

LEGAL UPDATES

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# Fraudulent Identification Numbers Issued Under EPA's Renewable Fuel Standard: Buyer Beware

The Environmental Protection Agency (EPA) has been heavily criticized by the media and members of Congress for its oversight of Renewable Identification Number (RIN) transactions under the Renewable Fuel Standard (RFS2). The criticism began in October 2011 after the owner of Clean Green Fuels was charged with wire fraud, money laundering and violating the Clean Air Act (CAA) for generating and selling more than 32 million RINs without producing any qualifying renewable fuel. Criticism of EPA intensified after the agency began pursuing enforcement actions for CAA and RFS2 violations arising from the purchase and use of the invalid 2010 and 2011 RINs. On November 7, 2011, EPA issued violation notices to 24 companies that used invalid RINs purchased from Clean Green Fuels to demonstrate compliance with the RFS2. In subsequent months, EPA continued issuing violation notices to additional companies, including Absolute Fuels, which allegedly generated and sold over 48 million fraudulent RINs to other companies.

Under § 211(o) of the CAA and RFS2 regulations, exporters of renewable fuel and obligated parties, meaning refiners and importers of gasoline or diesel fuel, must acquire enough RINs to demonstrate compliance with their Renewable Volume Obligation (RVO) for renewable fuel, advanced biofuel, biomass-based diesel and cellulosic biofuel. Obligated parties and exporters of renewable fuel must comply with their RVOs by generating RINs or purchasing valid RINs through the RIN credit trading program. Although the EPA requires all companies participating in the trading program to register as a producer or importer of renewable fuels prior to generating or selling RINs through the EPA Moderated Transaction System (EMTS), the RFS2 regulations explicitly state that purchasers are responsible for determining the validity of all RINs purchased through the EMTS.

The trading program does not have a safe harbor provision for parties who purchase invalid RINs with a “good faith belief” that the RINs were valid at the time of purchase. Consequently, all of the companies that used the fraudulently generated RINs to demonstrate compliance with their RVOs violated the RFS2 prohibition against the use of invalid RINs. Additionally, the companies may have also violated the RFS2 by failing to acquire a sufficient number of valid RINs to satisfy their RVOs. The RIN trading program’s prohibition against the use of invalid credits regardless of the purchaser’s good faith belief is consistent with other EPA fuel programs, such as the Nonroad, Locomotive and Marine (NRLM) low sulfur diesel fuel program. Unlike the RIN trading program, the EPA has never issued violation notices to parties that acquired and used credits that were later found to be invalid under the low sulfur diesel fuel programs. During the gasoline lead phase down in the 1970s and 1980s, however, the EPA pursued enforcement actions against companies that inadvertently purchased fraudulent lead credits and used the invalid credits to demonstrate compliance.

### **EPA’s Interim Enforcement Response Policy**

In an effort to streamline the resolution of the violations arising from the unknowing purchase and use of the fraudulent RINs, the EPA issued an interim enforcement response policy in March 2012. The policy applies a streamlined settlement approach to resolve “use violations” that arose from invalid RINs to demonstrate compliance and “shortfall violations” that arose from a failure to acquire sufficient valid RINs. As part of this settlement process, companies must submit a RIN Integrity Report and implement appropriate remedial actions, including resubmitting annual RVO reports after removing the invalid RINs and, depending on the type of violation, retiring the requisite number of 2011 and 2012 RINs.

The civil penalties provision of the interim enforcement response policy provides a compelling incentive for companies with multiple violations to settle with the EPA. Under the CAA, a civil penalty of up to \$37,500 per day may be assessed for each violation, plus the economic benefit or savings resulting from each violation, but under EPA’s interim policy, companies are paying 10 cents for each use violation and 20 cents for each shortfall violation arising from the invalid RINs. The policy also caps the total penalty for any use or shortfall violation arising from invalid RINs generated by individual renewable fuel producers or importers at \$250,000 and caps the maximum penalty for each type of violation at \$350,000.

As of April 18, 2012, the EPA had reached 31 settlement agreements after implementing its interim policy. Thus far, companies have agreed to pay approximately \$3.7 million, with individual settlement amounts ranging from \$440 to \$350,000. An unknown number of companies have not entered a settlement agreement, and at least one company has chosen to litigate the issue. OceanConnect, a RIN brokerage firm, filed a lawsuit against the EPA on March 15, 2012, alleging that the EPA failed to

exercise due diligence in its management of the RIN credit trading program and its investigation of Clean Green Fuels.

### **What This Means for RIN Purchasers**

Although the EPA's interim policy reduced the penalties for violating the RFS2 in 2010 and 2011, the agency intends to retain its "buyer beware" policy and expects all purchasers to develop adequate policies and procedures for ensuring the validity of RINs used to demonstrate compliance with RVOs. In its interim policy, the EPA repeatedly warned that it intends to take a more aggressive enforcement approach for violations arising from the use of RINs generated in 2012.

At the same time, however, the EPA has stated that it will begin notifying purchasers of potentially invalid RINs by posting information on its website, on a case-by-case basis, unless notifying the public would "unduly impair" the EPA's investigations. Regardless, RIN purchasers should not rely on a decision by the EPA to not pursue an enforcement action as evidence of the validity of a particular RIN. Unless the EPA provides guidance on the policies and procedures that a RIN purchaser could implement to ensure that it is acquiring valid RINs, the significant degree of uncertainty and confusion surrounding the RIN trading program will likely steer RIN purchasers toward larger, established renewable fuel producers.

### **Contact Info**

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