Environmental Audits: An Analysis of the Dilemma and an Assessment of Oklahoma's Response

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COMMENT

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I. Introduction

Over the last several years, both regulators and the parties they monitor have come to realize the tremendous value of environmental auditing as a means of ensuring the maintenance of regulated entities' compliance with federal and state environmental laws. This increase in the popularity of environmental auditing has given rise to complex statutes and administrative rules designed to provide incentives for performance and disclosure of environmental audits. As a result, a heated debate has ensued between regulated entities, the states, and the agencies within the federal government charged with the task of protecting the environment. The Environmental Protection Agency (EPA) has taken a strong stand against the adoption and maintenance of state statutes that provide evidentiary privileges and immunity from administrative and civil enforcement actions based on the results of environmental audits. The EPA fears that the protections offered by some of these laws may frustrate regulatory efforts at protecting the environment.

State regulators face a dilemma in deciding what protections to offer in order to provide incentives to encourage the performance of environmental audits. The problem lies in the fact that the protections offered in audit incentive policies may frustrate the purposes of the environmental regulations which state agencies are charged with enforcing. Viewing the advantages and disadvantages of the federal and various types of state environmental audit protection laws and administrative rules, it is possible to decide what types of protections for environmental audits are sufficient to accomplish the goals of environmental protection without sacrificing economic progress along the way.

A. Background on Environmental Regulation

Before the 1980s, the field of environmental protection was dominated by the "command-and-control" philosophy of regulation. Federal and state environmental authorities protected this country's natural resources under the confines of a rigorous system of intricate environmental laws and regulations designed to mandate methods of compliance and identify and prosecute all violators. Beginning with the Reagan administration, however, such a labor-intensive and economically burdensome system

2. See id.
of enforcement became highly unattractive in an era of regulatory downsizing. As one author put it, ‘Ronald Reagan and his advisors believed the president had been elected to bring ‘regulatory relief’ to the American economy, and environmental regulations were an early priority on the ‘hit list’ of laws needing ‘regulatory reform.’”4 Since that time, the government has begun to shy away from such resource-intensive methods of environmental enforcement. In an article on environmental audits, one commentator describes the problems that the EPA faces regarding its regulatory budget and the road blocks to environmental enforcement currently plaguing the EPA.5 In 1996, following a series of budget cutbacks, Carol Browner, head of the EPA, made the announcement that government agencies no longer had the resources to carry the environmental regulatory burden alone.6 Browner stated that “[t]he environmental cop is absolutely not on the beat. . . . We cannot ensure American people their air is clean, their drinking water is safe, [or] the health of their children is protected.”7 One way to close the regulatory gap in enforcement created by these budget cuts is to encourage industries to self-policing their environmental compliance.8

B. Dawn of the Environmental Audit

The EPA has called for a change in the means by which it enforces its regulations through an increase in voluntary assistance and a decrease in federal and state monitoring.9 This request for help from regulated entities has not, however, altered the substance of the environmental statutes the government seeks to enforce. The Federal Register is inundated with a myriad of intricate and complicated laws10 which impose strict requirements on a number of industries.11 While the EPA’s enforcement resources have been diminished by budget cutbacks,12 regulated entities are still expected to comply with environmental laws. In fact, most environmental laws call for voluntary monitoring and documentation of compliance.13 Whether a state statute requires voluntary monitoring or not, regulatory agencies still exist at all levels of government with the power to inspect potential violations and enforce the law against any wrongdoers.14 Environmental regulations are still

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3. See id.
6. See id.
7. Id.
8. See id.
11. See id.
12. See Campbell, supra note 5, at 1031 (stating that spending cuts have resulted in a 40% decrease in EPA inspections since 1995).
14. See Michael T Scanlon, A State Statutory Privilege for Environmental Audits: Is It a Suit of
being enforced despite cutbacks in agency inspections. Thus, regulated entities have a heightened need to stay on top of their compliance efforts. Though industry has largely been left to monitor its own compliance without the prodding of frequent agency evaluations, the failure of corporations and individuals to meet agency standards has the same result that it did in the days when agency enforcement activity was more intense.\(^\text{15}\) Severe civil and criminal penalties may be imposed as a result of failing to abide by federal environmental statutes.\(^\text{16}\)

1. Definition and Description of an Environmental Audit

One way that regulated entities have responded to the need for increased efforts in the voluntary monitoring of compliance is through the use of environmental audits. The EPA defines an environmental audit as "a systematic, documented, periodic and objective review by regulated entities of facility operations and practices related to meeting environmental requirements."\(^\text{17}\) An audit has been defined as an investigative procedure used by a regulated entity to gauge its own compliance with environmental standards.\(^\text{18}\) The results of the investigation are reported to management authorities within the company, along with any recommendations for remedial actions available to achieve compliance where necessary.\(^\text{19}\)

An environmental audit can be tailored to achieve a variety of objectives, including "verify[ing] compliance with environmental requirements; evaluat[ing] the effectiveness of environmental management systems already in place; or assess[ment] of the risks from regulated and unregulated materials and practices."\(^\text{20}\) Thus, an environmental audit can be general or specific, depending on the requirements and the nature of the regulated activity. In order to assist companies and individuals in the creation and employment of effective environmental auditing programs, the EPA has outlined several factors which it considers essential to the auditing process. Those factors include high level management support for environmental auditing and adequate staffing and procedures for the performance and reporting of audits.\(^\text{21}\)

2. Advantages of Auditing

The implementation of a thorough audit policy is a valuable and efficient means

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15. See id.

16. See id.


19. See id.


21. See id. at 25009 (discussing the basic elements of an environmental audit program: executive support for audit programs with a promise to act upon audit findings; auditing procedure independent of audited activities; adequate staffing and auditor training; specific audit program goals, scope, resources and frequency; efficient means for gathering and preparing audit findings, remedial recommendations and schedules for implementation; and a process to ensure the quality and accuracy of audit results).
for maintaining compliance with environmental standards for both regulators and the regulated. Voluntary auditing and disclosure enable regulatory agencies to learn about potential environmental problems to which they may not have otherwise been privy because of a lack of adequate investigatory resources. From the standpoint of a regulated company, environmental auditing ensures that when an agency investigation does occur, a regulated entity will not be caught by surprise. A company which employs auditing procedures will be aware of most or all of its potential violations and will be able to show regulators that measures have been taken to identify and rectify any problems. Further, environmental auditing allows regulated entities to discover problems in their infancy so that a violation can be mitigated before it becomes unmanageable.

3. Disadvantages of Auditing

Voluntary auditing conserves federal resources by allowing regulated entities to police themselves. Because of their soothing effect on the swelling of environmental regulatory costs, the EPA has expressly encouraged the voluntary performance of environmental audits by regulated entities. The EPA has not made the absolute promise, however, that the results of voluntary audit reports will not be used to impose civil and criminal liabilities against companies who heed the government's call to cooperate. As the old saying goes, "no good deed goes unpunished." For example, Coors Brewing Company's voluntary disclosure of environmental violations resulted in penalties in excess of a million dollars. The Coors example clearly illustrates the potential liability regulated entities face in disclosing environmental audits. Thus, regulated entities are hesitant to perform and submit environmental audits for fear that they may subject themselves to liabilities which they may have otherwise avoided. In addition, companies also worry that the disclosure of audit reports may reveal trade secrets.

4. Background to the Auditing Dilemma

Regulated entities have sought to protect the information contained in audit reports through certain legal doctrines, including the attorney-client privilege, the attorney work product doctrine and the self-evaluative privilege. However, these legal doctrines employed to protect the information contained in audit reports are not without their shortcomings. As a result, regulated entities have requested that the government provide some sort of protection for their cooperation in environmental regulation. Specifically, companies want the government to guarantee relief

23. See id.
25. See Environmental Auditing Policy Statement, supra note 17, at 25004.
26. See Campbell, supra note 5, at 1031-32.
27. See Farran & Adams, supra note 22, at 10,245.
from penalties. Furthermore, companies do not want the results of audits used by the EPA and the Department of Justice (DOJ) as a basis for agency enforcement actions or disclosed to third parties who may use the reports as evidence in civil suits. Thus, the main issues with regard to the future of environmental auditing are whether audit reports should be privileged and whether a company that volunteers audit information should be exempt from civil and criminal liability for violations reported through an environmental audit.  

In response to these questions and the rolling wave of state audit protection laws, the EPA formulated a final policy statement on environmental auditing in 1995. 

Unfortunately, many interested parties feel that the EPA's answer to their regulatory questions is incomplete at best since it fails to guarantee the application of the protections it offers. Before and after the adoption of the policy, industries petitioned state governments to pick up where the federal government left off by providing further protections for the disclosure of environmental audit reports. Nineteen states have enacted audit privilege and immunity laws and others are sure to follow. Oklahoma, however, has adopted a state agency regulation concerning environmental audit privileges, instead of a state statute. This comment will attempt to evaluate the adequacy of Oklahoma's environmental audit incentives policy as compared to the federal policy, similar state laws, and the factors opposing and favoring privileges and immunities for environmental audits.

II. Shortcomings of Legal and Other Nonstatutory Protections

Before industry's cry for statutory protections for environmental audits, several traditional legal doctrines such as the attorney-client privilege, the work product doctrine, and the self-evaluative privilege were employed in an attempt to shield companies from the imposition of criminal and civil liability based on the results of audit reports. These nonstatutory protections are, however, subject to certain limitations which may leave the contents of an audit report open to discovery. This presents a serious problem because, when performed correctly, an audit exposes the auditing party to the possibility of litigation, because it identifies the ingredients of a violation in detailed fashion.

28. See Campbell, supra note 5, at 1030.
30. See id. at 66,712 (stating that the policy is not a final agency action and thus does not create any rights, duties, or obligations).
31. See Campbell, supra note 5, at 1030 n.6 (listing states which have enacted audit privilege laws and the various types of privileges they offer).
33. See John Calvin Conway, Note, Self-Evaluation Privilege & Corporate Compliance Audits, 68 S. Cal. L. Rev. 621, 628 (1995) (stating that "since a good legal audit essentially provides a 'road map' to corporate wrongs, it can be very useful to parties opposing the corporation").
A. The Attorney-Client Privilege and Environmental Auditing

The attorney-client privilege is the oldest and most well-recognized traditional legal doctrine used to protect confidential information.\(^4\) The privilege has been successfully employed in the context of environmental audits as a means of protecting the confidentiality of the information gathered.\(^5\) The privilege prohibits the disclosure of any information revealed to an attorney by his client for the purpose of obtaining legal advice.\(^6\) The basic elements of the attorney-client privilege are: (1) the client must seek legal advice from a lawyer who is acting in a professional capacity; (2) the information revealed by the client must have been disclosed for the purpose of receiving legal advice; (3) the confidentiality of the information must not have been jeopardized by either the client or the attorney; and (4) the privilege must not have been waived by disclosure to third parties or by any other means.\(^7\)

Regulated entities often hire attorneys to conduct or assist in the performance of environmental audits, hoping that the information gathered will enjoy privileged status. As the elements outlined above suggest, the privilege is subject to limitations that may render it inapplicable in the case of environmental audits. For instance, the privilege will not protect purely factual information.\(^8\)

The protection of the privilege extends only to communications and not to facts. A fact is one thing and a communication concerning that fact is an entirely different thing. . . . The client . . . may not refuse to disclose any relevant fact within his knowledge merely because he incorporated a statement of such fact into his communication to his attorney.\(^9\)

Thus, any factual information contained in an audit may be accessed by the government through its own inquiries, as factual material is not privileged. In addition, the privilege will not apply in cases where a waiver has occurred.\(^10\) Further, in most instances, an attorney does not act as the sole auditor. Rather, an attorney merely assists in the preparation of the audit report itself.\(^11\) Specifically, in such a situation the attorney communicates with several persons in gathering the information for the report, who may or may not be employees of the corporation.

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35. See Chaumette & Cason, supra note 18, at 7-8 (citing Olen Properties Corp. v. Sheldahl, Inc., 24 Envtl. L. Rep. (Envtl. L. Inst.) 20936 (C.D. Cal., April 12, 1994) (holding that the attorney-client privilege could apply to an environmental audit where the information relayed in the audit was communicated to the attorney for the purpose of obtaining legal advice)).
37. See Chaumette & Cason, supra note 18, at 8.
38. See Upjohn, 449 U.S. at 396-97 (stating that a party cannot conceal a fact merely by revealing it to his attorney).
39. Id. at 395-96.
41. See Campbell, supra note 5, at 1033.
Thus, without addressing the implications of agency principles, the confidentiality of the information may be waived. Finally, the purpose of the communications between the attorney and the client must have been to obtain legal advice.\textsuperscript{42} Most audits are prepared for the purpose of creating a report, as required by statute,\textsuperscript{43} which will be submitted to regulators for the purpose of monitoring compliance. An audit is often conducted solely to comply with applicable environmental laws and not to obtain legal advice. Only in cases in which the company can establish that the primary purpose for the audit was to obtain legal advice will the court allow the privilege to stand.\textsuperscript{44}

Further, some courts have held that the attorney's involvement in the audit process must meet a certain threshold level. In United States v. Chevron,\textsuperscript{45} the court held that an attorney's role in an environmental audit must be more than mere presence during the process.\textsuperscript{46} The court held that the lawyer must be acting in his capacity as an attorney and must be performing a legal inquiry or like services which constitute more than simple fact-finding.\textsuperscript{47} Under these standards, the applicability of the attorney-client privilege to the results of environmental audit reports is significantly constrained. For audit reports to qualify under the privilege, the role of counsel must be cautiously constructed, both in terms of the content of the audit report and the reasons for its creation. As a result of these limitations, the apprehension felt by regulated entities in the creation of audit reports, even those helped by an attorney, is easy to understand.

B. The Work Product Doctrine and Environmental Auditing

The work product doctrine is a valuable safeguard for environmental audits, affording wider protections than those extended by the attorney-client privilege.\textsuperscript{48} As outlined in Rule 26(b)(3) of the Federal Rules of Civil Procedure,\textsuperscript{49} the work product doctrine shields an attorney's mental impressions, conclusions, opinions, and theories established in anticipation of litigation from disclosure.\textsuperscript{50} The work product doctrine applies to materials and communications exchanged within the attorney-client relationship\textsuperscript{51} as well as to information gathered by agents assisting the attorney, provided such materials were amassed in anticipation of litigation.\textsuperscript{52}

\textsuperscript{42} See id.
\textsuperscript{43} See, e.g., supra note 13 (examples of environmental protection statutes that require monitoring reports by regulated entities).
\textsuperscript{44} See IBM Corp. v. Sperry Rand Corp., 44 F.R.D. 10, 12 (D. Del. 1968) (outlining the requirements for the attorney-client privilege).
\textsuperscript{46} See id. at *6.
\textsuperscript{47} See id.
\textsuperscript{48} See In re Subpoena Duces Tecum, 738 F.2d 1367, 1377 (D.C. Cir. 1984).
\textsuperscript{50} See id.
\textsuperscript{51} See id.
\textsuperscript{52} See Chaumette & Cason, supra note 18, at 10.
Despite the differences in the protections afforded, the attorney-client privilege and the work product doctrine are similar in that both are subject to limitations which may render them inapplicable in the case of environmental audits. For example, courts recognize a distinction between factual work product and "opinion work product."\(^5\) In addition, under the work product doctrine, information designated as privileged must have been prepared in anticipation of litigation. While the privilege is not restricted to pending lawsuits\(^6\), the privilege only protects materials prepared, at a minimum, with "an eye toward litigation."\(^5\) Further, the possibility of litigation must be "distinct."\(^6\) Thus, in the case of environmental audits, the work product doctrine is limited to particular circumstances. For companies that prepare audits as a part of their everyday business operations and that are not constantly in the shadow of pending litigation, the work product doctrine may not apply.\(^7\) In addition, an exception to the privilege may further limit its application. If an opposing party can establish a "substantial need" for the information in question, or can prove that the opposition will be subject to "undue hardship" because of nondisclosure, a court may waive the privilege.\(^8\)

One final limitation on the application of the work product doctrine, which is especially pertinent to environmental audit reports, is the issue of confidentiality. The privilege requires the preservation of the confidentiality of the information contained in the audit.\(^9\) Because many companies voluntarily reveal the results of environmental audits to the government in order to remain in compliance with certain environmental monitoring requirements, the purposes of environmental audits are potentially inconsistent with the requirement of confidentiality inherent in the work product doctrine.\(^10\) Unfortunately, no case law has dealt with the clash between the work product doctrine and the voluntary disclosure of audit materials to the EPA. In the realm of securities law, however, case law holds that voluntary disclosure of confidential materials to a governmental agency that occupies an adversarial position toward the disclosing entity leaves no reasonable expectation of confidentiality of the disclosed information.\(^11\) Thus, much like the

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53. See Conway, supra note 33, at 633.
54. See Campbell, supra note 5, at 1034.
56. See Taroli v. General Electric Co., 114 F.R.D. 97, 99 (N.D. Ind. 1987) (holding the work product doctrine inapplicable because the defendant was unable to establish that a lawsuit was a distinct possibility at the time the information in question was gathered).
57. See United States v. IBM, 66 F.R.D. 154, 178 (S.D.N.Y. 1974) (stating that the work product doctrine does not shield information gathered in the ordinary course of business).
58. See Holmgren v. State Farm Mut. Auto. Ins. Co., 976 F.2d 573, 576-77 (9th Cir. 1992) (discussing the circumstances that result in a waiver of the privilege provided by the work product doctrine).
59. See In re Chrysler Motors Corp. Overnight Evaluation, 860 F.2d 844, 846-47 (8th Cir. 1988) (holding that the privilege provided by the work product doctrine is waived when the information in question is not kept confidential).
60. See Chaumette & Cason, supra note 18, at 12.
61. See In re Subpoena Duces Tecum, 738 F.2d 1367, 1374-75 (D.C. Cir. 1984) (holding that a voluntary disclosure of information to the SEC waived any privilege provided by the work product.
attorney-client privilege, the work product doctrine may be an unreliable source of protection for environmental audits.

C. The Self-Evaluative Privilege and Environmental Auditing

The self-evaluative privilege operates as a discovery shield for certain voluntary assessments that could conceivably be used in future litigation against the auditing party.62 The self-evaluative privilege recognizes the notion that investigations such as environmental audits have significant value in maintaining public health, safety, and welfare.63 In order to encourage companies to continue to engage in such investigations, the self-evaluative privilege seeks to promote open and voluntary self-evaluations by protecting the information gathered in inquiries such as environmental audits.64 One of the most significant benefits of the self-evaluative privilege is that it does not require that an attorney prepare the materials sought to be protected.65 The elements of the privilege are: (1) the material in question must have been gathered in the process of a self-evaluation; (2) a significant public interest must exist demanding the open exchange of the type of information sought; and (3) requiring the disclosure of such information would chill the incentive to perform self-evaluations.66 The self-evaluative privilege is very similar to Rule 407 of the Federal Rules of Evidence, which provide, in part, that "an entity's retrospective self-assessment of its compliance with [environmental] regulations should be privileged in appropriate cases."

Unfortunately, the self-evaluative privilege has limited application to environmental audits. Few, if any, courts have applied the doctrine at all in the case of environmental audits.67 Only one court to date has allowed the application of the self-evaluative privilege to protect the results of an environmental audit.68 Even in those cases in which the privilege is allowed, a showing of unique circumstances or special need may overcome the privilege.69 Therefore, regulated entities are

63. See Chaumette & Cason, supra note 18, at 13.
64. See id. at 13-14.
65. See id. at 17.
68. See Paula C. Murray, The Environmental Self Audit Privilege: Growing Movement in the States Nixed By EPA, 24 REAL EST. L.J. 169, 172 (1995) (stating that the self-evaluative privilege has been applied in other fields such as medical audits, but not environmental); see also, e.g., United States v. Dexter Corp., 132 F.R.D. 8, 10 (D. Conn. 1990) (holding that public policy considerations regarding uninhibited enforcement of the Clean Water Act override any interests in nondisclosure).
69. See Reichhold Chem., 157 F.R.D. at 527 (holding that the privilege should apply to environmental audits in appropriate circumstances because the public interest in environmental compliance is significantly furthered when regulated entities feel they can engage in open self-evaluation without having to worry about having their efforts turned against them in a lawsuit some time in the future).
70. See id. at 526.
not able to rely confidently on the self-evaluative privilege to shield them from liability for administrative penalties or criminal and civil suits.

III. EPA's Final Policy Statement Regarding Environmental Audits

As a result of the practical limitations inherent in nonstatutory privilege doctrines, regulated entities began to exert more pressure on the states and the federal government to provide some sort of statutory protections for environmental audits. The EPA attempted to heed the call of regulated entities for more protections by issuing its final policy statement dealing with "Incentives for Self-Policing: Discovery, Disclosure, Correction and Prevention."71 Besides attempting to satisfy regulated entities, the EPA issued this policy statement to avoid the passage of more state privilege and immunity statutes than those already in existence. Unfortunately, the federal government's response may not provide regulated entities with the protection they seek in order to encourage disclosure of audit reports.

The final policy statement clearly discourages state audit privilege and immunity laws for several reasons.72 First, the EPA argues that state audit protection statutes, especially those which offer a qualified privilege, only help violators avoid compliance by helping them to cover their tracks.73 "A privilege would invite defendants to claim as 'audit' material almost any evidence the government needed to establish a violation . . . ."74 Second, the EPA asserts that such laws are contrary to open environmental policy and decision making. "Privilege, by definition, invites secrecy instead of the openness needed to build public trust in industry's ability to self-police."75 Third, the EPA argues that audit privilege laws would only serve to increase litigation costs by inundating courts with lawsuits designed to test the limits of such privileges.76 Consequently, in states in which audit privilege and immunity statutes have been enacted despite regulatory frowning, the EPA has reserved the right to "take necessary actions" to protect the environment from violations hidden by the privileges afforded under state laws that contradict the federal policy.77 Those necessary actions most likely would include increased enforcement in those states offering such privileges and preemption of state laws which frustrate the purposes of federal environmental regulations.

A. Incentives to Audit

As an alternative to regulation by negative reinforcement, the EPA's final policy statement offers several positive protections in an effort to encourage voluntary policing, disclosure, and remediation of environmental violations. Generally, those

72. See id. at 66,710.
73. See id.
74. Id. at 66,710.
75. Id.
76. See id.
77. See id. at 66,712.
protections include the reduction of gravity-based punitive penalties, a refrain from criminal referrals, and desistance from routine requests for environmental audit reports, even in situations in which compliance is required by statute and enforced through penalties. The EPA views these protections as sufficient to encourage environmental auditing for regulated entities that are hesitant to audit.78

The foundation of the EPA's incentive policy is the reduction of gravity-based penalties in exchange for the prompt exposure and remediation of violations of environmental regulations.79 The EPA penalties have two components: (1) a gravity-based component, and (2) an additional fine to compensate for any economic gain realized as a result of noncompliance.80 A gravity-based penalty is one that fines the violator based on the seriousness of its conduct.81 In its policy, the EPA has offered to waive completely all gravity-based penalties where the violation in question was uncovered during a voluntary audit that meets the EPA's requirement of "due diligence."82 If discovery is not made during an audit and evidence of "due diligence" cannot be found, the EPA has offered to reduce the amount of gravity-based penalties by 75% if a violation is voluntarily uncovered, exposed, and remediated.83 However, this offer does not limit the EPA's ability to penalize a regulated entity for any economic gains which may have been obtained as a result of noncompliance.84 The EPA still reserves the right to levy fines in the amount of any profits that may have been earned as a result of noncompliance.85

In addition to the reduction of penalties, the EPA offers to refrain from referring a regulated entity for prosecution by the Department of Justice (DOJ) if certain conditions are met.86 There are nine general requirements for application of the policy87 and a few additional prerequisites that are specific to the offer to refrain from criminal referrals.88 In addition to the nine general requirements of the policy, the violation disclosed must not evidence a prevalent management policy that conceals or condones violations or involve assistance of high level management either consciously or deliberately ignoring a violation.89

The final incentive offered in the policy involves requests for audit reports. The EPA states that in exchange for cooperation with the audit policy, it will refrain from requesting an audit report, which could serve as a basis for an enforcement

78. See id. at 66,706, 66,711.
79. See id. at 66,706-07.
80. See id. at 66,711.
81. See id.
82. Id. at 66,707. In defining "due diligence," the EPA outlines the elements for this standard in detailed, lengthy fashion at 60 Fed. Reg. 66,710-11.
83. See id. at 66,707.
84. See id.
85. See infra Part III.B.1.
86. See 60 Fed. Reg. at 66,711.
87. See discussion infra Part III.B.
89. See id.
action. This component of the final policy on audits offers the assurance that the EPA will not require a regulated entity to conduct an audit that will then be used as a basis to prove violation. However, much like the other provisions of the policy, the EPA reserves its right to bypass the protections offered. For instance, in cases in which the EPA has information from an independent source suggesting that a violation has occurred, the EPA reserves discretion to request disclosure of an audit report in order to facilitate investigation of the alleged infraction.

B. Requirements for the Application of the Final Policy

In order for a regulated entity disclosing a violation to be eligible for any of the protections offered in the final policy statement, nine conditions must first be met. Provided that an entity complies with these requirements, the EPA has the discretion to offer the application of the final policy statement to the regulated party.

1. Discovery Through Audit

The violation reported must be discovered through an environmental audit or a related procedure that reflects certain qualities that will ensure the accuracy of the report. The report must be the result of a systematic, objective process which is well documented and which evidences the regulated entity's "due diligence" in avoiding, revealing, and remedying any violations. Failure to meet this first condition will not necessarily result in the loss of all benefits offered under the policy. A 75% reduction in gravity-based penalties is still available if this first condition is not met, provided that the regulated entity is in compliance with the remaining eight requirements.

2. Noncompulsory Discovery

The violation reported must be discovered voluntarily as opposed to being uncovered under a statutorily-mandated monitoring requirement. The benefits offered under the final policy statement are not applicable in situations in which sampling is required by law. The Toxic Substances Control Act (TSCA) is an example of a typical federal environmental regulation that requires regular monitoring and reporting. Thus, where the TSCA requires a regulated entity

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90. See id. at 66,708.
91. See id.
92. See id. at 66,711-12.
95. See id.
96. See id.
97. See id.
98. See id.
99. See id. at 66,708.
100. See supra note 13 (providing the statutory citation for the monitoring requirements of the Toxic Substances Control Act).

https://digitalcommons.law.ou.edu/olr/vol51/iss3/4
to monitor and report compliance with the statute, the incentives offered in the final policy statement are not applicable because the regulated entity's actions were not voluntary.

3. Timely Disclosure

The violation in question must be reported in writing within ten days, or less if required by statute.101 The preamble of the final policy statement provides an exception in cases in which the violation in question involves complicated biological reactions in which a problem does not become readily apparent within the ten-day period.102 The EPA may accept the delayed report of such a violation, provided the problem does not present an imminent threat to public health and safety.103 Acceptance of reports after the prescribed period is left to the discretion of the EPA.104

4. Unsolicited Discovery

The violation in question must be reported before the initiation of an agency inspection, civil suit, the filing of a complaint by a third party, the reporting of the violation by a whistle blower, or the impending discovery of the violation by a regulatory agency.105 A report is hardly voluntary when the incentive to perform and disclose an audit was provided by notice of a lawsuit or a call from the EPA telling a regulated entity that inspectors are on the way. Nevertheless, the final policy statement does not address the question of whether the benefits are available to a company that performs an audit while unaware of an imminent lawsuit or enforcement action.106

5. Timely Remediation

The violation reported must be remedied within a period of sixty days. Furthermore, the regulated entity must correct any environmental or human health hazards which directly or indirectly result from the problem disclosed. Any remedial measures taken must be certified and disclosed in writing.107

The EPA reserves the right to determine what measures are appropriate for the remediation of any subsequent problems. Further, the EPA does not guarantee the confidentiality of any of the corrective measures it imposes. The EPA also reserves the right to require that agreements are reached with the public to induce prompt and effective remediation. If a regulated entity anticipates that corrective actions will require more than sixty days, the EPA mandates that notice of such delay be expressed in writing before the sixty-day period ends.108

102. See id. at 66,708.
103. See id.
104. See Chaumette & Cason, supra note 18, at 27.
106. See Chaumette & Cason, supra note 18, at 28.
108. See id.
6. Antecedent Measures To Prevent Recurrence

The reporting entity must guarantee in writing that steps will be taken to ensure that the problem disclosed will not arise again. 109 One of the canons of environmental protection is the promotion of antecedent versus consequent remediation. The EPA wants to encourage regulated entities to fix problems before rather than after they occur. One reason underlying this philosophy of regulation is that damage to the environment is hardly ever completely remedied.

7. Disqualification for Recurring Problems

In order to enforce the provisions of the previous requirement, the EPA will refuse to extend the benefits offered in the final policy statement to any reporting regulated entity that demonstrates a past failure to enact preventative measures. Specifically, the violation reported must not be the same as or substantially similar to a problem that has occurred at the same facility within three years of the current disclosure. Further, the problem disclosed cannot be one that evidences a pattern of violations by the controlling organization of the facility in question within five years prior to the current reporting. A documented violation of any applicable environmental law or agency rule will be considered. 110

8. Exceptional Violations

The violation reported cannot result in substantial actual damage or pose an imminent and significant threat to human or environmental health. Further, the problem disclosed cannot be a violation of the express terms of a court or agency order or consent agreement. 111 The final policy statement fails to define the terms that determine the severity of the violation reported. Specifically, it is unclear how the EPA defines the terms "substantial, significant or imminent harm." 112 The impact of this ambiguity is that the failure to define these terms leaves the EPA with considerable discretion in determining whether the damage caused by a violation is so severe that exemption from the policy is warranted.

9. Guarantee of Assistance

If the reporting entity promises to cooperate with the EPA, then the final policy statement may apply. 113 The regulated entity must agree to afford investigators access to any relevant information, documents, and persons needed to expedite an inquiry into a reported violation or any related matters of noncompliance. 114 This final requirement allows the EPA to investigate matters not disclosed in an audit report where deemed necessary. 115

109. See id.
110. See id.
111. See id. at 66,712.
114. See id.
115. See id. at 66,709-10.
C. Shortcomings Of The EPA's Final Policy Statement

While some interested parties view the EPA's final policy statement as a step forward, many regulated entities have voiced the opinion that the policy leaves much to be desired. For instance, the EPA reserves broad discretion essentially to ignore the entire policy. After all, the final policy statement is nothing more than a guidance tool. The EPA expressly acknowledges this fact within the policy. "The policy is not a final agency action and is intended as guidance. It does not create any rights, duties, obligations, or defenses, implied or otherwise, in any third parties." Thus, the EPA may consider the factors listed in the policy in order to mitigate any punishment, but it provides no true guarantees. Further, regulated entities cannot rely on the final policy statement to protect the confidentiality of the audit reports submitted. Finally, the benefits offered in the policy do not apply when penalty reductions have been afforded under some other form of audit incentive policy. This last provision was apparently added in an effort to discourage the adoption of state audit privilege laws, as their application to a disclosure would foreclose any opportunity for mitigation under the EPA's policy.

1. Penalty Mitigation

The cornerstone of the EPA's incentive policy involves the mitigation of gravity-based penalties. Other forms of financial penalties not covered in the policy are relevant, however, to the disclosure of environmental audits. For instance, the EPA has the power to recover through administrative penalties any sums which are found to have been earned through noncompliance with environmental protection laws. Such a penalty ensures that regulated entities that fail to comply with environmental statutes do not gain an economic advantage over the companies that expend valuable resources in order to stay in compliance. The EPA loosely refers to these penalties as designed to "level the playing field." In a critique of the EPA's audit policy, one author states that regulated entities complain about these fines because there is no way to predict how the EPA will quantify these economic-balancing penalties. Specifically, industries are unsure how the EPA decides what amount of their profit was earned as a result of noncompliance. The EPA does use a system to determine the money a company may have earned through violating the law. However, the accuracy of this formula is questionable because it has never been evaluated by the public through the administrative rule-making process. Thus, despite the offer to alleviate some of the

116. Id. at 66,712.
117. See Campbell, supra note 5, at 1041.
118. See Chaumette & Cason, supra note 18, at 30.
120. See id.
121. Id.
122. See Campbell, supra note 5, at 1041.
123. See id.
124. See Chaumette & Cason, supra note 18, at 32-34.
financial burdens of enforcement, the threat of significant economic penalties still remains. The EPA's failure to allow regulated entities to comment on the procedure for calculating these non-gravity-based penalties has left many companies uncertain of how much they actually stand to lose by disclosing an audit report. Thus, the offer of penalty mitigation provides limited incentives to disclose an audit report.

2. Recommendations for Prosecution

Another loophole in the EPA's audit policy involves the agency's offer to refrain from recommending a violating entity for prosecution. Much like the offer of penalty mitigation, the EPA includes a reservation in its policy that cuts away at the incentive to disclose audits in order to avoid suggestions for prosecution. Specifically, the EPA retains the discretion to prosecute individuals within a reporting entity for any violations disclosed even if the company itself was not turned over to the DOJ for the commencement of an enforcement action.125 This lack of protection for individuals who actually engage in the audit process may render the results of a compliance inquiry meaningless, if an audit is performed at all.126 Due to the possibility of individual prosecutions, an auditor or manager may be reluctant to perform the task required with any sort of depth, and may be even more hesitant to report the actual results.127

3. Requests for Audit Reports

The final incentive included in the EPA's audit policy is also subject to reservations of authority. Though the EPA states that it will refrain from requesting frequent audit reports, in the hopes of triggering an enforcement action, it retains the power to request audit reports "[i]f the agency has an independent reason to believe that a violation has occurred."124 Thus, the offer to cut down on requests for audits is illusory considering that the EPA does not provide a definition for the term "independent reason." Though not likely, it is theoretically possible that under the terms of the policy, the EPA could simply demand an audit report on the basis that it heard a rumor of a violation. The threshold for what constitutes an independent reason is unclear from the language of the policy.

4. Lack of Confidentiality and the Possibility for Citizen Suits

The final policy statement makes no guarantee regarding the confidentiality of audit reports which are disclosed. Thus, even if the EPA and the DOJ decide not to prosecute a violating entity, a third party could institute a civil suit against a company based upon the information contained in an environmental audit. In fact, a number of environmental statutes recommend civil suits in certain situations.129

126. See Campbell, supra note 5, at 1041.
127. See id.
129. See Chaumette & Cason, supra note 18, at 31.
Further, many courts see civil suits as an integral part of environmental regulation.\textsuperscript{130} Consequently, many regulated entities have requested that the results of their audit reports remain confidential, and thus, privileged from discovery. Unfortunately, the EPA is unwilling to offer such an incentive. This reluctance to grant privileged status for environmental audits reveals a fear that such a privilege would interfere with the public's right to information regarding the health of the environment.\textsuperscript{131}

Both environmental law and basic principles of discovery are based upon the public's access to information regarding environmental threats. Without information, the public may lose faith in the EPA's ability to monitor environmental compliance. In addition, the assertion of a privilege implies that there is something to hide. Thus, the public may lose faith in the integrity of industry as well. Finally, the courts frown upon the extension of confidentiality.\textsuperscript{132} The United States Supreme Court places significant emphasis on the freedom of discovery. In \emph{U.S. v. Nixon},\textsuperscript{133} the Court stated that evidentiary privileges "are not lightly created nor expansively construed, for they are in derogation of the truth."\textsuperscript{134} For these reasons and others,\textsuperscript{135} the EPA will not extend confidentiality to environmental audits.

Considering the amount of discretion the EPA reserves in the application of the benefits offered, it is easy to see why regulated entities assert that the final policy statement leaves much to be desired. In the case of each benefit offered, the EPA makes no guarantees that the policy will be followed. Further, the lack of confidentiality for audit reports can expose companies to liabilities above and beyond those imposed by the federal government. As a result, industries nationwide have called out to their respective state legislatures for additional protections.

\textbf{IV. State Audit Protection Laws}

Heeding the call from industries and other entities that fall under the regulatory umbrella of federal environmental statutes and policies, many states have adopted their own audit protection laws. Generally, these statutes augment the protections offered by the EPA's final policy statement. By providing added incentives such as confidentiality, immunity, and testimonial privileges, states seek to appease regulated entities and encourage auditing by picking up where the EPA's policy leaves off.

\textsuperscript{130} See id.


\textsuperscript{132} See id.

\textsuperscript{133} 418 U.S. 683 (1974).

\textsuperscript{134} See Johnson, supra note 131, at 342 (citing United States v. Nixon, 418 U.S. 683, 710 (1974)).

\textsuperscript{135} See infra text accompanying notes 224-26 (discussing possible reasons for the Oklahoma DEQ's refusal to offer a privilege for environmental audits).
To date, at least nineteen states have enacted audit protection statutes, and many others have laws pending in their legislatures. There are two general types of statutes, based upon the protections offered. Most states provide either qualified confidentiality for audit reports, qualified immunity from criminal and civil prosecutions based on the information contained in an audit, or a combination of the two.

Oklahoma has elected to adopt a variation of the state audit incentive statutes in the form of an administrative rule. Administrative rules governing environmental audits offer the same types of incentives and protections as are offered by state statutes. However, important procedural differences exist between an administrative rule and a state statute that may make the adoption of a rule more attractive to state regulators than enactment of a law.

A. General Types of Statutes

One type of audit protection statute offers qualified confidential status for the results of audit reports, but not qualified immunity from civil or criminal suits. Oregon is an example of a state which has chosen to adopt a privilege-alone statute and was the first state actually to codify an audit protection law. Most state laws are modeled after the Oregon statute. For instance, Arkansas, Illinois, Indiana, Kentucky, and Utah all follow the Oregon model. Oregon’s audit

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136. The chart below is borrowed from Campbell, supra note 5, at 1030 n.6. The information in the chart was gathered by the Washington, D.C. law firm of Hale and Dorr, LLP and is accurate as of December 23, 1996.

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137. See id.
138. See Grayson & Riewer, supra note 1, at 10,249.
139. See Scanlon, supra note 14, at 651.
protection statute grants privileged status to audit reports, exempting them from disclosure. Two requirements must be met before the Oregon law will apply. First, the audit disclosed must result from a voluntary inquiry. Thus, after reading the first requirement of the statute, a limitation to its application is readily apparent. The statute will not protect any audit reports that are required to be submitted under any federal or state environmental laws. Because many state and federal environmental laws require auditing, this requirement may substantially limit the application of the Oregon law and is one of the main shortcomings inherent in the many other statutes that have a like requirement. The second requirement under Oregon's law is that companies take timely corrective steps in order to remedy any harm to the environment caused by the violation reported.

One final limitation contained in the Oregon law prevents the application of the statute when it is discovered that an audit was engaged in for fraudulent purposes. This limitation is designed to ensure that companies do not conduct an audit for the sole purpose of covering their tracks in the commission of an intentional violation.

Another type of state audit protection law offers qualified confidentiality for audit reports and provides immunity from prosecution based upon the information disclosed in an audit report, or offers immunity alone, without confidentiality. Essentially, this added provision of immunity allows a regulated entity to escape penalties for violations revealed through an audit. Colorado is one state that has adopted an immunity provision in addition to confidentiality privileges. Under the Colorado audit law, voluntary environmental audits which promptly disclose violations will receive confidential status and result in immunity from any civil and administrative penalties and immunity from criminal penalties for any negligent violations, provided the violations revealed are corrected in a timely manner. In defining what is a timely remediation, the Colorado statute requires that any violations be corrected within two years of being reported. In addition, the statute mandates cooperation with authorities in their investigation of the violation disclosed. Other states that have adopted laws similar to the Colorado statute include Michigan, Idaho, Texas, Kansas, New Hampshire, Minnesota, and

141. See id. § 468.963(5)(a).
142. See id. § 468.963(3)(d).
143. See id. § 468.963(3)(b)(A).
145. See COLO. REV. STAT. § 25-1-114.5(4) (1997) (providing immunity from civil and criminal penalties when a violation is disclosed through a voluntary audit).
146. See id.
147. See id. § 25-1-114.5(1)(c).
148. See id. § 25-1-114.5(1)(d).
South Dakota. Some states offer a variation of the Colorado immunity law by providing an exemption from civil suits, but not from criminal prosecution.

B. Limitations on State Audit Protection Statutes

1. Requirement of Voluntariness

Most of the state audit protection laws require that the violation disclosed be the product of a voluntary environmental audit. Thus, these state statutes will afford no protections for audits that are required to be disclosed under any state or federal environmental law. Since many companies only perform audits in order to stay in compliance with federal and state environmental laws, the protections afforded by state statutes that require voluntary auditing may not apply. This is especially true in light of the fact that federal and state regulatory agencies have the power to expand the circumstances in which an audit is required by law. This power has at times been used intentionally to circumvent audit protection statutes which are conditioned upon the voluntariness of the audit disclosed. However, this requirement may have the effect of encouraging regulated entities to engage in environmental audits with greater frequency in order to produce reports outside of those required by statute.

2. Intentional Violations

Violations disclosed in an environmental audit that are found to be intentional are not covered by any state's statutory protection. Some state laws have included criminal, grossly negligent, and reckless violations in their exemption from application of statutory protections. Most state audit protection laws are designed only to shield negligent actors. Thus, an intentional violation will not be eligible for protection in any state.

3. Fraudulent Abuse of an Audit

As an extension of the prohibition against knowing violations, many state laws also forbid regulated entities to use an audit to cover the tracks of an incident they

153. See Scanlon, supra note 14, at 655-56.
154. See id.
158. See id.
know to be a violation. For example, Oregon's audit law exempts the application of its confidentiality statute in situations in which an audit was engaged in for fraudulent purposes. In Colorado, a court may refuse to extend statutory protections to an audit which is found to have been conducted for fraudulent purposes. The Colorado statute elaborates on what is considered to be a fraudulent purpose for conducting an audit. It states that audit reports created to shield information from disclosure during imminent or ongoing agency enforcement actions or civil suits are performed as an evasive tactic rather than as an attempt at voluntary compliance. Thus, companies are prevented from committing intentional violations and abusing the audit protection statutes by performing an audit solely to circumvent environmental protection laws.

4. Exemptions for Duplicate Violations

Most state audit protection statutes exclude application where a disclosed violation evidences a pattern of past discrepancies or repeated violations of environmental laws. Such provisions ensure that state audit protection laws are not used to shield the conduct of so-called "bad actors" — regulated entities that would use the audit protection statutes as a means to facilitate the intentional violation of environmental laws. States may differ in the frequency with which duplicate or similar violations are allowed before an exclusion from benefits is triggered. In South Dakota, for example, a violation similar to the one currently exposed must not have occurred within the last two years. In New Jersey, however, a similar violation of the same permit or at the same facility must not have occurred within a year of a previously reported infraction. Thus, in almost all states, the protections offered in an audit privilege or immunity statute will not apply if a similar violation has been reported within a specific period of time. Considering the vast number of environmental regulations that are in force and the difficulty of maintaining compliance with all of them, it is easy to imagine the existence of repeated violations, especially at the same facility. This exception does not necessarily swallow the rule, but it does leave state regulators with a greater opportunity to exercise their discretion not to apply the protections offered.

5. Exemption for Violations Causing Substantial Environmental Harm

Many state audit protection statutes are inapplicable where the violation reported results in serious harm to human or environmental health and safety. Mississippi is one state that adopted a significant damage exemption in its audit privilege and immunity statute. Arguably, almost any violation reported will result in

161. See id.
162. See Spicer, supra note 144, at 14.
163. See S.D. CODIFIED LAWS § 1-40-36(2) (Michie 1998).
166. See MISS. CODE ANN. §§ 17-17-29(7)(g)(vi), 49-17-43(g)(vii)(6), 49-17-427(3)(g)(vi) (1995...
some damage to the environment. Under many of these statutes, however, when such damage becomes "significant" is unclear. For example, regulators may not feel that a chemical release was substantial enough to threaten human safety. However, it may result in the death of wildlife or the impairment of aesthetic values. Thus, by including such a provision in an audit incentive statute, states have reserved broad discretion in the decision of whether to apply their audit protection laws based on the nature and severity of the damage caused by the violation reported.

6. Waiver

Many state audit privilege statutes allow waiver of the protections under certain circumstances. Some state laws indicate that privileges may be waived by implication. However, the circumstances which result in an implied waiver are not always spelled out in the statutes. Thus, the implied waiver of confidentiality privileges may present state authorities with yet another opportunity to exercise their discretion and deny the protections offered in their audit protection statutes. The disclosure of confidential information to a third party constitutes the most common means by which a privilege can be impliedly waived. The rationale behind this policy stems from the fact that the voluntary disclosure of privileged information to a third party evidences a diminished expectation of privacy in the information revealed. Since many environmental audits are conducted with the help of outside consultants, statutes that allow waiver through disclosure to third parties create a significant possibility that an audit privilege law will not apply.

Questions also arise as to the result, under principles of waiver, of the disclosure of audit information to regulatory agencies, especially if the information in question does not qualify for the privilege offered by the statute. Under Wyoming law, the audit statute seems to suggest that disclosure of audit information to government agencies waives the privilege. Outside the realm of environmental audits, some courts have held that the communication of confidential information to the government constitutes a waiver of any privilege for the information disclosed in future actions. In states that allow an implied waiver of privileges, such a rule presents a discouraging possibility regarding the application of state audit privilege laws. Alternatively, some state statutes require that a waiver must

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\*167. See, e.g., IND. CODE ANN. § 13-28-4-7(a) (Michie 1996); see also WYO. STAT. ANN. § 35-11-1105(c)(i) (Michie 1997) (stating that the privilege is waived if audit information is introduced in any part of any proceeding, including the reporting of violations as required by statute).

\*168. See Spicer, supra note 144, at 27.

\*169. See id.

\*170. See WYO. STAT. ANN. § 35-11-1105(c)(i) (Michie 1997).

\*171. See, e.g., United States v. Billmyer, 57 F.3d 31, 36 (1st Cir. 1995) (holding that the voluntary communication of information to the government pursuant to an investigation for violations of RICO resulted in an implied waiver of privileged status for the information).
be expressed. For example, Arkansas' audit privilege law states that a waiver of confidentiality may only be accomplished expressly.172

7. Exception Upon Showing of Compelling Need

By demonstrating that a substantial need exists for the information contained in an audit report, a party bringing suit may induce the court to waive the qualified immunity offered by a state audit protection statute. For example, Colorado's statute provides that audit reports may be subject to discovery following a determination by the court that compelling circumstances exist.173 Unfortunately, the Colorado statute fails to establish the definition and scope of the exception for "compelling circumstances." Thus, broad discretion is retained by regulators and the courts in deciding whether to accord privileged status to an environmental audit report. Other statutes indicate that "compelling circumstances" may be shown based upon evidence that a substantial need exists and the information requested is unavailable from any other source.174

Thus, much is left to be desired by the protections these laws offer. There are many loopholes in the statutes which allow the states to revoke any privileges and deny immunity. Even though the protections offered present a potentially significant barrier to the enforcement of state and federal environmental regulations, states have reserved considerable discretion not to apply privilege and immunity statutes. Therefore, the protections contained in state environmental audit statutes may be illusory.

8. Alternative Enforcement Methods

Despite the application of a state's audit privilege or immunity statute, regulatory agencies still have the power to reach violators through the use of alternative theories of recovery. Many state laws expressly or impliedly establish the right to seek remediation of violations reported, even though the information that disclosed a violation may have become privileged or the entity reporting the violation may have become immune from an enforcement action or civil suit. In an action for remediation, a regulated entity may be required to pay for damages to the environment and even reimbursement for the state's costs in bringing the remediation suit.175 Thus, means are available to force a company to pay for its violations, even if it is granted immunity by an audit protection statute.

VI. Oklahoma's Policy Regarding Incentives for Environmental Auditing

As a result of the shortcomings found in state statutes protecting environmental audits and for other reasons, Oklahoma takes a different route in providing incentives for the performance and disclosure of environmental audits. Instead of enacting a

formal state statute, Oklahoma recently adopted a state environmental regulatory agency policy regarding incentives to promote environmental auditing. There are distinct differences between an agency policy and a state statute in terms of administration and enforcement. Some of these differences make the adoption of a policy more attractive than the creation of a state statute.

A. Regulatory Background: The Oklahoma Department of Environmental Quality (DEQ)

As discussed in the preamble of Oklahoma's environmental audit incentives rule, the Department of Environmental Quality (DEQ) "monitors the environmental compliance of regulated entities" in Oklahoma. The duties and powers of the DEQ are defined in its organic statute. One of the duties enumerated is to act as the official agency of Oklahoma to cooperate with federal agencies in the enforcement of pollution control laws. Among its various powers, the DEQ has the authority to determine and assess administrative penalties. In addition, the DEQ has the power to investigate violations of environmental regulations, recommend civil and criminal prosecutions, review records, and conduct hearings. The DEQ's power to mandate environmental auditing stems from its authority to "require the maintenance of records and reports and the installation, use, and maintenance of monitoring equipment or methods and the provision of such information to the Department upon request."

B. Analysis of the Policy

Similar to some state environmental audit immunity statutes, Oklahoma's administrative rule is designed to provide incentives to establish a system of self-monitoring through the performance of internal audits followed by a reporting of the results to management and regulators. The incentives proposed in the rule include mitigation of administrative and civil penalties for voluntary reports of non-compliance. Such a system encourages regulated entities to play a substantial role in ensuring their compliance with environmental regulations rather than relying on the DEQ to force compliance through inspections, enforcement actions, and penalties.

The rationale behind the rule is that self-auditing should be promoted because regulated entities have a "superior vantage point" to observe and monitor compliance

177. Id. § 252:2-11-7(a).
179. See id.
180. See id. § 2-3-202.
181. See id.
182. See id. § 2-3-202(8).
184. See id.
185. See id.
and also have more resources at their disposal to ensure that environmental regulations are followed.\textsuperscript{186} Thus, the DEQ asserts that the regulated entities must play the primary role in ensuring their compliance with environmental laws and protecting the environment.\textsuperscript{187} This concept is especially true considering the decrease in funding available for regulatory enforcement at federal and state levels.\textsuperscript{188} In addition to helping regulators, the DEQ points out that adherence to the rule will enable regulated entities to concentrate their resources on ensuring compliance rather than on paying penalties.\textsuperscript{189}

Though the rule offers to mitigate penalties, the drafters of the DEQ rule maintain that administrative and civil sanctions still serve an important function in the enforcement process.\textsuperscript{190} Even though the role of economic penalties in ensuring enforcement is not as central as it once was, administrative fines are still necessary as a primary incentive for the performance of environmental audits and the monitoring of compliance with environmental laws. Without regulatory prodding through penalties, the free market provides little incentive to cover the spillover costs associated with environmental harm. The effects of environmental damage are for the most part indirect and, if not \textit{mala prohibita}, are simply viewed as just another cost of doing business that can be avoided.\textsuperscript{191} Thus, the DEQ does not offer to eradicate completely the use of penalties, rather only to mitigate them where appropriate. The DEQ offers penalty mitigation in cases in which a regulated entity discloses a violation, takes timely remedial action, and employs measures to prevent recurrence of the problem or similar violations in the future.\textsuperscript{192}

The DEQ outlines several specific factors that the agency will consider in deciding whether to seek administrative or civil penalties against a regulated entity that voluntarily reports a violation of environmental regulations.\textsuperscript{193} These requirements for the application of the rule are very similar to the factors listed in many if not all other state statutes or regulations designed to provide incentives for environmental auditing.\textsuperscript{194} First, the disclosure must be voluntary, complete, and in writing before the DEQ is aware of the problem or is likely to become aware through pending investigation. Second, the violation cannot be intentional. Third, the problem reported cannot evidence a lack of good faith in the attempt to comply with environmental regulations. Evidence of bad faith can be found in the failure to use an

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{186} See Okla. Admin. Code § 252:2-11-7(a) (1997).
\item \textsuperscript{187} See id. § 252:2-11-7 (setting forth the reasoning behind the DEQ's desire to increase regulated entities' involvement in ensuring compliance with environmental laws).
\item \textsuperscript{188} See Campbell, supra note 5.
\item \textsuperscript{189} See Oklahoma Dep't of Env'tl. Quality, Board Briefing Paper, Title 252: DEQ, Chapter 2: Procedures of the DEQ, Permanent Rulemaking, Executive Summary 1 (n.d.) (on file with the Oklahoma Law Review).
\item \textsuperscript{190} See id.
\item \textsuperscript{191} See William F. Funk \textit{et al.}, Administrative Procedure and Practice 15 (1997) (discussing the reasons that administrative regulations are necessary for ensuring the coverage of spillover costs in an unregulated market).
\item \textsuperscript{192} See Okla. Admin. Code § 252:2-11-7(b) (1997).
\item \textsuperscript{193} See id.
\item \textsuperscript{194} See, e.g., EPA's Final Policy Statement, supra note 29.
\end{enumerate}
\end{footnotesize}
"environmental management system" designed to meet the specific needs of the entity in question. Fourth, the reporting entity must have taken timely steps toward remediation. Fifth, measures must be employed, or the reporting party must agree in writing to employ, corrective actions which will prevent the recurrence of the violation or similar problems in the future. Sixth, any damage to the environment as a result of the violation must be corrected, if not already remedied. Seventh, the regulated entity must not have received any economic or competitive advantages as a result of its noncompliance. Finally, the reporting entity must cooperate with the DEQ in the investigation of the problem disclosed and in its remediation.\textsuperscript{195}

Even if a regulated entity fails to meet all of the required conditions for mitigation of penalties, the DEQ will take into consideration the nature and extent of any efforts by the reporting party to comply with the policy in deciding whether and to what extent to penalize a violator.\textsuperscript{196} Further, part [c] of the policy states that in the event a regulated entity meets all the requirements except number seven, dealing with economic gains as a result of noncompliance, the DEQ will limit its penalty to the recovery of those economic gains only.\textsuperscript{197} It is clear that the DEQ's intent is to provide incentives to audit and to further the goals of environmental protection rather than to punish violators. This is evidenced by the DEQ's willingness to offer penalty mitigation despite a failure to meet all the conditions required by the auditing policy. However, the last clause of the policy states that any mitigation of penalties offered by the DEQ is subject to agreements between the DEQ and the EPA.\textsuperscript{198} Oklahoma's policy thus offers no guarantee that the benefits for disclosing an audit will apply. Therefore, Oklahoma's policy is subject to the same limitation to which most other state audit protection statutes fall prey: the ultimate discretion of the EPA.

\section*{C. Operation of the DEQ Policy in Conjunction with the EPA's Final Policy Statement}

The two rules are very similar in the protections offered and in the conditions required. The DEQ policy's prerequisites are almost identical to the EPA's. In addition, both offer only qualified immunity from penalties and no privilege for voluntary audit reports. In fact, the DEQ's rule was considered as a model for the formulation for the EPA's final policy statement. A proposed version of the DEQ policy was submitted prior to the formulation of the EPA's final policy statement during the administrative comment period.\textsuperscript{199} The proposed draft of the DEQ policy submitted during the comment period strongly resembles the final version of the DEQ policy. Judging by the similarities of the DEQ and EPA policies, the Oklahoma policy may have provided the EPA with a working model of the type of policy the federal government would ultimately adopt. Thus, the DEQ policy may have played

\begin{itemize}
\item 195. \textit{See supra} note 192 (outlining the conditions or the application of the DEQ's audit incentives policy).
\item 196. \textit{See OKLA. ADMIN. CODE} § 252:2-11-7(c) (1997).
\item 197. \textit{See id.}
\item 198. \textit{See id.} § 252:2-11-7(d).
\item 199. \textit{See Gerald B. Davenport, Proposed Policy on Self-Reported Violations, Oklahoma Department of Environmental Quality (Sept. 8, 1994) (EPA Enforcement & Compliance Docket C-94-01 / II-C-12).}
\end{itemize}
a significant role in the formulation of the federal policy on incentives for environmental auditing.

Though the DEQ's rule cannot guarantee the EPA will not overturn its decisions to mitigate penalties, two factors indicate that it is unlikely the EPA would override any decision by the DEQ to mitigate penalties. First, the two policies are so similar. Second, the role the DEQ policy played in the establishment of EPA's policy and the existence of a positive working relationship between the DEQ and the EPA200 imply that deference will be afforded to the decisions of the DEQ. To reinforce this notion, Oklahoma's rule can be compared to a recent policy statement by the EPA.

The EPA policy sets out a number of factors it will consider in determining whether a state audit privilege and/or immunity statute contravenes federal authority to regulate the environment and prevents states from doing the job which the government has delegated the power to do.201 First, the EPA requires that states retain the ability to obtain an injunction against violators, regardless of whether a violation was reported through an environmental audit. The Oklahoma policy does not hinder the issuing of injunctions for violations. It only mitigates penalties. It does not completely eradicate them. Second, states must have the power to levy economic penalties against violators in order to level the economic playing field so that no party can benefit from a violation. The DEQ rule offers to mitigate only gravity-based penalties, not remedial penalties. Third, states must have the ability to gather information necessary for criminal investigations and prosecutions. The DEQ requires that companies cooperate with the investigating agency for the protections of the rule to apply.202 Finally, state audit protection laws must not interfere with the public's access to information regarding environmental violations.203 The DEQ policy affords no privilege for the information contained in an audit that would block the public's access to information regarding violations. Therefore, although the DEQ rule offers no guarantees, deference to its decisions is highly likely since the rule is almost identical to the EPA's policy and complies with the recently issued minimum requirements for a state audit incentive rule or law.

D. Choosing Administrative Rules Over State Statutes To Provide Incentives to Audit

As evidenced by statements made in the EPA's final policy statement, the EPA strongly opposes state audit protection laws which offer incentives such as a qualified privilege.204 With this in mind, Oklahoma and other states have opted to avoid

200. See Oklahoma Dep't of Envtl. Quality, Summary of Comments and Responses to DEQ's Proposed Audit Policy at 252:2-11-7, cmt. 3, response 2 (Aug. 8, 1996) [hereinafter DEQ Summary of Comments & Responses] (stating that there is a good working relationship between the EPA and the DEQ such that EPA will rarely override decisions of the DEQ regarding the mitigation of penalties).
203. See id.
increased federal scrutiny by adopting administrative policies for audit protection that resemble the federal policy rather than enacting state statutes that offer incentives besides penalty mitigation. By doing so, Oklahoma and other states that follow the EPA's lead may avoid offending the EPA with state laws that appear to federal regulators as an abuse of federally delegated power to regulate the environment. Therefore, Oklahoma avoids the risk of having its power to regulate the environment revoked because of an audit statute that runs contrary to the goals of the EPA.  

In addition to notions of not biting the hand that feeds, several procedural reasons exist for why a state regulatory agency would choose to adopt an administrative policy rather than seek the enactment of a state law. First, agency policies have the binding effect of law, but may be adopted and changed through quicker and more efficient processes than those required for the creation of a state statute. Second, enacting a policy rather than a state law affords the agency enforcing the rule greater flexibility in carrying out its regulatory mission. This flexibility arises because an agency's interpretation of its own rule enjoys great deference. Such deference may not otherwise be available in the case of the interpretation and enforcement of laws adopted by the state. For instance, an agency may refuse to take action in the enforcement of one of its rules without incurring any judicial scrutiny. In the case of environmental audit incentive policies, such discretion can work to the advantage of regulated entities that choose to comply with the rules. On the other hand, an agency's decisions of whether and to what extent to enforce state laws may be beyond the agency's discretion. Agency rules allow flexibility in enforcement. This flexibility results in a savings of scarce regulatory resources.

Besides the regulatory discretion, the third reason that agencies may prefer to adopt their own rules is because the procedures required in the enactment of administrative rules supply the agency with valuable information. Under section 553 of the Federal Administrative Procedure Act, agencies are required to provide the public with general notice of a proposed rule and must afford interested parties the opportunity to comment on the proposed rules. This procedure allows the agency to hear

205. See John H. Cushman, Jr., Battle Lines Form Over Environmental Disclosure Laws, J. Rec. (Oklahoma City), Apr. 22, 1996, available in 1996 WL 11095517 (stating that President Clinton has warned states that if they go too far in providing protections for environmental audits, the administration will "withhold the authority that is commonly delegated to states to enforce federal laws").

206. See PUNK ET AL., supra note 191, at 18.

207. For example, agency policies require no procedures except publication in the federal register; not even informal rule-making procedures such as notice and comment. See 5 U.S.C. § 553 (1994).

208. See PUNK ET AL., supra note 191, at 139 (recounting Chevron v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984) (stating that in the absence of a clear inconsistency with the statute, an agency's interpretation need only meet the standard of reasonableness)).

209. See id. at 431 (quoting Heckler v. Chaney, 470 U.S. 821, 830 (1985) (stating there are "several occasions . . . where an agency's decision not to prosecute or enforce, whether through civil or criminal process, is a decision committed to an agency's absolute discretion"). The Court in Chaney reasoned that agencies should be able to decide how their limited resources are spent in order to facilitate the pursuit of their statutory mandate. Chaney, 470 U.S. at 831.


211. See id. § 553; see also Oklahoma Administrative Procedures Act, 75 OKLA. STAT. § 303(A)
interested parties' opinions and suggestions regarding the proposed rule, thus facilitating the adoption of a policy that most people can live with and avoiding problems in the future. "[U]tilizing rulemaking procedures opens up the process of agency policy innovation to a broad range of criticism, advice, and data that is ordinarily less likely to be forthcoming . . ."

E. Adequacy of the DEQ Rule from the Perspective of the Regulated

Following its notice of the proposed rule, the DEQ summarized the comments it received regarding the audit incentives policy. Most of the input from the parties that submitted a comment was positive. For instance, a comment submitted from the Environmental Foundation began by applauding the DEQ for its reduction of the self-reporting policy to writing. Even Coors Brewing Company, an entity well aware of the dangers inherent in reporting violations, stated that a policy such as the DEQ's is a "positive step forward toward encouraging the voluntary disclosure of environmental violations." Coors went on to say that it "heartily supports Oklahoma's assessment of the need to provide relief from civil penalties for self-reported violations."

Despite the positive input provided by most of the comments, suggestions for change were also submitted. For instance, Mobil Exploration and Producing U.S. (MEPUS) articulated its concern that certain revisions should have been included in the rule to prevent Oklahoma from being placed at a disadvantage relative to other states regarding its ability to attract industry. Specifically, MEPUS recommended that the DEQ clarify how it will decide when a company has gained a "significant economic or competitive advantage as a result of non-compliance." In response to this suggestion, the DEQ stated that it thought the language regarding economic advantage is sufficiently clear but that it can be clarified as needed on a case-by-case basis. In addition, MEPUS stated that the DEQ must provide a means of assuring regulated entities that a decision by the DEQ to mitigate penalties will not be overridden by the EPA. The DEQ responded to this recommendation by stating that while it cannot guarantee that the EPA will not overturn the decisions of the DEQ, such a reversal will be rare due to the positive working relationship between the EPA and the DEQ.

(Supp. 1995).

213. See DEQ Summary of Comments & Responses, supra note 200.
214. See id. at cmt. 1.
215. Id. at cmt. 4.
216. Id.
217. See id. at cmt. 3.
219. See DEQ Summary of Comments & Responses, supra note 200, at cmt. 3.
220. See id.
221. See id.
Coors Brewing Company submitted suggestions for change in conjunction with its favorable comments regarding the DEQ rule. Coors called for an increase in the protections offered by the rule. Specifically, Coors recommended that the DEQ provide a qualified privilege for environmental audit reports disclosed pursuant to the rule. In response, the DEQ stated that such a privilege is unnecessary because regulated entities will have sufficient incentive to perform audits under the protections already offered.

F. Reasons for the DEQ's Failure to Offer a Qualified Privilege for Audits

Besides the response to the Coors comment given by the DEQ, there are several other possible reasons that the agency may have opted not to offer privileged status as an incentive to perform environmental audits. First, it can be argued that audit privilege laws foster an unrealistic and irresponsible notion that companies can avoid liability for their improper actions simply by keeping them a secret. Civil and administrative enforcement actions are the only way to ensure that regulated entities take responsibility for actions that negatively impact the environment. If the information contained in an environmental audit is elevated to the level of privileged status, enforcement actions related to the information reported in an audit become almost impossible because the information in question cannot be accessed. The object of environmental audit incentive laws is to encourage companies to perform audits in order to further the goal of environmental health and safety through a monitoring of compliance with environmental laws. If audit incentive laws provide regulated entities with a means of skirting responsibility for their actions by allowing them to avoid enforcement suits, then the benefits offered in the policy defeat the purposes for which the policy was established. Further, when regulators offer to mitigate the penalties imposed by civil or administrative enforcement actions, companies have little to fear by going to court. Once punitive penalties are mitigated, all an enforcement suit will require of a company is that it take responsibility for remediating the damage it caused to the environment. By allowing regulated entities to evade enforcement suits, evidentiary privileges may enable companies to avoid cleaning up their own messes, and thereby to dodge one of the most elementary notions of responsibility.

Preemption is the second reason that the DEQ may have decided not to offer a qualified privilege for audit materials. Most federal and state environmental protection statutes require prosecution of violators of the statutory provisions. Because evidentiary privileges seriously inhibit regulators and the public from engaging in enforcement actions, the privilege may prevent the implementation of federal law. When the application of a state law conflicts with the enforcement of federal statutes, the Supremacy Clause provides that state statutes must yield to federal law. The United States Supreme Court has found that a state law that "stands as an obstacle to the accomplishment and execution of the full purposes and

222. See id. at cmt. 4.
223. See id.
224. See U.S. CONST. art. VI, cl. 2.
objectives of Congress" is in actual conflict with federal law and is thus preempted.225 By shielding violators from enforcement actions, audit privilege laws may defeat the congressional goals behind environmental regulations. Therefore, state laws that contain such privileges may be found to be inapplicable due to federal preemption.

A third reason that may have influenced the DEQ not to offer a qualified privilege is that such provisions often contain many limitations in order to avoid abuse by regulated entities and also to prevent the exceptions from swallowing the rule. Thus, a privilege provision is often an ineffective protection and is therefore unnecessary. An examination of a typical audit privilege provision illustrates the limitations that render such protections meaningless. Louisiana has chosen to adopt an audit privilege law.226 Considering just the sheer number of exceptions provided, it is easy to see why the DEQ may have been hesitant to offer a qualified privilege as an incentive

226. See H.B. 2083, 1995 Leg. Sess. (La.). Section 2514 of the Louisiana law outlines the circumstances in which the self-evaluation privilege will not apply. First, information or materials gathered pursuant to a permit or an order are exempt from the privilege. Second, information or documents required to be reported under an environmental law fall outside the privilege. Third, any information that a regulatory agency gathers on its own is not subject to the privilege. Fourth, the privilege will not be extended to any information received through an independent source, notwithstanding its inclusion in an audit report. Fifth, any records compiled independent of or before an audit is performed are also exempt from the privilege. Sixth, any information gathered independently of an audit or following its completion is discoverable. Seventh, factual information contained in an audit report, revealed by a person who played a part in the performance of the audit and who has actual knowledge of the events that constitute the violation in question are admissible in court. It is not inconceivable to imagine an auditor, or any other personnel assisting in the performance of an audit, revealing the information he gathered, for any number of reasons. This may be especially true if the violation catalogued in the audit has resulted in severe damage to human or environmental health. Eighth, the actual existence of the audit report is discoverable, along with the subject matter of its contents, the dates it was conducted, and the names of the persons who performed the audit. Once the existence of an audit is revealed, along with the subject matter of the violation it contains, the interest of third parties may be sparked. If an independent source is then able to gather information about the audit in question, the materials obtained by the third party will be exempt from the privilege under the fourth and sixth exceptions mentioned above.

In addition to the aforementioned exceptions to the application of Louisiana's audit privilege statute, section 2513 of the bill provides another list of circumstances in which the privilege will not apply. First, the privilege is inapplicable where it has been waived by the auditing party. Second, upon a finding that the audit report evidences noncompliance and a failure to take steps to remedy the violation within thirty days, an administrative law judge (ALJ) may refuse the application of the privilege. Third, the privilege will not apply where a court finds that the audit report is being compiled for fraudulent purposes. Fourth, where an ALJ finds that the report is being used to cloak a violation from disclosure in a pending administrative or civil proceeding, the privilege is inapplicable. Fifth, the privilege will be waived where it is determined that the violation reported constitutes a significant threat to human or environmental health and safety. The bill fails to define the term "significant," leaving broad discretion to regulators in determination of the gravity of the violation reported. Finally, any third party possessing independent knowledge that one of the thirteen exceptions applies may gain access to the audit report in order to observe under an in camera review. In light of this final exception, it is conceivable that a third party could gain access to the audit report, learn of its contents, and then apply the fourth exception of section 2514, dealing with independent sources, to relay the contents of the audit to regulators, thereby exempting the information reported from the protection of the privilege.
for auditing. As the DEQ stated in its response to Coors' comment recommending such a privilege, the protections offered under the current rule are sufficient to perform the task the law was designed to achieve: providing regulated entities with an incentive to perform environmental audits. In addition, regulated entities may rely on the limited privileges provided by traditional legal doctrines such as the attorney-client privilege and work product doctrine. Though these privileges have their limitations, they are still effective, especially in conjunction with the benefits offered in an auditing incentives policy such as the one adopted by the DEQ.

Regulated entities have a legitimate interest in avoiding being haled into court as a result of a voluntary audit. However, there is little to fear when companies can rely on a mitigation of any punitive administrative or civil penalties, as offered in exchange for compliance with the Oklahoma rule. At most, regulated entities may be held accountable for the damage they caused and for any advantages they may have realized as a result of their noncompliance. Companies that complain about this sort of liability could stand to pay a visit to a local kindergarten. While in attendance, there are a few simple rules that we all learn to follow: clean up your mess and return what does not belong to you.

VII. Conclusion

Due to the possibility of penalization, the importance of environmental laws has become clear to most regulated entities. Environmental threats are serious, and regulations to protect the health of our surroundings are necessary. Numerous arguments circulate in the media that explain away almost every environmental problem of which we are aware today. However, any doubts regarding the reality of environmental threats can be dispensed with easily by reference to the sheer number of environmental regulations contained in the endless volumes of the Federal Register. The government obviously takes environmental health and very safety seriously. It expends millions of dollars each year in the formulation of environmental laws and the support of regulatory agencies that enforce them. Rarely in the history of policy making has the federal government established such a multitude of antecedent safeguards to defend against a threat, the existence of which the public is not yet entirely convinced.

In the most maternalistic sense, environmental regulations punish in order to protect us from ourselves. If people really knew the harm they inflict on themselves by damaging the environment that supports them, they would be more cautious. Despite a history of ambivalence, some awareness of the importance of environmental protection on the part of regulated entities has clearly blossomed. Voluntary environmental audits illustrate such awareness. Command and control regulation, focusing on punishment, is not necessary. Environmental audit incentive policies like Oklahoma's strongly encourage self-monitoring by the regulated community. Oklahoma's audit incentive policies provide incentives to audit without compromising the goals of federal regulations established to ensure environmental protection. Thus, the DEQ's policy will perform the tasks it was designed to accomplish.

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