Source Civil Penalty Policy (the "Penalty Policy").[1] *See* Complainant's Initial Prehearing Exchange ("IPHE") at 9-10. The rule of thumb method has been repeatedly used in administrative enforcement cases under the CAA. The rule is based on EPA's observation, developed through its enforcement expertise, that the cost of emission controls is "roughly proportional to the engine size." Penalty Policy at 8–9. The Penalty Policy explains that the rule is appropriate to use when information regarding the actual economic benefit is not available; and is generally appropriate for cases involving "missing emission controls and similar types of violations" and "cases where uncertified vehicles or engines are introduced into commerce or imported (*i.e.*, where economic benefit is delayed and/or compliance expenditures are avoided)." Penalty Policy at 4, 8, 11. In this case, information

[1] The Penalty Policy appears in the record as Exhibit CX022, and is available to the public at http://www2.epa.gov/sites/production/files/documents/vehicleengine-penalty-policy_0.pdf (last visited August 9, 2016).

regarding the actual economic benefit is not available, and the violations involve missing emission controls on uncertified vehicles that have been imported and introduced into commerce. Complainant employed the rule of thumb when calculating the proposed penalty and assessed the minimum economic benefit allowable for that method under Penalty Policy, $15 per vehicle. IPHE at 9–10; Penalty Policy at 8–9.

Citing the Penalty Policy, Respondents contend that use of the rule of thumb is not appropriate in this case because a hearing is likely to occur on the amount of the penalty. Respondents' Joint Prehearing Exchange ( "Respondents' PHE") at 6. The Penalty Policy states that the rule of thumb method *generally* should not be used in circumstances where a hearing is likely on the amount of the penalty. Here, however, the rule of thumb provides a simple formula to calculate the economic benefit that results from introducing into commerce or importing uncertified vehicles and will provide a substantially accurate estimate of the economic benefit of the violations. These circumstances warrant an exception to the general limitation referred to in the Penalty Policy.

Respondents also argue that the penalty should not include an economic benefit component because any "benefit was *de minimis*." *Id.* Respondents' argument mischaracterizes the nature of the economic benefit in this case, economic benefit consists of three components: delayed costs (e.g. deferred capital expenses or one-time non-depreciable costs); avoided costs (e.g. benefits from the failure to install pollution controls or the importation of uncertified vehicles); and benefits "from business transactions that would not have occurred but for the illegal conduct, and/or the competitive advantage the violator obtained in the marketplace as compared to companies that have complied with the motor vehicle emission control laws and regulations." Penalty Policy at 5–7. In this case, Respondents avoided costs by failing to install pollution controls on their manufactured vehicles containing precious metals in the amounts or ratios specified in the vehicles' applications for Certificates

of Conformity, and failing to have an adequate compliance assurance program in place for manufactured vehicle testing and for identifying precious metals amounts or ratios as specified in the vehicles' applications for Certificates of Conformity. Respondents then benefited by importing and selling uncertified vehicles into United States commerce, where they competed with other manufacturers' certified vehicles. As to the sales of uncertified vehicles, EPA has consistently found the appropriate penalty for the sale of a prohibited product is the net profits accruing from that sale. Penalty Policy at 7.

**2. Egregiousness**

Respondents appear to argue that the violations in this matter should be assessed at the "moderate" egregiousness level, rather than "major," because emissions data for the vehicles shows they do not exceed emissions standards. Respondents' PHE at 6–7. The Penalty Policy states that violations should generally be assessed as "major" if they are likely to result in excess emissions. Penalty Policy at 13. The Penalty Policy goes on to state: "engines with missing or defective catalytic converters would be expected to have emissions that are greater than those on which proper catalytic converters had been installed." *Id.* In this case Respondents violated the Clean Air Act by equipping their vehicles with catalytic converters that did not contain precious metals in the amounts or ratios specified in the vehicles' applications for Certificates of Conformity ("COC applications").

As set forth more fully in Complainant's Initial Prehearing Exchange, Complainant assessed six of the ten counts at the "moderate" egregiousness level. IPHE at 10. Counts 1 and 2 were assessed at the "major" egregiousness level because information in the record shows that emissions test results for the vehicles selected for testing from the engine families identified in those counts exceeded emissions standards. *Id.*; *see* CX108 (test vehicle exceeded emissions standard for carbon monoxide (CO)); CX134–CX139 (confirmatory test orders and results showed emissions that exceeded the emissions standard for CO). Counts 9 and 10 were assessed at the "major" egregiousness level because the EPA

does not have information about the emissions from the uncertified vehicles labeled as belonging to the engine families identified in those counts, and the violation is one that would be expected to result in excess emissions. IPHE at 10; *see* Penalty Policy at 13.

**3. Gravity & Upward Adjustment for Failure to Remediate**

Respondents argue that a gravity penalty and upward adjustment for failure to remediate are not warranted because they claim "there is no evidence of any violations of the emission standards." Respondents' PHE at 7. Respondents also contend that any violations were unintentional, and a penalty will therefore not provide them with any incentive to change their behavior to comply with the Clean Air Act. *Id.* Respondents go further to argue that the Penalty Policy should not apply to them in this case because, again, they claim there is no evidence of emissions exceedances. *Id.* Respondents' arguments are without merit.

The Penalty Policy applies to violations of Title II of the Clean Air Act, including "the manufacture and sale, or the importation, of uncertified vehicles or engines in violation of Section 203(a)(1) of the Act, 42 U.S.C. § 7522(a)(1), and relevant implementing regulations. Penalty Policy at 1. Complainant alleges that Respondents manufactured, sold, or imported into the United States approximately 109,964 uncertified vehicles in violation of Section 203(a)(1) of the Act, 42 U.S.C. § 7522(a)(1). Amended Complaint ¶¶ 36–38, 49, 59, 69, 78, 88, 98, 108, 118, 126, 134. The Penalty Policy applies to these violations, and accounts for violations' emissions consequences through the use of an "egregiousness" multiplier applied to the gravity of component of a penalty. Penalty Policy at 1–2, 13–14. As explained part E.2 of this Rebuttal Prehearing Exchange and on page 10 of Complainant's Initial Prehearing Exchange, Complainant applied the "major" egregiousness multiplier to the violations alleged in Counts 1 and 2 because vehicles from those families produced emissions in excess of Clean

Air Act standards during emissions testing, and for Counts 9 and 10 because the EPA does not have information about emissions from the uncertified vehicles labeled as belonging to these engine families.

As Respondents note in their PHE, the Penalty Policy provides "incentives for companies to remedy violations involving uncertified vehicles or engines in order to prevent the actual excess emissions that would result from their use." Penalty Policy at 9. Remediation may take the form of exporting the uncertified vehicles, recalling and repairing the uncertified vehicles, or installing proper emissions labels. *Id.* When using the rule of thumb method for calculating economic benefit as Complainant did here, the Agency *may* reduce or eliminate the economic benefit component of a penalty for violations concerning vehicles that have been remediated. *Id.* In this case, 66 uncertified vehicles identified in Counts 9 and 10 were remediated because they were stopped at the point of importation and Complainant believes they were not sold in the United States. IPHE at 10 n.3. Complainant did not assess an economic benefit for these remediated vehicles when calculating the proposed penalty. *Id.*

The impact remedial action has on the gravity component of a penalty is separate from the impact it has on the economic benefit component. Penalty Policy at 9, 14. The Penalty Policy instructs that when computing the gravity component of a penalty, the gravity should be increased by 30 percent "in the case of vehicles or engines for which no remedial action is taken, or where the action is ineffective. Percentages between zero and 30 percent are appropriate where some but not complete remedial actions are taken or where the remedial action was delayed." *Id.* at 14. Complainant did not increase the gravity component attributable to the 66 remediated vehicles to account for this factor. *See* Initial PHE at 11. Pursuant to the Penalty Policy, Complainant did increase the gravity component attributable to the remaining unremediated vehicles by 30 percent. *Id.*

**4. Impact on Ability to Continue in Business**

In Complainant's Initial Prehearing Exchange, EPA identified public statements by Respondents suggesting that T-Group has annual revenues of $100 million, employs over 1,000 individuals, and does business in North America, South America, Northern and Western Europe, the Mid-East, and Asia. *See* CX034–CX038. The statements also suggest that T-Group has diversified operations and, in addition to the types of highway motorcycles and non-road vehicles at issue in this case, manufactures lawn and garden equipment, fitness equipment, and wooden and steel doors. *Id.* Complainant also provided an article from Dealernews.com noting that in 2013 Respondents accounted "for 70 percent of China's total ATV exports to the" United States, "sold 120,000 ATVs and motorcycles in the" United States, and had 30 percent market share in the United States. CX042. Respondents contend that the evidence of these statements is unreliable and does not accurately reflect their financial condition. Respondents contend that they do not have the ability to pay the proposed penalty, and/or the penalty would impact their ability to continue in business.

Complainant offers additional information concerning the finances of Respondents. Further, Complainant has requested additional, current information about Respondents and other entities in a letter included as Exhibit CX169. When evaluating an entity's ability to pay a penalty, it is appropriate to look into the assets of other interrelated entities. *See In re New Waterbury, Ltd.*, 5 E.A.D. 529, 548–49 & 549 n.32 (EAB 1994); Guidance on Evaluating a Violator's Ability to Pay a Civil Penalty in an Administrative Enforcement Action, at 10 (Exhibit CX025). Complainant is aware of other entities that, on information and belief, are or may be interrelated with Respondents. Complainant is therefore asking for additional information regarding these entities.

Respectfully Submitted,

10/13/16
Date

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10/13/2016
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## CERTIFICATE OF SERVICE

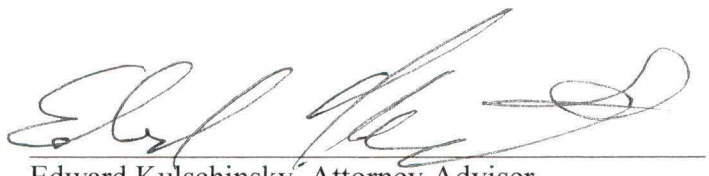
I certify that the foregoing Complainant's Rebuttal Prehearing Exchange in the Matter of Taotao USA, Inc., et al., Docket No. CAA-HQ-2015-8065, together with Complainant's Proposed Exhibits that do not contain CBI, were filed this day electronically using the EPA Office of Administrative Law Judges' E-Filing System. In addition, the original and two copies of Complainant's Rebuttal Prehearing Exchange, two full sets of Complainant's Proposed Exhibits, and one set of Complainant's Proposed Exhibits from which exhibits containing CBI have been omitted, were filed this day by hand delivery to the Headquarters Hearing Clerk in the EPA Office of the Headquarters Hearing Clerk at the address listed below:

U.S. Environmental Protection Agency
Office of the Headquarters Hearing Clerk
1300 Pennsylvania Ave., NW, MC-1900R
Ronald Reagan Building, Room M1200
Washington, DC 20004

I certify that three copies of Complainant's Rebuttal Prehearing Exchange, and, with the consent of Respondents' counsel, one compact disc containing a full set of Complainant's Proposed Exhibits in an electronic format, were sent this day by certified mail, return receipt requested, for service on Respondents' counsel at the address listed below:

William Chu, Esq.
The Law Offices of William Chu
4455 LBJ Freeway, Suite 909
Dallas, TX 75244

10/13/2016
Date



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