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18th Annual Environmental Law Institute

Office of Continuing Legal Education at the University of Kentucky College of Law

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SECTION A
INTRODUCTION

The Environmental Defense Council devotes most of its website to the "rollback" of environmental progress by the George W. Bush Administration and has published a book entitled "Rewriting the Rules: The Bush Administration's Assault on the Environment." While the Bush Administration has reversed a number of the prior administration's environmental policies, its influence has yet to be seen in court decisions.

LAND USE


The Tahoe Regional Planning Agency imposed a 32-month moratorium on development in the Lake Tahoe Basin while formulating a comprehensive land-use plan for the area. Real estate owners affected by the moratorium filed suit claiming the agency's action constituted a taking without just compensation. Overruling the district court, the Court of Appeals for the Ninth Circuit held that because the moratorium had only a temporary impact on the property owners' interest, no compensable taking had occurred. The U.S. Supreme Court agreed, holding that the moratorium imposed by the planning agency was not a per se taking of property requiring compensation under the Takings Clause of the United States Constitution.

There are two types of takings - direct government appropriation of property and government regulation that imposes such a severe restriction on property usage that it produces nearly the same result as direct appropriation. The moratoria placed on the Lake Tahoe Basin property were regulatory in nature.

A regulation constitutes a taking when it either does not substantially advance a legitimate state interest or it denies the owner economically viable use of the property at issue. Because of potential damage to the lake, the district court rejected the first alternative. However, as the regulation imposing the moratoria did not contain an express termination date, the district court held the affected property owners were entitled to compensation for the regulatory taking. The appellate court reversed, holding that because the regulations had only a temporary impact on the property owners' interest, a categorical taking had not occurred.

According to the U.S. Supreme Court, whether a temporary moratorium constitutes a taking depends on the particular circumstances of the case. The Court distinguished acquisitions of property for public use and regulations
prohibiting private uses. The Court noted that, under a prior case, _Lucas v. South Carolina Coastal Council_, compensation is required only when a regulation deprivs a property owner of all economically beneficial uses of the property. The Court also noted that if it were to rule in favor of the Lake Tahoe property owners and create a categorical rule in the interest of fairness and justice, every regulatory delay would become a taking. The Court ultimately held that a temporary restriction that merely causes diminution in value does not constitute a compensable taking.

- **Southwest Williamson County Community Association, Inc. v. Slater, et al. 243 F.3d 270 (6th Cir. March 14, 2001)**

Southwest Williamson County Community Association filed a motion for a preliminary injunction to halt construction of a 77-mile length of highway designed to bypass Nashville, Tennessee. The district court denied the motion after finding that Southwest was not likely to succeed on the merits of the case. The appellate court affirmed the denial. The Sixth Circuit Court of Appeals held the district court did not abuse its discretion in finding that construction of a highway corridor was not a "major federal action" requiring the Federal Highway Administration to respond to the state's environmental assessment with certain documentation of environmental impact. Typically, a project is considered a major federal action when it is funded with federal money. However, a state-funded project may become a major federal action upon involvement of multiple federal agencies. Major federal actions are bound by the National Environmental Policy Act (NEPA) to perform additional environmental reviews.

The appellate court held there are two alternative bases for finding that a non-federal project constitutes a "major federal action" invoking NEPA requirements: (1) when the non-federal project restricts or limits the statutorily prescribed federal decision-maker's choice of reasonable alternatives; or (2) when the federal decision-makers have authority to exercise sufficient control or responsibility over the non-federal project so as to influence the outcome of the project. The court concluded that the state's work on the highway did not restrict the federal decision-makers' choice of reasonable alternatives. The court further concluded the relevant decision-makers did not have authority to exercise sufficient control or responsibility over the highway construction so as to influence the outcome of the project. Construction of the highway did not involve federal funding. Further, no federal agency had jurisdiction over the non-federal project.

Plaintiff filed a motion for preliminary injunction to restrain issuance of a surface-mining permit to mine a ridge top in the headwaters of a creek. Defendant performed a cumulative hydrologic impact assessment (CHIA) and concluded that the project was designed to prevent material damage to the creek. Plaintiff alleged that in conducting the assessment and reaching its conclusions (1) Defendant relied upon inadequate baseline sampling of the streams; (2) the material damage limits of the CHIA were inadequate; (3) the creek’s placement on the Clean Water Act § 303(d) list of streams impaired by pollution precluded a finding that the project was designed to prevent material damage to the stream; and (4) the lack of baseline data rendered the plan useless. The United States District Court for the Southern District of West Virginia, Huntington Division, denied Plaintiff’s motion holding Plaintiff was unlikely to succeed on the merits of the case.

The district court considered several factors in ruling on Plaintiff’s preliminary injunction motion. The court found Plaintiff was unlikely to succeed on the merits of the case. The court recognized Defendant’s discretion to determine baseline data, Defendant’s discretion to determine a material damage limit, the current relatively good condition of the creek since being placed on the § 303 list, and found that Defendant did not violate its duty with regard to its monitoring plan which the West Virginia Department of Environmental Protection determined to be sufficient. Additionally, the court balanced the potential harm to Plaintiff, Defendant, and the surface mine operation. The court held the evidence did not support a finding that the activities at issue would cause or contribute to water quality violations. Further, Plaintiff’s right to pursue administrative review mitigated any harm.

AIR

• Wall v. U.S. EPA, 265 F.3d 426 (6th Cir. Sept. 11, 2001)

Plaintiffs, residents of Ohio, challenged the US EPA’s determination that the metro Cincinnati Area State Implementation Plan (SIP) would comply with ground level ozone level standards and provided the requisite commitments to guarantee enforcement of air quality standards. Plaintiffs, who were joined by the Sierra Club, contended that redesignation from moderate nonattainment to an attainment area under the Clear Air Act (CAA) was precluded because the plans submitted by Kentucky and Ohio failed to adopt rules relating to reasonably available control technologies (RACT).

US EPA had reviewed the plans submitted in November 1993 by Kentucky and Ohio and after finding various deficiencies never published a
notice of disapproval as required by CAA because in November 1994 the states submitted a request for redesignation. The requests were based on the fact that the area had not violated the ozone standards over the previous 3-year period. The requests were denied because the Cincinnati area experienced an ozone violation in 1995. The US EPA granted two one-year extensions for the states to show compliance with the standards.

In 1999 Ohio and Kentucky had again requested redesignation based on three years of data. In January 2000 the US EPA published a notice that the request would be approved. The agency acknowledged that Kentucky did not have fully approved transportation conformity requirements in its SIP because “areas are subject to the conformity requirements regardless of whether they are designated attainment.” The US EPA also acknowledged that Ohio had not fully adopted the RACT rules. The agency proposed to depart from its policy of requiring full adoption, submission and approval of RACT rules prior to approval of a redesignation request.

The court vacated the US EPA’s action to redesignate the Cincinnati metropolitan area and remand for further proceedings consistent with the opinion. The court held that the agency reasonably concluded that air quality modeling was not required in evaluating the maintenance plans submitted by the states, since the demonstration of attainment was not also required, and the data used to develop a major transportation emissions program was not applicable to the evaluation of maintenance plans. Further, there was no express requirement that the plans contained current enforcement commitments. Also, the partial failure to comply with transportation-conformity requirements did not preclude redesignation. However, the Ohio plan’s optional contingency measures could not be substituted for the statutorily required adoption of the RACT rules, and the redesignation without adoption of the rules would be invalid.


In October, 1998, EPA issued the "NOx SIP Call", a final rule under the Clean Air Act requiring 22 states and the District of Columbia to revise their state implementation plans (SIPs) to impose additional controls on nitrogen oxide (NOx) emissions. Under the NOx SIP Call, each upwind state had to limit its summertime NOx emissions to a statewide emission budget for the year 2007. In setting the NOx budgets, EPA relied on emission inventory data collected by the Ozone Transport Assessment Group and divided each state’s NOx emissions according to five source types. It then obtained source-specific utilization data and applied growth factors derived from growth projections for the years 2001 through 2010. In the final NOx SIP Call rule, EPA reopened public comment on the accuracy of the data upon which it had based its emission inventories and
budgets. Petitioners challenged the data used to create the state emission budgets, particularly the budget determinations for electric generating units (EGUs).

The court held that when EPA reopened comment on the emission baselines, it also reopened comment on the growth-rate methodology used because EPA's rulemaking notice was ambiguous. The court then noted that "agency determinations based upon highly complex and technical matters are entitled to great deference." However, the EPA must be able to fully explain the basis upon which it makes its determinations. The court remanded the EPA's EGU growth factor determinations for further reasoned decision making. The court also remanded EPA's redefinition of EGUs for further consideration in light of its insufficient notice and opportunity for comment. The court further vacated and remanded the statewide budget specific to Missouri based on EPA's lack of an analytical basis for its ozone standard calculations.


EPA promulgated a rule in response to petitions from several northeastern states that nitrogen oxide (NOx) emitted in neighboring states was harming their local air quality. The rule required several NOx-emitting facilities in midwestern and southeastern states to conform to EPA set emission limits and participate in an emissions trading program. Petitioners challenged the rule as inconsistent with the Clean Air Act (CAA), arbitrary and capricious, and technically deficient.

In October 1998, EPA issued a request for 22 states and the District of Columbia to revise their state implementation plans (SIPs). Prior to that, eight states had petitioned EPA to find, under § 126 of the CAA, that certain sources in specified states were contributing to their failure to meet air quality requirements for ozone. EPA adopted an "automatic trigger mechanism" which provided that a formal finding would be made under § 126 if by an EPA set deadline, EPA had not approved a state's SIP revision to comply with the NOx SIP call or promulgated implementation plan provisions under § 110 of the CAA. Petitioner's argued that the CAA included an element of "cooperative federalism" under which EPA determines requisite levels of air quality, but must defer to the states on how to achieve those levels. The appellate court noted that it grants a high level of deference to agency interpretation and opted to defer to the EPA's timetable as it was not plainly erroneous or inconsistent with CAA regulations.

Other petitioners challenged the methodology by which EPA reached its findings of significant contribution to nonattainment of ozone under CAA § 126 claiming that findings based on all emissions could not determine whether stationary source emissions were sufficient. The appellate court again deferred to EPA determinations. The court also deferred to EPA's refusal to reopen and
reconsider its significant contribution findings with regard to the state of North Carolina and a report submitted by the state, which EPA concluded was too preliminary.

Additionally, to allocate NOx emission allowances to individual sources, EPA made state-by-state emission projections for 2007. The projections were based on projected 2007 heat input for electric generating units (EGUs) and non-EGU industrial facilities. The projections were developed from computer models working off baseline data from 1995 and 1996. Petitioners challenged EPA's budget allocations as arbitrary and capricious. The appellate court noted that it typically upholds EPA's authority to make emission projections and set limitations. However, only in those situations where EPA has adequately responded to comments and explained the basis for its decisions. The appellate court ultimately upheld a portion of EPA's applications, but remanded EPA's model-derived growth factors for further explanation. While agency determinations on highly complex and technical matters are entitled to great deference, EPA must be able to explain its determinations and provide a complete analytical defense should its model be challenged. In this instance, the appellate court determined the agency's growth factor determinations were oversimplified and thus unreasonable. The appellate court similarly remanded EPA's classification of cogenerators.

Petitioners also challenged EPA's authority to impose NOx cap limits on future, un-proposed, stationary sources under CAA § 126. The appellate court employed a two-prong test in reviewing EPA's determination. First, the court considered whether Congress had spoken directly to the issue. The court found sufficient ambiguity in the statutory language to move to the second prong, whether the agency's determination was reasonable. The appellate court held EPA's determinations were reasonable with regard to the inclusion of future sources. The 1990 amendments to the CAA allowed EPA to make findings with regard to "any major source or group of stationary sources". Additionally, CAA § 110 and § 126 confer authority based on the type of activity without temporal limits. The court held it was reasonable to include future sources in the group of stationary sources it was attempting to regulate.

Finally, non-EGU petitioners demanded remand and reallocation of all emission allowances because of alleged errors in the initial allocation. The appellate court held petitioners waived their claims by failing to object with reasonable specificity during the period for public comment. Petitioners had failed to provide EPA with sufficient information during the comment period.


  EPA disapproved Michigan's revisions to a state implementation plan (SIP) which permitted an automatic exemption for a source that violated
emissions standards if that violation resulted from startup, shutdown, or malfunction and met certain other criteria. The United States Court of Appeals for the Sixth Circuit affirmed the EPA's conclusion that the proposed SIP revision did not meet Clean Air Act requirements. EPA's interpretation of the Clean Air Act was not unreasonable as the proposed SIP revision provided no means for the state to enforce attainment and maintenance of national ambient air quality standards.

HAZARDOUS & SOLID WASTES/SUBSTANCES


The Kentucky Natural Resources and Environmental Protection Cabinet (Cabinet) issued a permit to the U.S. Department of Energy (DOE) for the construction and operation of a contained solid waste landfill at the DOE's Paducah Gaseous Diffusion Plant, an active uranium enrichment facility. The operating permit restricted disposal of radioactive materials in the landfill. The DOE challenged the permit on the grounds that (1) the Atomic Energy Act of 1954 preempted state regulations relating to the disposal of radioactive materials; (2) the permit conditions violated federal sovereign immunity from state regulation; and (3) the state failed to comply with its own statutes and regulations in imposing the permit conditions. The Cabinet filed a motion to dismiss claiming that (1) the Declaratory Judgment Act and the Burford abstention doctrine afforded the district court discretion to decline jurisdiction; (2) the DOE failed to state a claim; and (3) the challenged permit conditions complied with Kentucky law.

The district court concluded that the Cabinet's attempt to impose conditions on the DOE's disposal of radioactive materials was preempted by federal law. The appellate court affirmed holding the Atomic Energy Act preempts the field of state regulation of radioactive materials. The appellate court further noted that neither the Atomic Energy Act, nor any other federal law, waives federal sovereign immunity from regulation of DOE facilities with respect to materials governed by the Atomic Energy Act. Thus, the U.S. had not waived it immunity with respect to the permit conditions at issue. Finally, the appellate court held the district court properly found abstention to be inappropriate. Determination of the questions at issue did not require a detailed analysis of state law, which might have indicated a state court was better suited to consider the case.

Plaintiff filed suit challenging the constitutionality of Ohio waste processing restrictions. The Indiana landfill at which Plaintiff preferred to dispose waste declined to meet the Van Wert Solid Waste Management District’s conditions for designation as an approved disposal site. Specifically, the landfill declined to collect a per-ton surcharge and remit it to the district. Absent non-collection of the surcharge, the landfill could have been approved as a designated landfill. The district court held, and the Sixth Circuit Court of Appeals affirmed, that dismissal of Plaintiff’s suit was proper. The surcharge restriction did not violate Plaintiff’s constitutional rights under the Commerce, Equal Protection, or Due Process Clauses. The restriction was not territorially based – Plaintiff was not forbidden to dispose of waste at its preferred landfill simply because it was located in Indiana. No landfill was arbitrarily excluded. Further, the restriction bore a relation to the defendant’s police power.

• Franklin County Convention Facilities Authority v. American Premier Underwriters, Inc., et al., 240 F.3d 534 (6th Cir. Feb. 13, 2001)

Plaintiff acquired property from several railroad companies who agreed to remain responsible for any claims that might affect any portion of the premises. While digging with a backhoe on the property, Plaintiff’s contractor accidentally uncovered and split open a box that had been buried at the site. Chemical analyses revealed the box contained creosote mixed with benzene. None of the parties were aware of the box prior to its unearthing. Defendant, the surviving successor of the several railroad companies, declined to accept financial responsibility for the resulting remediation. Plaintiff sued.

The Court of Appeals for the Sixth Circuit affirmed the district court’s findings that the substance found in the box was a hazardous substance under CERCLA and held that Plaintiff substantially complied with the National Oil and Hazardous Substances Pollution Contingency Plan. The appellate court further held the lower court did not err in determining that Defendant was an owner or operator of the property at the time the hazardous substance was deposited. A colored lithograph from 1853 showed the property was used as a pasture at that time. As of 1864, tracts of the property were acquired for railroad use. Thus, while there was no direct evidence as to ownership, the court did not err in its reliance on circumstantial evidence.

However, the appellate court disagreed with the district court’s determination that Plaintiff was an innocent landowner. Plaintiff’s contractor split open the box. Further, the appellate court held Plaintiff did not take sufficient action to prevent seepage from the box upon its discovery. Nevertheless, the
appellate court refused to reverse the determination of the district court that Defendant was liable for a 100% contribution share of the recovery costs. Equitable factors, such as Defendant’s refusal to participate in cleanup efforts and its contractual agreement to remain responsible for claims which might affect the property justified allocation of total liability to Defendant.

Additionally, the appellate court affirmed the district court’s award of attorney fees as a necessary CERLCA response cost and held that the retroactive application of CERCLA did not violate substantive due process or the Takings Clause. Apportionment of response costs to Defendant fulfilled Congress’ goal of spreading costs to responsible parties. Further, Defendant contractually retained liability for any claims related to the property.


The Sixth Circuit Court of Appeals affirmed the district court’s finding that a defendant company and its sole shareholder were jointly liable under CERCLA for clean-up of a contaminated site. The sole shareholder controlled transactions that constituted CERCLA violations in which the company was involved. Equity and CERCLA’s broad legislative purpose directed the shareholder be held responsible for the damage.

Defendant company engaged in both the legitimate business of selling and purchasing motorcycle parts and machinery and an illegitimate business involving used electrical transformers containing PCBs. While the sole shareholder did not control every aspect of the company affairs, he clearly controlled the particular PCB transactions for which the company was held liable for CERCLA violations. Under Ohio law, a shareholder is liable for the wrongdoing of the corporation of which he is an owner if (1) his control over the corporation is so complete that the corporation has no separate existence; (2) his control over the corporation was exercised in such a manner as to commit a fraud or illegal act; and (3) injury results from the wrong doing. The court noted there was no dispute that the defendant shareholder used his control over the corporation to violate the law and that injury resulted. The court then looked to several factors to determine whether the defendant corporation was the alter ego of its shareholder and determined that the shareholder’s control of the corporation was sufficient to pierce the corporate veil. The appellate court affirmed.


This was an action under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA) to determine strict liability for
past and future response costs of a prior owner/operator. Both parties moved for summary judgment. The court denied both motions. There was no evidence to indicate Defendant had engaged in any type of activity that would have produced the hazardous materials found at the site, which resulted in denial of Plaintiff’s motion. Defendant’s summary judgment motion was denied because Plaintiff produced sufficient evidence to show it had incurred at least one recoverable cost in response to the release, that being a Phase II site assessment. Plaintiff was further limited to an action for contribution because it was unable to show it was entitled to the innocent landowner defense.

Plaintiff purchased the property in 1985. Defendant did not notify Plaintiff that it had placed hazardous substances on the property and Plaintiff did not perform an environmental assessment. Plaintiff thereafter used the property to store empty shipping containers. Contamination was discovered when Plaintiff attempted to sell the property. The prospective purchaser decided not to purchase the property and Plaintiff filed suit seeking a declaratory judgment that Defendant was strictly liable as a prior owner and operator of the site at the time hazardous wastes were disposed of. Defendant counterclaimed alleging Plaintiff was jointly and severally liable as the current property owner.

There are two ways for private parties to recover response costs. 42 U.S.C. § 9607(a) authorizes recovery from responsible parties, or in the alternative, establishes joint and several liability. 42 U.S.C. § 9613(f) allows responsible parties to seek contribution from other responsible parties. Liability under either section rests on four elements. Although Plaintiff was able to show there had been (1) a release, (2) at a facility covered under CERCLA, (3) that caused Plaintiff to incur response costs, Plaintiff was unable to prove the fourth element — that Defendant was among the classes of persons subject to liability. There was no evidence presented to show the hazardous materials were placed on the site when Defendant owned the property. Further, Plaintiff was not able to recover under the innocent landowner defense because Plaintiff was unable to show that it had made any attempt to remove the contamination once it was discovered.
INSURANCE


Defendant insured plaintiff, Olin Corporation, under a comprehensive general liability policy. Plaintiff filed suit for indemnification of certain environmental cleanup costs. A pollution exclusion clause in the policy meant Defendant was only responsible for liability resulting from accidental damage. Following a jury trial, the United States District Court for the Southern District of New York held the policy term “accident” applied to the matter. The court held this term did not only apply to events that happened abruptly or quickly. Rather, the term included unintended damage irrespective of the time period over which the damage occurred. The Court of Appeals for the Second Circuit affirmed this decision.

However, prior to the district court’s bench trial, the jury had determined that only a portion of the damages resulting in injury to the soil was caused by accident. Olin thus had substantially greater coverage for injury to groundwater than it did for injury to soil. Unfortunately, Olin had spent considerably more money remediating soil contamination. The district court ultimately held that coverage of costs for groundwater remediation did not include coverage of costs for soil cleanup. The Court of Appeals for the Second Circuit affirmed this decision as well.

The court further held, and the appellate court affirmed, that cleanup costs should be apportioned pro-rata over all the years in which there was injury to the property, and that the full policy deductible applied in each triggered policy year.

NATURAL RESOURCES


Citizens and an environmental group filed suit against the Director of the West Virginia Division of Environmental Protection to challenge his issuance of permits for mountaintop-removal coal mining in the state. The United States District court for the Southern District of West Virginia at Charleston denied motions to dismiss and found that West Virginia's approval of mountaintop mining practices violated both state and federal law. The district court enjoined the state from issuing further permits that authorized dumping of mountain rock within 100 feet of intermittent and perennial streams. The United States Court of Appeals for the Fourth Circuit vacated the district court's injunction, holding that the doctrine of sovereign immunity barred the citizen claims against a West Virginia official in federal court. The appellate court did, however, affirm the district court's entry of a consent decree of settlement.
The West Virginia Coal Mining Act, which operates in lieu of the federal Surface Mining Control and Reclamation Act of 1977 (SMCRA), vests the Director with authority to administer the Act and provides minimum performance standards. Nevertheless, the Eleventh Amendment bars citizen suits against state officials when the state itself is the real party in interest. Plaintiffs admitted that the State of West Virginia was the real party in interest, but asserted as a defense the *Ex Parte Young* exception to sovereign immunity. The *Ex Parte Young* exception allows suits against a state officer for violation of federal law. The appellate court held that the *Ex Parte Young* exception to Eleventh Amendment sovereign immunity did not apply in this case. In this instance, since the State of West Virginia had exclusive authority under the West Virginia Coal Mining Act, as a result of approval of its program under SMCRA, the citizen suit was in reality a suit under that Act and not under SMCRA. The appellate court further held the State of West Virginia did not waive its sovereign immunity in federal court by submitting its coal-mining program to the federal government for approval under SMCRA.

**WATER**

- *Jones v. City of Lakeland, Tennessee, 224 F.3d 518 (6th Cir. Aug. 9, 2000)*

  Plaintiffs were riparian landowners who filed suit against the city for its ongoing practice of discharging contaminated sewage, sludge, and other toxic, noxious, and hazardous substances into a creek in violation of the Water Pollution Control Act and the Tennessee Water Control Act. The United States District Court for the Western District of Tennessee at Memphis dismissed the action for failure to state a claim. The Court of Appeals for the Sixth Circuit held Plaintiffs' action was not precluded and remanded the case to the trial court for further proceedings.

  The Clean Water Act contains a limiting provision, which prohibits a civil enforcement action where the EPA or a state has already commenced and is diligently prosecuting a compliance action in state or federal court. Plaintiffs argued that the city's demonstrated lax enforcement of various compliance orders did not constitute diligent prosecution as mandated by the Clean Water Act. The appellate court ruled on other grounds and held that since neither the state's Water Quality Control Board nor the Tennessee Department of Environment and Conservation rose to the level of a federal or state court, the plaintiff's citizen suit was not precluded.
Pending Kentucky Cases

*Patton v. Sherman et al., Franklin County Circuit Court*

In 2001, Governor Paul Patton filed suit against the legislature and the Legislative Research Commission (LRC). At issue was the regulation governing Confined Animal Feeding Operations (CAFOs) promulgated by the Natural Resources and Environmental Protection Cabinet (NREPC).

On March 27, 2002 House Bill 728 became law without Governor Patton's signature. This action created a new section of KRS Chapter 13A to provide that administrative regulations that have expired or are scheduled to expire shall be null, void, and unenforceable. The also prohibits administrative bodies from promulgating regulations that are identical or substantially similar to the void regulations until adjournment of the 2003 Regular Session.

NREPC will continue to permit CAFOs under the existing regulation 401 KAR 5:060 Section 10. However, setbacks and other provisions will not apply.
## ENVIRONMENTALLY-RELATED LEGISLATION
### 2002 KENTUCKY GENERAL ASSEMBLY

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SECTION B
ENVIRONMENTALLY-RELATED LAWS PASSED
DURING THE 2002 GENERAL ASSEMBLY

SB 13

This bill bans the use of methyl tertiary butyl ether (MTBE) in gasoline produced after January 6, 2006. SB 13 also strongly encourages, but does not mandate, the use of bio-diesel and ethanol.

SB 193

This measure streamlines procedures for the Petroleum Storage Tank Environmental Assurance Fund. The University of Kentucky is to update the study completed in 1995 concerning appropriate cleanup standards for petroleum contamination. The bill also contains unrelated provisions concerning economic development, taxes, and private airstrips.

SB 257

This bill regulates the siting of merchant power plants in Kentucky. The bill creates a new state board for facilities not regulated by the Public Service Commission and establishes siting standards, as well as new requirements for cumulative environmental impacts.

SCR 17

This bill creates the Kentucky Watershed Task Force and directs that they study the need for managing the state’s water on a watershed basis and consider the necessity of working with border states on the management of shared watersheds.

HB 174

This bill presents a comprehensive plan for cleaning up abandoned landfills and dealing with roadside litter. The bill is funded through the assessment of a $1.75 per ton fee to be imposed on all waste disposed of at a municipal solid waste landfill and waste going through a transfer station. The bill authorizes the use of bonds for cleanup activities and appropriates $5 million from the state road fund to assist in cleaning up roadside litter.

HB 243

This measure provides that unmined coal, oil and gas reserves, and other mineral or energy resources are to be assessed as a distinct interest in real property unless they are owned in their entirety by the surface owner and the surface owner is not engaged in the severance of the reserves. The bill also requires the owner to use the land primarily for agricultural purposes.
HB 244

This bill renews the two-year sunset provisions on the hazardous waste assessment fund. The tax will now sunset in July 2004 and, in the meantime, an audit is to be conducted to study the sources and uses of the fund.

HB 270

This measure deals with the siting of cell towers. It provides a comprehensive system taking into account the different jurisdictions of the Public Service Commission and local planning and zoning, or the lack thereof.

HB 367

This measure grants confidentiality to certain documents submitted pursuant to the Agriculture Water Quality Act.

HB 405

This measure removes the requirement of a mining permit if coal extraction activities related to construction is under 5,000 tons and the coal or profits of a sale are donated to charity or the government.

HB 422

This measure extends the waste tire fee until July 31, 2006 and provides for a waste tire amnesty program.

HB 556

This bill establishes the Pine Mountain Trail State Park, a linear state park tracking over 100 miles on the ridge of Pine Mountain.

HB 618

This bill requires Jefferson County to eliminate the vehicle emission testing (VET) program by November 1, 2003 if it is in attainment of the air quality standards. The bill requires the county to re-assess the need for a VET program if the county returns to non-attainment.

HB 705

This bill authorizes the Division of Oil and Gas to allow a drilling permit to be extended by one year upon the payment of a fee and updating of the original application information.
HB 728

This measure provides that administrative regulations which have expired shall be null, void, and unenforceable. This bill was filed in reaction to a court decision limiting the General Assembly’s authority on regulation oversight.

HB 745

This bill deletes existing provisions related to owners that elect not to participate in the risk and cost of the drilling, deepening, or reopening of an oil or gas well. It sets forth procedures for the pooling of interests.

HB 809

This bill provides a mechanism for a surface mining permittee to enter property in order to abate a violation where the permittee does not otherwise have a legal right of entry.

HCR 13

This measure directs the Legislative Research Commission to study the effects of tax policies on forest management practices and present those results to the 2003 General Assembly. The measure also requires a study of the Kentucky Enterprise Zone Program.

HCR 244

This measure requires a study of the competitiveness of Kentucky coal in the generation of electricity. This measure also requires action against the federal government for failure to convert and dispose of depleted uranium hexafluoride waste in Paducah, Kentucky.
ENVIRONMENTALLY-RELATED PROPOSED LEGISLATION THAT DID NOT PASS DURING THE 2002 GENERAL ASSEMBLY

ADMINISTRATIVE REGULATIONS

SB 1

Requires legislative oversight of executive orders and administrative regulations.

SB 33

Requires an administrative body that is filing an emergency administrative regulation replacing an ordinary administrative regulation to file both regulations at the same time.

SB 200

Provides that administrative regulations which have expired or are scheduled to expire shall be unenforceable and also prohibits any similar regulations to be filed. Companion bill to HB 728.

HB 771

Requires an administrative body that is filing an emergency administrative regulation that will be replaced by an ordinary administrative regulation to file the ordinary administrative regulation and the emergency administrative regulation at the same time. Requires an administrative body to provide a form to be completed and filed by a person who wishes to be notified that the administrative body has filed an administrative regulation.

ENVIRONMENTAL MANDATES

HB 40

Requires all diesel fuel sold in the Commonwealth to contain 2% biodiesel until July, 2007, when the requirement increases to 5%.

HB 708

Ban MTBE and require reformulated gas to replace MTBE with ethanol by January 1, 2005.
HJR 24

Create the Subcommittee on Ethanol Production in Kentucky of the Interim Joint Committee on Agriculture and Natural Resources.

HCR 113

Direct the Interim Joint Committee on Agriculture and Natural Resources to study the benefits and risks associated with legislation encouraging the use of biodiesel fuel.

FEES/FUNDS/TAXES

HB 173

Would establish the "Local Government Landfill Assistance Program" to assist local governments in remediating out-of-service landfills that pose a threat to public health and the environment.

HB 798

Allows payments by a coal mine operator into a fund in lieu of physical mitigation when a stream is impacted by a coal mine.

HB 864

Imposes a tax, that shall be administered by the Revenue Cabinet, of 0.2 cents per kilowatt hour of electricity generated by peaking power plants located in Kentucky.

GENERAL ISSUES

HB 496

Requires the Natural Resources and Environmental Protection Cabinet to provide preliminary notice of an alleged violation. Exempts environmental emergencies from the preliminary notice requirement.

HJR 139

Direct the Natural Resources and Environmental Protection Cabinet to suspend until November 30, 2002, issuing new or modified permits for applicants in western Jefferson County. Requires the cabinet to report to the LRC by November 30, 2002, on efforts undertaken by the
cabinet to assess the risks to the citizens of western Jefferson County from the concentration of industrial plants within that part of the county.

**NITROGEN OXIDE ALLOCATION**

**HB 275**

Requires the Division of Air Quality to promulgate regulations to implement a nitrogen oxide budget trading program. Requires the Natural Resources and Environmental Protection Cabinet to establish an EGU source pool and an efficient energy reserve source pool for electric generating units.

**HB 408**

Original Intentions -- Requires the Division of Air Quality to first allocate NOx credits from the compliance supplement pool to those industrial sources that have made early reductions and then sell any remaining credits to industrial sources that are unable to meet their compliance deadlines. Permits the Division of Air Quality to contract with a private entity for the sale of allowance credits.

House Committee Substitute -- Deletes original provisions of the bill. Requires the Public Service Commission to require all electric utilities to inform all Kentucky coal operators of a utility's request for bids on a purchase coal contract, and require the bidder to disclose the amount of coal severance and unmined minerals tax to be remitted to the Commonwealth on the coal specified in the bid. When conducting a review of a utility's coal purchase contract for the purpose of disallowing any portion of the contract price in the utility's rates, require the utility to submit the bids by suppliers that remit tax to the Commonwealth. If the utility accepts a bid from a supplier that does not remit a tax, require the commission to determine the amount of coal severance and unmined minerals tax lost and apply the tax lost as an offset to be added to the contract price for the coal. Requires the commission to compare the lowest bid by a supplier that remits tax to the Commonwealth to the contract price for the coal after adding the prescribed offset.

**OIL AND GAS**

**SB 194**

Authorizes the Department of Mines and Minerals and the Division of Oil and Gas to allow a drilling permit to be extended by one year upon the payment of a fee and updating the original permit application information. Companion bill to HB 705.
SITING

HB 540

Establishes the Kentucky State Board on Electricity Generation and Transmission Siting and the Environment that is attached to the Public Service Commission. Establishes procedures and filing requirements for merchant plant siting.

SMART GROWTH

SB 72

Authorizes local governments to establish restoration zones and to administer a tax credit program for residential rehabilitation projects in restoration zones.

HB 465

Provides that a local planning commission must submit its plans to the regional planning commission and then to the state planning committee for approval and changes, and provide procedures for doing so, before it may adopt the elements, allow citizen to commence civil action against a state, regional, or local comprehensive plan.

HB 600

Requires all state agencies to promote, assist, and pursue the rehabilitation and revitalization of infrastructure, structures, sites and previously developed areas that are still suitable for reuse.

HB 797

Provides an income tax credit for taxpayers who convey land to an eligible conservation agency for conservation or preservation purposes.

SOLID WASTE

SB 34

Creates KY-CLEAN and the KY-CLEAN fund. Provides a check-off on the Kentucky Income Tax Return to designate a portion of the return to be contributed to the fund.
HB 28

Requires each waste management district to propose a universal collection system. Provides a method of collection for entities currently inaccessible to collection services.

HB 323

Provides that a statewide program of deposit for the purchase of beverage containers to be redeemed for deposit be voted on by the Commonwealth at the time of election for Governor and Lieutenant Governor.

HB 694

Provides enforcement power relating to litter laws for the solid waste coordinator in counties that have solid waste coordinators.

VET

SB 102

Requires certain air pollution control district boards to develop plans to meet the requirements of the National Ambient Air Quality Standards without the use of the VET program.

SB 169

Requires that government registered vehicles be VET tested biennially rather than yearly.

HB 46

Exempts vehicles four years and newer from mandatory vehicle emission tests.

HB 317

Exempts farm trucks from mandatory vehicle emissions tests.
ENVIRONMENTAL LIABILITIES AND FINANCIAL DISCLOSURE REQUIREMENTS – INTERSECTION OR COLLISION?

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ENVIRONMENTAL LIABILITIES AND FINANCIAL DISCLOSURE REQUIREMENTS – INTERSECTION OR COLLISION?

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SECTION C
I. The Development of Modern Environmental Protection Programs

A. Since the flowering of environmental activism during the 1960's and the first Earth Day in 1970, programs designed to protect the environment have proliferated. Environmental issues have increasingly come to share center stage with other critical concerns confronting our society. Changing awareness and perceptions regarding the interrelationship between varying types of activities and their impact on the ecosystem which we inhabit have fostered broad political support for environmental regulations.

B. Environmental programs and requirements now exist at federal, state and local levels which broadly affect individuals, businesses and government. These programs and requirements influence a wide array of disparate activities ranging from the selection of raw materials and the management of wastes to the provision of safe drinking water, the production of food supplies and the recycling of household trash.

C. As the reach of environmental regulation has expanded and the sensitivity to environmental concerns has increased, the potential costs of compliance have multiplied. Employing sophisticated pollution control equipment, maintaining detailed operational records, implementing enhanced monitoring procedures, satisfying complex permitting requirements, developing emergency response plans and compiling detailed information regarding chemical usage and handling are common examples of the types of demands confronting the regulated community. The costs of compliance, at least in the first instance, have fallen most heavily on business and industry.

1. The costs of complying with environmental requirements relating to discharges to surface waters and the air as well as the disposal of hazardous and other types of wastes has influenced balance sheets, profitability, and the ability of certain companies to remain in business.

2. Environmental requirements in certain instances have fundamentally altered the way that in which businesses operate and the types of activities in which businesses engage. Rather than complying with environmental requirements that would otherwise be applicable to their operations, businesses have chosen to recast their operations to avoid compliance costs or have simply exited altogether certain sectors of the market which are perceived to carry unacceptable costs or risks. Many types of waste minimization and pollution prevention programs have been based on such fundamental changes. These changes have had a positive impact on environmental quality in many instances but have also resulted in major shifts in the marketplace. For example, if a business decides to use water-based solvents instead of chlorinated solvents due to hazardous waste management requirements, it may be good for the environment but bad for the business's bottom line.

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environment but have an adverse impact on the company that was supplying the chlorinated solvents.

3. Compliance with environmental requirements (both governmentally imposed and voluntary) may be spurred through market forces. For example, intermediate consumers of goods and services may require their suppliers to meet certain types of standards such as ISO 14001. Environmental compliance in such contexts may be one of the predicates to survival in the marketplace. In fact, a study commissioned by the United States Environmental Protection Agency ("EPA") found that there is a "moderate positive correlation" between environmental performance and financial performance. Nevertheless, the report indicates that the cause of this correlation is unclear. See Office of Cooperative Environmental Management, "Green Dividends? The Relationship between Firms’ Environmental Performance and Financial Performance" (May 2000) (hereinafter, the "Green Dividends Report").

4. "Green" marketing is becoming increasingly common. Businesses may use a positive environmental record to achieve a competitive advantage. For example, with increasing deregulation of the distribution of electricity, companies that use "green" technologies to generate electricity have sought to capitalize on that fact even if such electricity may cost more than electricity generated by other means.

5. Environmental compliance has become a factor in attracting and retaining capital.

D. Separate and apart from the broad sweep of environmental regulatory programs designed to prospectively minimize the environmental impact of ongoing activities, a number of programs are also now in place to address environmental threats posed by past activities associated with more than a century of industrial activity. Undoubtedly the most familiar of these programs is the federal Superfund program developed under the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended ("CERCLA"), 42 U.S.C. §§ 9601 - 9675. The Superfund program is designed to facilitate the cleanup of sites posing a threat to human health or the environment as a result of the release or potential release of hazardous substances. Waste disposal sites, landfills, recycling facilities, abandoned dumps, factories, lagoons, drum storage areas, and a host of other types of facilities qualify as potential Superfund sites.

1. While the Superfund program may be the best known and most notorious of the environmental cleanup programs, it is by far not the only such program. For example, many states have similar programs to supplement cleanup efforts resulting under CERCLA. Facilities that store, treat or dispose of hazardous wastes or have done so in the past may be independently subject to cleanup requirements emanating under the Resource Conservation and Recovery Act, as amended ("RCRA"), 42 U.S.C. §§ 6901 – 6992k. Contamination resulting from leaking underground storage tanks must be addressed under the federal underground storage tank program and a host of analogous state programs.
2. The costs associated with cleanup activities can be staggering, often reaching tens and hundreds of millions of dollars at specific locations. For example, on February 1, 2002, EPA issued a Record of Decision setting forth its selected remedy for addressing PCB contamination in the sediments in the upper Hudson River in New York. The selected remedy will require that sediments be removed by dredging the Hudson River at an estimated cost of $460 million. General Electric Company is the only responsible party that EPA has identified in connection with the PCB contamination.

3. One estimate from the early 1990’s of the costs associated with cleaning up the nation’s known waste disposal sites over a thirty year period exceeded $750 billion. These costs are being spread to individuals, businesses and governmental entities which in some instances may only have a remote connection with the activities that created the wastes.

4. Along with remediation activities mandated by governmental directives, certain contaminated properties are being voluntarily remediated. During the last five years, a substantial number of states have developed programs to facilitate the remediation and reuse of “brownfields” sites – properties that have become contaminated through historical activities and which are often abandoned or underutilized.

E. As environmental cleanup and compliance costs have grown, they have had a profound influence on balance sheets, profits, cash flow, and even the very ability of certain businesses to compete. The financial implications of environmental cleanup and compliance costs thus have become an increasing concern to investors, lenders, and other individuals and entities with a stake in the financial health of a particular enterprise. In addition, environmental considerations have become a significant aspect of many real estate and business transactions.

II. Disclosure of Environmental Liabilities in the Financial Marketplace

A. With the growing financial impact of environmental cleanup and regulatory programs, the Securities and Exchange Commission (“SEC”) has increasingly scrutinized the way and the degree to which information regarding environmental liabilities and costs is being disclosed to potential investors by companies subject to the SEC’s jurisdiction. Certified Public Accountants (“CPAs”), investment bankers, borrowers, attorneys, and corporate officers and managers are wrestling with the thorny issues of how and when environmental liabilities and costs should be reported.

B. Deep concerns have been raised over the apparent lack of disclosure by certain companies, publicly held and otherwise. A provocative article appearing in the Wall Street Journal in 1988 entitled “Can $100 Billion Have ‘No Material Effect’ on Balance Sheets? Huge Toxic-Waste Cleanup Will Burden Many Firms, SEC Questions Disclosure” highlighted the gulf between the projected costs for environmental compliance and cleanup, and those that historically had been disclosed in financial materials made available to potential investors.
C. A report issued on October 13, 2000, by the World Resources Institute ("WRI") entitled “Coming Clean: Corporate Disclosure of Financially Significant Environmental Risks” reveals that few companies are adequately disclosing material risks that may arise from environmental exposures and that this failure to disclose does not arise from ignorance of such risks. The report studied thirteen (13) U.S. pulp and paper companies’ 10K, 10Q and 8K filings from 1998 and 1999. The report also indicates that SEC enforcement efforts in the area of environmental disclosure have been “minimal” and recommends the issuance of guidance to clarify existing regulations regarding environmental disclosure obligations and the heightened enforcement of these existing regulations.

D. Among the difficulties in dealing with the disclosure of environmental liabilities are the following:

1. The scope of environmental regulatory programs and environmental liability has shifted dramatically over time and has generally expanded. Businesses may face large expenditures simply to remain in compliance with changing environmental regulatory requirements. The complex and stringent requirements imposed by the 1990 amendments to the federal Clean Air Act, many of which even now are being implemented for the first time, are illustrative of this dynamic.

2. Deciphering what is necessary to achieve compliance may be difficult in certain circumstances. Many environmental regulatory requirements are quite complex and difficult to interpret, particularly in the context of the tremendous diversity of activities that they are designed to cover. The manner in which these issues are resolved can often have significant financial impacts on the members of the regulated community which are subject to such requirements.

3. Information concerning past waste disposal practices may be incomplete or lacking entirely. Accordingly, companies may face significant liabilities and yet be entirely unaware of the lurking danger to their financial well-being until receiving a notice from EPA or a state environmental regulatory agency.

4. Identifying with precision the magnitude of environmental contamination and associated cleanup costs is often difficult. Contamination is frequently located in subsurface areas where it can only be characterized through extensive testing. Many types of contamination are not detectable except through sophisticated analytical methods. The way in which contamination migrates from source areas can be influenced by a wide variety of factors, some of which may not be recognized or well understood.

5. The cleanup standards applicable to a particular site may be poorly defined or subject to differing interpretation by regulatory agencies and those conducting the remediation. Because cleanup standards typically establish the stopping points for remediation activities, where such standards are not well defined or understood, the ability to predict with precision the costs associated with cleanup is impaired.
6. Insurance coverage for environmental contamination caused by past activities is fraught with uncertainties. Insurance policies contain varying provisions which can influence the availability of coverage. Moreover, courts in different jurisdictions have reached contradictory results in interpreting identical provisions thereby making the availability of coverage somewhat dependent on jurisdiction.

7. Environmental compliance and cleanup costs may have varying effects on profits, cash flow and net worth. For example, mandatory environmental expenditures may severely impact the cash flow of a company over a short period of time without necessarily having the same degree of impact on the overall net worth of the company. Determining how to describe these disparate impacts thus may be difficult and hinder disclosure.

8. Where a business has failed to comply with environmental requirements, civil penalties and/or criminal sanctions generally may be imposed. Penalties can often be extremely large, with many of the environmental statutes authorizing civil penalties of up to $25,000 per day per violation. Such liability may accrue in addition to cleanup and compliance costs.

9. Environmental liabilities are often extremely hard to extinguish. For example, under the Superfund liability scheme, a person who owned a site at the time wastes were disposed thereon can be held liable for cleanup costs even if he or she no longer owns the site or was even aware of the disposal activities at the time of ownership. Superfund liability has also been found to pass through to successor companies and corporations. Accordingly, a company may have acquired or retained an environmental liability in circumstances where other types of liability may have been extinguished.

10. Activities impinging on the environment may give rise to third party claims for property damage and/or personal injuries.

11. Those responsible for preparing disclosure statements may have little familiarity with the intricacies of the environmental field. The technical and legal complexity of many environmental issues may tend to impede disclosure of environmental matters in comparison with issues that are more commonly confronted in the financial arena.

12. There is a profound lack of standards that makes it difficult for investors and corporate officers alike to effectively compare environmental performance between companies. As reported by EPA’s Office of Cooperative Environmental Management in its Green Dividends Report, “environmental and financial analysts do not have common analytic frameworks or terminology and separate regulatory regimes have tended to discourage their development.”

E. The foregoing considerations do not excuse the failure to disclosure environmental liabilities in circumstances where disclosure is warranted and
required. However, they may make disclosure more difficult in many instances and they may increase the risk that whatever is disclosed will later turn out to be inaccurate. At a minimum, matters of environmental disclosure are likely to require the use of a team approach involving accountants, securities attorneys, environmental consultants, and environmental attorneys to ensure that appropriate information is provided.

F. At the heart of the matter is the perception that the numbers simply do not add up. If the estimated costs of environmental cleanup and compliance are as significant as many believe, then presumably many of those costs should be reflected in the disclosure statements of publicly-held companies. However, this has not always been the case. For example, in a 1993 report to the House Energy and Commerce Committee, the General Accounting Office found that leading insurance companies rarely disclosed the amount of their exposure for environmental liabilities despite their claims that such liabilities could bankrupt the industry. The report recommended that the SEC take steps to require insurance companies routinely to disclose both the number and type of environmental claims and the estimated costs associated with those claims.

G. In addition to issues relating specifically to disclosure of environmental costs and liabilities to investors or others with a financial interest in the business in question, certain environmental statutes and regulations require that information relating to releases of potential contaminants be provided to environmental regulatory agencies. Indeed, EPA has pressed for greater disclosure of information relating to the use and management of a broad spectrum of substances. The nexus between this body of information and what is disclosed to investors may take on increasing importance.

H. Whatever the reasons for the apparent lack of disclosure, the SEC, the investment community, and even the courts are sending strong signals that it is not a situation which should be allowed to continue. Moreover, disappointed investors and/or the SEC may seek to hold accountants, lawyers, and other professionals responsible for inadequate disclosure of environmental liabilities, thereby placing additional burdens on the accounting and securities professions to perform due diligence concerning the scope and magnitude of environmental liabilities. This potentially could place professionals with expertise in the securities and financial fields in the center of a vortex of liability involving highly technical issues concerning environmental compliance, contamination and cleanup requirements. With the financial collapse of Enron Corporation, auditing and disclosure standards are under increasing scrutiny. This dynamic may well manifest itself in the context of environmental disclosure.

III. Summary of Key Requirements Imposed by the SEC Relevant to the Disclosure of Environmental Liabilities and Compliance Costs

disclosure of information by regulated companies relevant to investors and potential investors.

B. The SEC has developed a complex body of regulations setting forth requirements relating to the disclosure of information by companies subject to the SEC's regulatory authority. These regulations help implement requirements of the Securities Act and the Exchange Act.

C. The regulations promulgated by the SEC cover the content of both financial statements and narrative disclosures.

D. Regulation S-X, 17 C.F.R. Part 210, governs the SEC accounting rules and requirements pertinent to the form and content of financial statements. Under Regulation S-X, financial statements are normally to be prepared in accordance with generally accepted accounting principles ("GAAP"). Specifically, 17 C.F.R. § 210.4-01(a)(1) provides that "[f]inancial statements filed with the Commission which are not prepared in accordance with generally accepted accounting principles will be presumed to be misleading or inaccurate, despite footnote or other disclosures, unless the Commission has otherwise provided." As a result, the regulations promulgated by the SEC regarding financial statements not only set forth specific requirements that must be followed but essentially incorporate by reference GAAP. This is consistent with the SEC's long-standing policy to look to the private sector for the promulgation of GAAP. The SEC initially issued this administrative policy in 1938 and updated it in 1973 to recognize the establishment of the Financial Accounting Standards Board ("FASB"). See 64 Fed. Reg. 1728 (Jan. 12, 1999).

E. Regulation S-K, 17 C.F.R. Part 229, contains requirements applicable to the non-financial statement portions of the following categories of documents:

1. Registration statements under the Securities Act (to the extent provided in the forms to be used for such registration statements). See 17 C.F.R. § 229.10(a)(1).

2. Documents and reports required pursuant to the Exchange Act (to the extent provided in the forms and rules thereunder) including:

a. Registration statements pursuant to Section 12 of the Exchange Act.

b. Annual or other reports pursuant to Sections 13 and 15(d) of the Exchange Act (including Form 10-Q (quarterly), Form 10-K (annual) and Form 8-K (episodic)).

c. Going private transaction statements under Section 13 of the Exchange Act.

d. Tender offer statements under Sections 13 and 14 of the Exchange Act.
Annual reports to security holders and proxy and information statements pursuant to Section 14 of the Exchange Act.

Any other document required pursuant to the Exchange Act to the extent provided in the forms and rules thereunder.

See 17 C.F.R. § 229.10(a)(2).

F. Three areas under Regulation S-K are most likely to involve the potential for narrative disclosure of information related to environmental compliance and environmental liabilities -- Item 101 (Description of Business), 17 C.F.R. § 229.101; Item 103 (Legal Proceedings), 17 C.F.R. § 229.103; and Item 303 (Management's Discussion and Analysis of Financial Condition and Results of Operations), 17 C.F.R. § 229.303.

1. Item 101 includes a requirement that as part of a narrative description of the business, the registrant discuss the material impacts of environmental compliance, as follows:

   Appropriate disclosure also shall be made as to the material effects that compliance with Federal, State and local provisions which have been enacted or adopted regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, may have upon the capital expenditures, earnings and competitive position of the registrant and its subsidiaries. The registrant shall disclose any material estimated capital expenditures for environmental control facilities for the remainder of its current fiscal year and its succeeding fiscal year and for such further periods as the registrant may deem materials [sic].

   17 C.F.R. § 229.101(c)(1)(xii). Where material, the business segments to which environmental compliance matters are significant must also be identified. 17 C.F.R. § 229.101(c).

2. Item 103 requires registrants to "[d]escribe briefly any material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the registrant or any of its subsidiaries is a party or of which any of their property is the subject." 17 C.F.R. § 229.103. Instruction 5 to Item 103 amplifies on these requirements as they apply to environmental proceedings, as follows:

   [A]n administrative or judicial proceeding (including, for purposes of A and B of this Instruction, proceedings which present in large degree the same issues) arising under any Federal, State or local provisions that have been enacted or adopted regulating the discharge of materials into the environment or primary [sic] for the purpose of protecting the environment shall not be
deemed "ordinary routine litigation incidental to the business" and shall be described if:

A. Such proceeding is material to the business or financial condition of the registrant;

B. Such proceeding involves primarily a claim for damages or involves potential monetary sanctions, capital expenditures, deferred charges or charges to income and the amount involved, exclusive of interest and costs, exceeds 10 percent of the current assets of the registrant and its subsidiaries on a consolidated basis; or

C. A governmental authority is a party to such proceeding and such proceeding involves potential monetary sanctions, unless the registrant reasonably believes that such proceeding will result in no monetary sanctions, or in monetary sanctions, exclusive of interest and costs, of less than $100,000; provided, however, that such proceedings which are similar in nature may be grouped and described generically.

Instructions to Item 103, Section 5.

3. Item 303 requires discussion of prospective information as that information relates to issues such as liquidity, capital resources, and results of operations. 17 C.F.R. § 229.303(a). Item 303 also requires discussion of such other information that the registrant believes is necessary to an understanding of its financial condition, changes in financial condition and results of operations. Instruction 2 to Item 303 clarifies that the "purpose of the discussion and analysis shall be to provide to investors and other users information relevant to an assessment of the financial condition and results of operations of the registrant as determined by evaluating the amounts and certainty of cash flows from operations and from outside sources. The information provided pursuant to this Item need only include that which is available to the registrant without undue effort or expense and which does not clearly appear in the registrant's financial statements."

G. While disclosure obligations are generally governed by Regulation S-K, Rule 10b-5 may also mandate disclosure of environmentally-related information in certain instances. Rule 10b-5 provides as follows:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5.

IV. The SEC's Historical Approach to Environmental Disclosure

A. The SEC has had a long history of involvement with disclosure of environmental liabilities and compliance costs dating back to 1971. Under the spur of the National Environmental Policy Act of 1969 ("NEPA"), the SEC reviewed its existing disclosure requirements and issued an interpretive release entitled "Disclosures Pertaining to Matters Involving the Environment and Civil Rights." Release No. 33-5170 (July 19, 1971), 36 Fed. Reg. 13989 (July 29, 1971). In that release, the SEC expressed its view that, under general materiality principles, two existing disclosure items -- the description of the company's business and the description of the company's legal proceedings -- called for the disclosure of (1) circumstances, if material, in which compliance with environmental laws "may necessitate significant capital outlays, may materially affect the earning power of the business, or cause material changes in ... [the current or future] business;" and (2) proceedings, if material, arising under environmental statutes and regulations.

B. In 1973, in response to pressure exerted by the Natural Resources Defense Council, Inc. ("NRDC") and others, the SEC amended its existing disclosure requirements to conform, in its view, with the requirements of NEPA. These amendments directed that the material effects on future capital expenditures, earnings and the competitive position of the company resulting from compliance with environmental laws and regulations be disclosed. In addition, the amendments described the extent to which litigation disclosures were required to contain specific descriptions of environmental proceedings. Moreover, the amendments foreclosed the possibility of disregarding environmental suits in excess of the requisite 10 percent of current assets threshold as ordinary routine litigation incidental to the business. See Release No. 33-5386 (April 20, 1973).

C. In early 1975, in the aftermath of NRDC v. SEC, 389 F.Supp. 889 (D.D.C. 1974), the SEC revisited the topic of environmental disclosure in Release No. 33-5569 (February 11, 1975) and gave notice of public proceedings to determine
whether its present disclosure rules were adequate in view of NEPA. The SEC thereafter proposed substantial amendments to existing disclosures rules requiring additional disclosure relating to (1) present and certain future estimated capital expenditures for environmental control facilities and (2) environmental compliance reports showing the failure to meet an applicable federal standard in the preceding 12 months. The SEC also proposed to impose the obligation on companies to provide copies of such compliance reports to the public upon request. See Release No. 33-5627 (October 14, 1975).

D. In 1976, the SEC abandoned requiring the listing and provision of compliance reports, finding the burdens "grossly disproportionate" to the benefits. The SEC, however, adopted the proposed expanded disclosure requirements concerning capital expenditures for environmental controls. See Release No. 33-5704 (May 6, 1976). The SEC also expressed its view that existing disclosure requirements tended to adequately protect investors in connection with environmental concerns.

E. In 1979, the SEC issued another interpretive release concerning environmental disclosure requirements, both reviewing the scope of those requirements and reiterating its interpretation of the requirements. See Release No. 33-6130 (September 27, 1979), 44 Fed. Reg. 56924 (Oct. 3, 1979). Among the significant aspects of the Release were the following:

1. In the SEC's view, companies could be required to develop and disclose estimates of future costs of environmental controls if future costs were expected to be materially greater than current, reported costs. In addition, the SEC indicated that disclosure was required of such estimates if necessary to prevent reported costs from being misleading.

2. The SEC interpreted the term "proceedings" broadly so as to require disclosure of a proceeding involving the government as a party, even if the proceeding were initiated by a private party.

3. The SEC explained that "the obligation to disclose 'the relief sought' by the government" required that "an estimate of the level of expenditures required to install the pollution control equipment sought by the governmental authority be provided if such expenditures are likely to be material."

4. The SEC took the position that while there was no general requirement that a company disclose its policies regarding environmental protection, companies that chose to make such disclosures had to ensure that the disclosures were accurate and not misleading.

5. The SEC noted that compliance with its specific environmental disclosure rules did not necessarily ensure full compliance with the disclosure requirements under the federal securities laws where disclosure of additional material information was necessary to make the required statements not misleading.
In 1982, the SEC again revised the environmental proceedings requirement, adopting materiality thresholds in order to address criticisms that the existing requirement imposed excessive burdens on companies and resulted in preparation of cluttered disclosure of questionable utility to investors. See Release No. 33-6383 (March 3, 1982). In adopting the revised version of the requirement, the SEC discussed the new "reasonable belief" standard, which limited disclosure of environmental proceedings to which a governmental authority was a party, provided the registrant reasonably believed that a proceeding would not result in monetary sanctions of $100,000 or more.

V. The SEC's Response to the Growth in Superfund Liability

A. In 1980, Congress passed CERCLA to address the legacy of more than a century of industrial waste disposal practices. To deal with the problem of responding to abandoned waste sites, Congress crafted an extremely broad liability framework which imposes strict and joint and several liability on generators and transporters of hazardous substances as well as current and past owners and operators of sites from which releases or threatened releases of hazardous substances have occurred or are occurring. See 42 U.S.C. § 9607(a).

B. As the Superfund program slowly gained momentum during the early 1980's, many publicly traded companies started to feel the financial impacts associated with CERCLA's broad liability framework. By the second half of the 1980's, many businesses were facing potentially huge liabilities for investigating and remediating sites identified by EPA throughout the country. Because of the imposition of strict liability and the availability of only extremely limited defenses, the threshold for becoming ensnared in Superfund cases was extremely low. Moreover, parties found to be liable generally faced the prospect of joint and several liability with uncertain prospects of being able to recoup excess response costs from third parties through contribution actions.

C. The financial ramifications associated with the Superfund program caused the SEC to take notice. Superfund liability both in terms of its nature and magnitude presented different scenarios than the types of environmental regulatory programs that EPA and the states had developed during the 1970's. By the second half of the 1980's, the SEC was raising significant concerns regarding the degree to which publicly-traded companies were disclosing environmental liabilities.

D. On May 18, 1989, the SEC released a lengthy interpretive release regarding the disclosure required by Section 303 of Regulation S-K, captioned "Management's Discussion and Analysis of Financial Condition and Results of Operation" ("MD&A"). See Securities Act Release No. 33-6835; Exchange Act Release 34-26831 (May 18, 1989), 54 Fed. Reg. 22427 (May 24, 1989). The Release set forth the SEC's views regarding several disclosure matters that should be considered by registrants in preparing MD&As. It also included as an illustrative example of a situation requiring disclosure the designation of a registrant as a potentially responsible party ("PRP") by EPA under CERCLA.

1. In connection with its example, the SEC assumed the following facts:
a. The registrant had been correctly designated as a PRP by the EPA with respect to the cleanup of hazardous wastes at three sites.

b. No statutory defenses were available.

c. The registrant was in the process of conducting preliminary investigations of the three sites in question to determine the nature of its potential liability and the amount of cleanup costs necessary to remediate the sites.

d. Other PRPs had been designated but the ability to bring an action for contribution was unclear as was the extent of insurance coverage, if any.

e. Management of the registrant was "unable to determine that a material effect on future financial conditions or results of operations is not reasonably likely to occur."

2. In light of these facts, the SEC expressed the view that disclosure in MD&A was required as to the designation of the registrant as a PRP, the effects of which should be quantified to the extent reasonably practical.

3. The SEC also identified the following factors to be considered in connection with determining the extent of disclosure in MD&A in connection with the designation of the registrant as a PRP:

   a. The aggregate potential cleanup costs in light of the joint and several liability to which a PRP is subject.

   b. Whether there is any insurance coverage and, if so, whether it may contested.

   c. The existence and extent of any potential sources of contribution or indemnification (in determining whether there might be reliable sources of recovery).

4. In a footnote to the Release, the SEC indicated that mere designation as a PRP does not itself trigger a duty to disclose pursuant to Item 103 of Regulation S-K regarding "Legal Proceedings." Moreover, the SEC clarified that cleanup costs generally are not "sanctions" for purposes of Instruction 5(B) or (C) of Item 103.

5. More generally, under the Release, MD&A requires management to make a two-step assessment with respect to any known trend, commitment, event or uncertainty.

   a. If management determines that the known trend, demand, commitment, event or uncertainty is not reasonably likely to occur, no disclosure is required.
b. If management cannot make such a determination, however, management must objectively evaluate the consequences of the known trend, demand, commitment, event or uncertainty, on the assumption that it will come to fruition. Disclosure is then required unless management determines that a material effect on the registrant's financial condition or results of operations is not reasonably likely to occur.

6. From an enforcement perspective, the SEC indicated in the Release that where a material change in a registrant's financial condition (such as a material increase or decrease in cash flows) or results of operations appears during a reporting period and the likelihood of such a change was not discussed in prior reports, the SEC will inquire into the circumstances existing at the time of the earlier filings to determine whether the registrant failed to discuss a known trend, demand, commitment, event or uncertainty as required in MD&A.

E. In early 1990, EPA agreed to furnish SEC with environmental enforcement action information regarding registrants and SEC agreed to consider SEC enforcement in connection with those companies' environmental disclosure. Computerization has enhanced the impact of this information exchange.

F. On June 8, 1993, the SEC issued a staff accounting bulletin (Release No. SAB 92) regarding accounting and disclosure rules relating to loss contingencies involving, among other things, environmental liabilities. See 58 Fed. Reg. 32843 (June 14, 1993). The statements in staff accounting bulletins are not rules or formal interpretations of the SEC. However, they represent interpretations and practices followed by the SEC's Division of Corporation Finance and the Office of Chief Accountant in administering the disclosure requirements of the federal securities laws. According to the SEC, SAB 92 merely reflects the interpretation of existing disclosure obligations and does not represent a change in accounting requirements. SAB 92 includes a number of points relevant to accounting and disclosure in the context of environmental liabilities, including the following.

1. In circumstances where a contingent liability is probable of occurring (such as liability for environmental cleanup costs) but that liability may be offset, in part or in whole, by a claim for recovery that is probable of realization (such as recovery under applicable insurance policies), the SEC staff nevertheless concluded that ordinarily the contingent loss and the potential recovery should be reported separately on the balance sheet rather than reported together as a single net amount. The SEC staff pointed to the inherent uncertainties in shifting liabilities to third parties and the fact that the uncertainties associated with contingent liabilities tended to be distinct and independent from the uncertainties associated with claims for recovery as militating in favor of separately reporting gross liabilities and potential recoveries.

2. In circumstances where a registrant is jointly and severally liable for environmental cleanup costs but those costs may be apportioned among a number of potentially responsible parties, the SEC staff concluded that the registrant need not recognize liability for those costs to be assigned to
other potentially responsible parties unless it is probable that the other parties will not fully pay such costs. The SEC staff cautioned, however, that discussion of uncertainties with respect to the registrant's ultimate obligation to pay might be required and that any additional losses that are reasonably possible should be noted.

3. The SEC staff warned that notwithstanding the significant uncertainties typical with respect to measuring environmental liability, delaying recognition of a contingent liability until a single dollar amount can reasonably be estimated is not permissible. If the amount of the liability is likely to fall within a certain range and no single amount within the range represents a best estimate, the registrant should recognize a loss equal to the minimum amount of the range. Moreover, the SEC staff indicated that cost estimates for environmental liabilities should be refined as more information becomes available and that the revised estimates should reported during the accounting period in which they occur.

4. The SEC staff indicated that environmental liabilities typically are of such significance that detailed disclosures regarding the judgments and assumptions underlying the recognition and measurement of the liabilities are necessary to prevent financial statements from being misleading and to fully inform readers of such statements regarding the range of reasonable possible outcomes that could have a material effect on the registrant's financial condition, results of operations, or liquidity.

5. The SEC staff emphasized that disclosure and discussion of environmental liabilities was crucial in documents outside of financial statements (such as MD&A). The SEC staff stated that disclosures should be sufficiently specific to enable a reader to understand the scope of the contingencies affecting the registrant and noted that separate discussion of issues such as the registrant's ongoing environmental compliance costs, capital expenditures incurred to implement environmental controls, and non-recurring cleanup costs might be required.

6. The SEC staff indicated that material liabilities for environmental "exit" costs associated with activities such as site restoration and cleanup, closure and post-closure steps, and ongoing monitoring should be disclosed in the notes to financial statements. The SEC staff also indicated that it had no objection to accruing such costs over the useful life of the asset.

7. The SEC staff also addressed issues relating to discounting the costs associated with environmental liabilities to reflect the time value of money and issues relating to disclosure rules for public utilities.

G. As the foregoing indicates, the growth of the Superfund program helped spur the SEC to increase the consideration given to environmental liabilities and compliance costs.
1. EPA and the SEC are cooperating in terms of sharing information with the expected result that the SEC will cross-reference various filings and disclosure statements for a company with information obtained from EPA as to the company's potential environmental liabilities. EPA is also helping to train the SEC staff as to what to look for with respect to environmental disclosure.

2. During his tenure, former Securities and Exchange Commissioner Richard Roberts repeatedly emphasized that publicly-held companies must fully and fairly disclose their environmental liabilities. The SEC generally has intensified its scrutiny of environmental disclosure, particularly with respect to ensuring that environmental liabilities are adequately addressed in MD&A and that such liabilities are reported in accordance with SAB 92.

3. In a report in 1993 to the House Energy and Commerce Committee, the General Accounting Office found that leading insurance companies rarely disclosed the amount of their exposure for environmental liabilities despite their claims that such liabilities could bankrupt the industry. The report recommended that the SEC take steps to require insurance companies routinely to disclose both the number and type of environmental claims and the estimated costs associated with those claims.

4. The SEC has suggested that in addition to scrutinizing environmental liabilities associated with being classified as a PRP in connection with Superfund sites, it intends to examine the manner in which disclosure of cleanup costs associated with contaminated facilities and real estate which are not being addressed through the formal Superfund process is being handled.

H. With the growth in costs associated with environmental liabilities, the SEC has recognized that environmental issues can have a very real and significant impact on the financial viability of a company thereby giving increased attention to the effect of environmental issues on the investing public. For example, in remarks made in 1993, former Securities and Exchange Commissioner Roberts cited a University of Tennessee study estimating the cost of cleaning up the nation's hazardous waste sites at $752 billion over the next thirty years under then current environmental policies. The SEC's heightened sensitivity to environmental matters is in sharp contrast with the SEC's position in the early 1970's that environmental issues were primarily of social rather than financial importance and lacked direct and immediate economic significance. See generally Manko, Environmental Disclosure--SEC v. NEPA, 31 Business Lawyer 1907 (July 1976).

VI. Recent Developments Concerning the Disclosure of Environmental Liabilities

A. The SEC has had a long-standing policy to recognize and rely on GAAP for purposes of financial disclosure. This policy is embodied in Regulation S-X. Accordingly, not only are the actions of the SEC important to issues relating to
the disclosure of environmental liabilities but so are developments relating to GAAP.

B. The Financial Accounting Standards Board ("FASB") is responsible for issuing GAAP. Major pronouncements by FASB are known as Statements of Financial Accounting Standards ("SFAS").

C. Statement of Financial Accounting Standards No. 5 ("FASB Statement No. 5") governs accounting for contingencies. Under FASB Statement No. 5, a liability must be accrued if (1) information available prior to issuance of the financial statements indicates that it is probable that an asset has been impaired or a liability has been incurred at the date of the financial statements and (2) the amount of the loss can be reasonably estimated. Application of this standard in the context of environmental liabilities has proved to be challenging.

D. On October 10, 1996, the American Institute of Certified Public Accountants ("AICPA") issued Statement of Position 96-1 ("SOP 96-1"). SOP 96-1 is designed to provide guidance concerning the application of FASB Statement No. 5 with respect to environmental remediation liabilities that relate to pollution arising from past activities. It offers authoritative guidance on the recognition, measurement, display and disclosure of environmental remediation liabilities. By contrast, SOP 96-1 does not provide guidance on accounting for pollution control costs with respect to current operations or on accounting for costs of future site restoration or closure activities that are required upon the cessation of operations or sale of facilities. SOP 96-1 also does not cover accounting for environmental remediation activities that are undertaken at the sole discretion of management (i.e., voluntarily).

1. SOP 96-1 contains explicit guidance on the recognition of environmental remediation liabilities (i.e., when liabilities should be reported in financial statements). While recognizing that in the environmental context, remediation obligations become determinable and the amount of liability becomes estimable over a continuum of events and activities, SOP 96-1 makes clear that reporting generally cannot be deferred until all the facts have been gathered and an ultimate assessment of liability has been made. Instead, SOP 96-1 provides that an environmental remediation liability should be treated as probable of being incurred if the following two conditions are met:

a. Litigation has commenced or a claim or an assessment has been asserted, or, based on available information, commencement of litigation or assertion of a claim or an assessment is probable. (In other words, it has been asserted or it is probable that it will be asserted that the entity is responsible for participating in a remediation process because of a past event.)

b. Based on available information, it is probable that the outcome of such litigation, claim, or assessment will be unfavorable. (In other words, an entity will be held responsible for participating in a remediation process because of the past event.)
2. SOP 96-1 discusses in detail the various administrative stages of a typical Superfund matter and how reporting of liabilities should be handled at each stage.

3. SOP 96-1 also provides guidance on how to estimate the amount of an environmental remediation liability once it has been determined that such a liability must be recognized. Under SOP 96-1, the estimated costs should include the allocable share of the liability for a specific site and the share of amounts related to the site that will not be paid by the government or other PRPs.
   a. Specific costs that are to be included in the determination of the magnitude of a liability include the incremental direct costs of the remediation effort and the costs of compensation and benefits for those employees who are expected to devote a significant amount of time directly to the remediation effort to the extent of the time spent on such effort.
   b. Remediation efforts include precleanup activities (such as site characterization), remedial activities, government oversight and enforcement related activities, operation and maintenance (“O&M”) activities and post-remediation monitoring.
   c. Incremental direct costs of remediation include consulting and contractor fees, costs of dedicated machinery and equipment that does not have an alternative use, PRP group assessments, O&M costs, government oversight and response costs, and attorneys fees for work related to determining the extent of remedial actions that are required, the type of remedial actions to be used, or the allocation of costs among PRPs.
   d. Remediation liabilities should be based on the statutes, regulations and policies currently in place rather than those requirements as they might evolve at the time the remediation is actually performed. Moreover, remediation liabilities should be based on the remediation technology that is expected to be approved to complete the cleanup effort.
   e. Remediation liabilities should be based on the estimated cost to perform each of the remediation elements when those elements are expected to be undertaken. Discounting to take into account the time value of money is permissible under certain circumstances.

4. SOP 96-1 provides specific guidance on methods for determining an allocable share of overall liability assuming that multiple PRPs are being subject to joint and several liability.

5. SOP 96-1 provides that potential recoveries that might offset remediation liabilities are to be determined and recognized separately.
6. While SOP 96-1 provides very useful guidance, the assumptions about the manner in which site contamination cases unfold may be overly simplistic in certain circumstances. The central thrust of SOP 96-1 suggests, however, that accrual of liabilities associated with site contamination may need to be done earlier than had been typically occurring, even if such accrual is done in a piecemeal fashion.

E. FASB has developed rules to address obligations stemming from the closure of long-lived “hard” assets. See “Statement of Financial Accounting Standards No. 144: Accounting for the Impairment or Disposal of Long-Lived Assets (Aug. 2001). Such assets run the gamut from power plants, mines and waste management facilities to utility poles and metal finishing shops. In many instances, such assets may be subject to legally enforceable obligations such as closure or reclamation plans under environmental statutes and regulations. How to properly account for such obligations has sparked controversy.

F. In 1998, the SEC brought an administrative enforcement action against a pharmaceutical company and three individuals affiliated with the company (the current CEO and chairman of the board, the former chairman of the board, and the CFO) arising out of inadequate disclosure of environmental liabilities. See In re Lee Pharmaceuticals, Admin. Order No. 3-9573 (April 9, 1998). This action brought to fruition repeated warnings by the SEC that it intended to enforce requirements pertaining to environmental disclosure.

1. The SEC charged that Lee Pharmaceuticals learned in 1987 that its property was contaminated. The California Regional Water Quality Control Board thereafter ordered the company to perform an investigation and the investigation confirmed the presence of contamination. In 1991, EPA designated the company a PRP in connection with the San Gabriel (area 1) Superfund Site, a regional groundwater contamination site. The same year, the company obtained an estimate of $465,000 for its share of investigation and remediation costs associated with the site. In 1992, the company submitted an insurance claim estimating its costs at $700,000.

2. The SEC charged that despite the foregoing information, the company failed to disclose the nature of its environmental liabilities in reports filed with the SEC between 1991 and 1996. For example, in its 1991 Form 10-K, the company failed to disclose that it was not continuing to investigate groundwater conditions as it had been ordered and failed to disclose that it had been named a PRP by EPA. The SEC also charged that the company falsely reported that environmental tests were “inconclusive.” In subsequent Form 10-Ks, the SEC charged that the company included false and materially misleading statements including representing that it was not a PRP, that EPA had determined that no cleanup would be required of groundwater, that it had no information about cleanup costs for its property and that it had not caused the contamination (despite a study conducted by EPA that concluded to the contrary).
3. The SEC determined that the company had failed to properly accrue a liability on its financial statements for remediation costs in accordance with GAAP. The SEC also determined that the company had violated the antifraud provisions of the Exchange Act and Rule 10b-5 thereunder.

4. In settlement of the enforcement action, the respondents agreed to entry of a cease-and-desist order. The SEC also barred the CFO from practicing as an accountant before the SEC for a period of three years.

G. During the past several years, shareholders of various corporations have sought to include in proxy materials proposals regarding environmental matters over the objection of the corporation. The SEC has resolved these disputes. For example, in 1999, the SEC ruled that Eastman Kodak Company could not exclude from proxy materials a shareholder proposal requesting that the company disclose in its environmental progress report a list of hazardous waste sites and other circumstances in which it expected to accrue environmentally-based financial liabilities.

H. On August 12, 1999, the SEC issued a staff accounting bulletin (Release No. SAB 99) emphasizing that exclusive reliance on quantitative benchmarks to assess materiality in preparing financial statements and performing audits of those financial statements is inappropriate. See 64 Fed. Reg. 45150 (Aug. 19, 1999). In particular, SAB 99 focuses on the materiality of misstatements in a registrant's financial statements. While not aimed directly at the disclosure of environmental liabilities, the points emphasized in SAB 99 may have particular relevance in evaluating the reporting of environmental liabilities on financial statements.

1. In SAB 99, the SEC's Division of Corporation Finance and the Office of the Chief Accountant underscored the fact that materiality must be considered in the context of all of the facts. As stated in SAB 99, "[a] matter is 'material' if there is a substantial likelihood that a reasonable person would consider it important."

2. Under the foregoing formulation of materiality, the SEC staff noted that both "quantitative" and "qualitative" factors are to be used in determining what is material.

3. While acknowledging that quantitative "rules of thumb" may be useful as an initial step in assessing materiality, the SEC staff emphasized that such rules of thumb cannot be used as a substitute for a full analysis of all relevant considerations.

4. In determining whether multiple misstatements may cause the financial statements of a registrant to be materially misstated, the SEC staff directed that each misstatement should be considered separately and the aggregate effect of all misstatements should be independently considered.

5. SAB 99 includes a number of strongly-worded directives against intentional misstatements in financial statements, even where such
misstatements might not be considered to be material. Moreover, the
SEC staff noted that while the intent of management does not, itself,
render a misstatement material, it might provide significant evidence of
materiality in circumstances, for example, where management misstated
items in financial statements to “manage” reported earnings.

I. Investing based on non-financial considerations is on the rise. For example,
investors may select companies based not only on their financial performance but
also on their environmental performance. Recent studies are indicating that
“socially conscious” investing may reap significant financial rewards. It has
been suggested that as a strong proxy for management quality, relative
environmental performance is increasingly being used to project stock market
returns. See William Thomas, Taking Stock: New Methods Emerge to Assess
Financial Gains by Environmental Leaders, Trends, September/October 2000. If
environmental performance becomes a benchmark for predicting overall financial
performance, it could have dramatic implications for environmental disclosure
requirements. Certainly additional information regarding the environmental
management and performance of a company could take on added importance to
investors. This in turn may stimulate further evolution of the SEC’s disclosure
requirements with respect to environmental matters. Nevertheless, as the Office
of Cooperative Environmental Management’s Green Dividends Report indicates,
there are a number of “informational and institutional barriers to the
incorporation of environmental information in financial analysis.”

J. In February 2002, ASTM International issued a publication entitled “Standard
Guide for Disclosure of Environmental Liabilities” (Standard E 2173-01). This
guide, a supplement to GAAP, provides general parameters for determining
whether a disclosure of environmental liabilities is warranted and for determining
the content of that disclosure. It also identifies sources of information to be
reviewed in determining whether conditions warrant disclosure.

K. Future reform is likely in the wake of the collapse of Enron Corporation in late
2001 and the media attention that it attracted. In January of 2002, President Bush
indicated that the Treasury Department, the SEC, the Federal Reserve Board and
the Commodities Futures Trading Commission will all be reviewing disclosure
regulations with an eye toward ensuring the protection of the investor. Further,
the major accounting firms proposed the issuance of a MD&A guidance
document as a starting point for disclosure reform post-Enron. Although not
specifically addressing environmental risk disclosure, the guidance does call for
increased risk disclosure in other areas, such as off-balance-sheet arrangements
and certain trading activities. On February 13, 2002, the SEC announced that the

2 Another potential information barrier is SEC Regulation FD (fair disclosure). Promulgated in August,
2000, Regulation FD prevents issuers from intentionally disclosing material information to securities
analysts without simultaneously making a public disclosure of such information. Following the
promulgation of Regulation FD, there was a heated debate regarding its likely impact. Some analysts
claimed that the regulation would chill all disclosure, while others claimed it would encourage the
dissemination of relevant information to all investors and discourage selective disclosure. It appears that
both sides of the argument are correct, as early reports on the effect of Regulation FD reveal that some
companies have restricted their disclosures, while others have fulfilled the intention of Regulation FD and
undertaken to make more complete disclosures of material information.
corporate disclosure regulations will undergo major changes to require companies to explain, in the words of Chairman Harvey Pitt, "what the key factors are that drive the company's business, what the significant trends are that could impact the company's performance going forward, and other key factors that could affect the company's business, both on an historical and prospective basis." It is unclear when this reform effort will be completed.

VII. Litigation Highlights Pertaining to the Disclosure of Environmental Liabilities and Compliance Issues

A. Litigation concerning environmental disclosure (or lack thereof) has occurred on a repeated basis.

B. Cases which have involved issues relating to environmental disclosure include the following:

1. In Levine v. NL Industries, Inc., 926 F.2d 199 (2nd Cir. 1991), the Second Circuit affirmed dismissal of an action charging NL Industries with fraudulently failing to disclose that a wholly-owned subsidiary was operating a federal uranium processing facility in violation of federal and state environmental requirements. The court's decision turned on the fact that because the subsidiary was fully indemnified by the federal government for any environmental liabilities, the alleged environmental non-compliance was not material. The court noted, however, that as a general rule "disclosure of potential costs for violations of environmental law, if material, is ordinarily required." 926 F.2d at 203.

2. In United Paperworkers International Union v. International Paper Company, 801 F.Supp. 1134, (S.D.N.Y. 1992), the district court held that the defendant company had knowingly made misleading statements and omissions concerning the company's environmental compliance record in proxy materials distributed to its shareholders in an effort to defeat a shareholder proposal sponsored by the Presbyterian Church (USA) that the company adopt and implement the Valdez Principles, a set of principles pertaining to corporate environmental responsibility. In its opinion, the court stated, "The Board [of the defendant] was presumptively and constructively aware of all relevant details of the Company's environmental record [which indicated serious and ongoing environmental difficulties]; rather than portraying that record accurately, or remaining silent, it chose instead to engage in flowery corporate happy-talk in order to defeat the proposal." 801 F.Supp. at 1144. On appeal, the Second Circuit affirmed the district court's conclusion that the proxy materials in question were materially misleading. United Paperworkers International Union v. International Paper Company, 985 F.2d 1190 (2nd Cir. 1993). The Second Circuit also ruled that the Presbyterian Church could include a description of the results of the litigation in connection with the resubmission of its resolution concerning the Valdez Principles.

3. In Roosevelt v. E. I. DuPont de Nemours & Co., 958 F.2d 416 (D.C. Cir. 1992), the District of Columbia Circuit Court of Appeals recognized a
private right of action to enforce a corporation's obligation to include shareholder proposals in annual meeting proxy materials, but held that the specific proposal at issue - relating to the timing of DuPont's phase-out of the production chlorofluorocarbons and halons and the reporting of (a) research and development efforts to find environmentally sound substitutes and (b) marketing plans to sell those substitutes - concerned matters relating to the corporation's normal business operations and therefore could be excluded from the proxy materials.

4. In Goldsmith v. Rawl, 755 F.Supp. 96 (S.D.N.Y. 1991), the district court rejected motions for summary judgment filed by the defendants, holding that issues of material fact existed as to whether Exxon could be held liable to shareholders for failure to disclose in proxy materials pending shareholder litigation arising out the 1989 accident involving the Exxon Valdez.

5. In AES Corporation Securities Litigation, 825 F.Supp. 578, 588-89 (S.D.N.Y. 1993), the district court refused to dismiss claims brought on behalf of purchasers of securities of AES Corporation where the plaintiffs alleged that statements in prospectuses regarding AES's environmental achievements were rendered false or misleading by the fact that AES's employees had intentionally falsified wastewater discharge reports to give the appearance that one of AES's facilities was operating in compliance with relevant environmental regulations.

6. In Endo v. Albertine, 812 F.Supp. 1479, 1486-88 (N.D. Ill. 1993), the district court refused to dismiss claims for securities fraud based on the alleged failure of Fruit of the Loom, Inc. to disclose adequately environmental liabilities under Superfund and other environmental statutes retained from Velsicol Chemical Company potentially exceeding $60,000,000. In a subsequent decision, the court likewise refused to grant defendants summary judgment on the same issues. Endo v. Albertine, 863 F.Supp. 708 (N.D. Ill. 1994).

7. In Klein v. PDG Remediation, Inc., 937 F.Supp. 323 (S.D.N.Y. 1996), the district court refused to dismiss a class action suit claiming that a company involved in the remediation of petroleum contaminated sites in Florida funded largely by a state reimbursement program for leaking underground storage tanks had violated the Securities Act by failing to disclose information relating to the curtailment of this program in connection with an initial public offering of common stock. The company derived a large portion of its revenue from the reimbursement program but failed to disclose in its registration statement and prospectus that three separate governmental entities had conducted investigations relating to the program. As a result of these investigations, the governmental entities had called for modifications to the program and a moratorium on payments. In addition, the company failed to disclose that the program had operated at a sizable deficit for the previous two years. The court rejected arguments by the company that disclosure was not required because the reports were publicly available and in the "total mix" of information available to prospective investors. The court
maintained that it was unreasonable to assume that nationwide investors, or even Florida investors, would be aware of the reports in question, and denied the company's motion to dismiss.

8. In Horsehead Resource Development Co., Inc. v. B.U.S. Environmental Services, Inc., 928 F.Supp. 287 (S.D.N.Y. 1996), the district court dismissed a complaint alleging that a corporation's filings failed to disclose that it had been the subject of regulatory investigations in Germany relating to serious environmental matters, "repeatedly resulting in the finding of violations of environmental laws and/or regulations in the recent past." The suit was brought by more than five percent of the corporation's shareholders whose stock was registered with the SEC. In an earlier ruling, the court had held that the corporation was obliged to disclose the existence of any and all ongoing criminal cases related to environmental violations. Specifically, the court directed the corporation to either report that its criminal environmental lawsuits were continuing or present evidence that the case had been closed without convictions. Ultimately, the corporation submitted the necessary evidence that the criminal cases were closed and that neither the corporation nor any of its personnel had been convicted of any environmental violations.

9. In Gannon v. Continental Ins. Co., 920 F.Supp.566 (D.N.J.1996), the district court dismissed a claim by a stockholder against the parent company of an insurance carrier alleging mismanagement and violations of federal securities law. The court held, inter alia, that annual reports for 1990, 1991 and 1992, which failed to state that the insurance company had not established reserves for incurred but unreported environmental pollution and asbestos losses, were not actionable as securities fraud. The court determined that the failure to include such information was a simple omission which did not render misleading statements that were actually made. The district court likewise dismissed the claim that inclusion of a statement in the 1993 annual report that no reserves had been established violated the Exchange Act and Rule 10b-5 because the thrust of the claim was one of corporate mismanagement rather than securities fraud.

VII. Conclusion

A. The issues posed by the intersection of financial disclosure and environmental requirements are of critical importance to many businesses. The marriage of these requirements may not be a happy one but is likely to be one of long duration. It is also a marriage that can generate issues of enormous difficulty and complexity - issues that may require the cooperation of professionals from a variety of different fields to resolve in any meaningful fashion.

B. Those businesses which fail to pay close attention to the issues of environmental disclosure may find themselves held accountable by the SEC, lenders, those with whom they engage in transactions, and/or disappointed investors. At the same time, recognition must be given to the many intrinsic difficulties associated with accurately evaluating environmental liabilities and compliance obligations.
Ultimately, it may be left to the courts to sort out whether environmental disclosure responsibilities are being satisfied in an appropriate manner.

C. As the environmental field continues to evolve and members of the regulated community respond in new ways to the challenges posed by environmental considerations, disclosure issues are likewise almost certain to change. For companies that successfully and fully integrate environmental considerations with their overall operations, a meaningful and accurate description of the manner in which environmental issues are being handled may become as important if not more important to investors than a description of episodic compliance problems. In this respect, disclosure models that the SEC considered and rejected in the 1970’s during a period in which the SEC perceived environmental issues to be primarily of social rather than financial importance may take on a renewed vitality.
GOVERNOR'S MORATORIUM ON POWER PLANTS AND NON-COAL MINING

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SECTION D
GOVERNOR'S MORATORIUM ON POWER PLANTS AND NON-COAL MINING

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I. MORATORIUM ON PERMITTING POWER PLANTS

A. Energy Restructuring and the Rise of Merchant Power Plants

1. The Growth of Merchant Plants in the Region

- Ongoing energy “restructuring” by FERC has resulted in development of “merchant” power plants that sell power on the open market as opposed to serving a specific utility customer base.

- The Midwest and Southeast markets have been targeted for merchant plant projects by many developers. Dozens of projects have been proposed for states such as Kentucky, Ohio, Indiana, and Tennessee.

- Many of the proposed merchant plants are gas-fired peak load units as opposed to the coal-fired base load units that make up most of the existing generating capacity.

- States such as Georgia and Tennessee have adopted permitting moratoria to buy time to assess potential impacts of the proposed facilities.

2. Merchant Power Plant Proposals in Kentucky

- Most of Kentucky’s 34 existing power plants were built more than 20 years ago with only 4 built since 1980. These plants were largely built to serve a specific utility customer base.

- From 1999-2001, the state received permit applications for 29 new or expanded power plants, most of which involved merchant generation. Most of the plants would be gas-fired peak load facilities, although some are coal or coal refuse-fired.

- The proposed plants would add more than 12,000 Megawatts (MW) of capacity to the existing capacity of 18,000 MW.

B. Preliminary Regulatory Developments in Kentucky

1. Permitting Moratorium and Review of Impacts

- On June 19, 2001, Governor Patton issued a six-month moratorium on permitting new power plants. This was subsequently extended to July 16, 2002.
• The Governor directed the NREPC and PSC to review the impacts of the proposed power plants on the environment and the state’s power supply grid.

• The Governor created the Kentucky State Energy Policy Advisory Board to develop a statewide energy policy, coordinate review of these issues, and make recommendations for legislation in the 2002 General Assembly.

2. NREPC Cumulative Assessment of Environmental Impacts – December 17, 2001 Report

• The report concluded that most environmental impacts were associated with existing power plants and that the limited impacts of the proposed plants could be mitigated through the environmental permitting process.

• Potential air quality impacts include NOx emissions that could impact attainment under the 8-hour ozone standard and emissions of hazardous air pollutants.

• Potential water impacts include water withdrawal rates that could impact aquatic life or downstream users, wastewater discharges that could impact surface waters, and groundwater impacts from ash ponds.

• Land quality impacts include substantial additional disposal and beneficial reuse of coal combustion ash and deposition of acids and metals from flue gas that could contribute to soil toxicity and bioaccumulation of heavy metals.

• Recommendations include determining the need for additional NOx reductions beyond the NOx SIP call, analyzing air toxic emissions and developing appropriate standards, removing water withdrawal exemptions for power plants, establishing limits for additional effluent constituents, establishing appropriate groundwater standards, addressing landfill and ash pond groundwater issues, modifying the special waste permitting and beneficial reuse programs, studying the total statewide carrying capacity for power plants, adding more staff, and analyzing secondary impacts.

3. PSC Review of the Adequacy of Kentucky’s Generation Capacity and Transmission System – Case No. 387

• Kentucky’s transmission system is adequate to reliably serve native load and, with minor upgrades, to handle a large portion of the proposed new generation.
• Significant upgrades may be needed if the transmission system is to more fully support the future wholesale markets envisioned by FERC.

• Upgrades and expansions required to serve new generation should be funded by those who cause and benefit from these upgrades.

• In the event of transmission constraints, native load should be curtailed only after all other customers have been curtailed.

• Consideration should be given to a public power authority to develop coal-fired generation, shared utility ownership of future base load generation, and coordination of scheduled maintenance of units by utilities.

• There is a need for a regulatory body with jurisdiction over the siting of merchant power plants and transmission.


• The Advisory Board established siting, moratorium, and NOx allowance committees to assess key issues identified by stakeholders.

• The committees recommended that the governor extend the permitting moratorium, establish siting requirements for power generation and transmission lines, and auction the five percent NOx allowance pool set aside for new generation.

C. New Siting Legislation Passed in the 2002 General Assembly - Senate Bill 257

1. The bill creates the Kentucky State Board on Electric Generation and Transmission Siting and the Environment.

• No person may construct a merchant electric generating facility or non-regulated electric transmission line without first obtaining a construction certificate from the Board.

• “Merchant plant” is defined to cover facilities capable of generating 10 MW or more which sell power on the wholesale market at rates not regulated by the PSC.

• “Non-regulated electric transmission line” is defined to cover lines which do not require a certificate of public convenience and necessity, are not subject to PSC regulation, and can operate at or above 69,000 volts.
• Merchant plants do not include facilities which are qualifying cogeneration facilities or contract to sell 100% of their power to PSC-regulated utilities for baseload purposes, locate on existing utility sites, and obtain PSC approval of their power supply contracts.

• Approval requirements do not apply to a utility owned by a municipality unless it constitutes a merchant plant.

• Replacement with a like facility or repair, modification, retrofitting, enhancement or reconfiguration does not constitute construction.

• The Board may assess fees to cover the cost of reviewing applications.

2. Board membership includes representatives of state agencies and local governments.

• The three members of the PSC (with the PSC chairman also chairing the Siting Board)

• The Secretary of the NREPC or designee

• The Secretary of the Cabinet for Economic Development or designee

• One representative at large appointed by the Governor for a two year term

• One local representative appointed by the county judge/executive or mayor of the local jurisdiction in the case of merchant generation or non-regulated transmission line applications.

3. Setback requirements for merchant plants.

• Setback of 1,000 feet from the property boundary of any adjoining property owner (except for facilities to be located on former coal prep plant sites which will utilize on-site waste coal as a fuel source).

• Setback of 2,000 feet from any residential neighborhood, school, hospital, or nursing home facility.

• Setback of 400 feet from any residential structure, residential neighborhood, school, hospital, or nursing home facility if the proposed facility is to be located on a river and use clean coal technology.

• Setback requirements established by a local Planning and Zoning Commission have primacy over the Board’s setback requirements.
The Board may grant a deviation, except in the case of local setback requirements, on a finding that the proposed facility is designed and located to meet the goals of the Act at a closer distance.

4. **Application requirements for merchant plants.**

- A full description of the site, including map showing distance to specified structures within a two mile radius.

- Evidence of compliance with public notice requirements.

- A report of the applicant’s public involvement program activities.

- Proof of service of the application upon the chief executive officer of county, municipal corporation, and land use planning agency.

- A summary of the efforts made to locate the proposed facility on a site where existing facilities are located.

- A certification that the plant will be in compliance with all local ordinances and regulations concerning noise control and with any applicable planning and zoning requirements.

- A statement that the plant complies with setback requirements.

- Analysis of the proposed facility’s projected effect on the electricity transmission system.

- Analysis of the proposed facility’s economic impact on the affected region and state.

- A detailed listing of all violations by the applicant or any of its affiliates or subsidiaries where violations have resulted in criminal convictions or fines exceeding $5,000 (and status of any pending action whether judicial or administrative).

- A site assessment report identifying site impacts (or in the alternative, documentation of NEPA compliance).
5. Site assessment reports

(a) Preparation of the report

- The report must be prepared by a consultant from a list of board-approved consultants.
- The board may hire a consultant to review the site assessment report and provide recommendations concerning the adequacy of the report and proposed mitigation measures.

(b) Element of the report

- A description of the proposed facility including surrounding land uses; proposed site access control, location of proposed structures and property boundaries; location and use of access ways, internal roads, and railways; existing or proposed utilities; compliance with setback requirements; and evaluation of expected noise levels.
- An evaluation of the compatibility of the facility with scenic surroundings.
- The potential changes in area property values resulting from siting, construction, and operation.
- Evaluation of anticipated peak and average noise levels associated with construction and operation.
- Impact of operation on road and rail traffic, including anticipated fugitive dust levels, and degradation of roads and lands in the vicinity.
- Suggested mitigating measures including planting trees, changing outside lighting, erecting noise barriers, and suppressing fugitive dust.

6. Determination to grant or deny.

(a) Criteria for determination

- Impact of the facility on scenic surroundings, property values, the pattern and type of development of adjacent property, and surrounding roads.
• Anticipated noise levels expected as a result of construction and operation.

• The economic impact upon the affected region and the state.

• Whether the facility is proposed for a site upon which are located existing generating facilities of greater than 10 MW capacity.

• Whether the applicant has met all requirements for transmission interconnection under Kentucky law and the open access transmission tariff of the host transmission owner or regional transmission owner.

• Compliance with setback requirements.

• Whether the applicant possesses the financial, technical, and managerial capacity to construct and operate the proposed facility.

• The efficacy of any proposed measures to mitigate adverse impacts.

• Whether the applicant has a good environmental compliance history.

(b) Other approval issues

• The Board may also consider the policy of the General Assembly to encourage the use of coal as a principal fuel for electricity generation.

• The Board may condition approval on implementation of any mitigation measures the Board deems appropriate.

• A construction certificate for a merchant generating plant may not be transferred to another party without a Board determination that the acquirer has a good environmental compliance history; and the financial, technical, and managerial capacity to meet obligations.

7. Compatibility certificates for proposed utility generating plants.

• No utility shall commence construction of a generating facility with a capacity of more than 10 MW, for which a certificate of public necessity and convenience has not been granted prior to the effective date, without having first obtained a site compatibility certificate from the PSC.
• An application shall include submittal of a site assessment report, except that a facility proposed for an existing generating site shall not be required to comply with setback requirements.

• The PSC may deny an application or require reasonable mitigation of impacts including planting trees, changing outside lighting, erecting noise barriers, and suppressing fugitive dust. The PSC may not order relocation of the facility.

• No person may acquire ownership or control or the right to control any assets that are owned by a utility without prior PSC approval if such assets have an original book value of $1 million or more and are transferred for reasons other than obsolescence or will continue to be used to provide the same or similar service to a utility or its customers.

8. Non-regulated transmission lines.

(a) Application Requirements

• A description of the proposed route including proposed right of way and proximity to specified structures.

• A description of the proposed line including design, specifications, capacity, costs, and appearance.

• A statement that the facilities will be constructed and maintained in accordance with the National Electric Safety Code.

• Evidence of compliance with requirements for notice to the public and local officials and a report of the applicant's communication and public involvement efforts.

(b) Determination to grant or deny

• A determination, by majority vote, to grant or deny must be made within 90 days of receipt of the application or 120 days if a local public hearing is held.

• The determination to grant or deny must be based on the following criteria: the proposed route will minimize adverse impact on the scenic assets of Kentucky; the applicant will construct and maintain the line in accordance with all applicable legal requirements.
• If the Board determines that there will be degradation of scenic factors or violation of applicable legal requirements, the Board may deny the application or condition approval on relocation of the route of the line.

9. A Cumulative Environmental Assessment must be submitted by persons applying to the NREPC for a permit.

(a) Applicability

• No person shall commence construction of a facility to be used for the generation of electricity on or after April 15, 2002 without submitting a cumulative environmental assessment and paying any fees imposed by the NREPC.

• The requirement applies to both the merchant and utility generating plants.

(b) Elements of report

• Identification and quantification of air contaminants that may be emitted, description of emissions controls, and identification and quantification of air contaminants that may be deposited onto land or waters.

• Identification and quantification of water pollutants that may be discharged and description of control methods.

• Identification and quantification of waste that may be generated and description of methods to be used to manage and dispose.

• Identification and quantification of waters that may be withdrawn and description of methods for managing water usage.

(c) Conditional approval

• The NREPC may condition approval of a permit subject to reduction or elimination of cumulative environmental impacts.

• Conditions may include reductions in air emissions, water discharges, waste generation, and water withdrawal as necessary to prevent air pollution, prevent water pollution, protect the best interests of the public and water users, or promote waste reduction.
10. **Procedural Requirements.**

- A local public hearing may be convened if requested by not less than three interested parties that reside in the county or municipal corporation of the proposed facility or the planning and zoning commission, mayor, or fiscal court of the jurisdiction of the proposed facility.

- Parties to hearings include the applicant and interested persons granted the right of intervention. Hearings must be conducted in accordance with rules adopted by the Board.

- The Board must, by majority vote, grant or deny a certificate within 90 days of receipt of an administratively complete application or within 120 days of receipt if a hearing is requested.

- Any party may appeal a final determination to the circuit court of the county in which the proposed facility is to be located within 30 days of receipt of the determination.

11. **Mitigation of transmission impacts.**

- No utility shall begin construction of facilities to establish interconnection with a merchant plant in excess of 10 MW capacity without prior approval of plans and specifications by the PSC.

- Expenses associated with upgrading the existing transmission grid as a result of additional load caused by a merchant plant shall be borne by the merchant plant.

- In the event of transmission curtailments, there shall be no curtailments or interruptions of retail electric service or wholesale electric service to a distribution cooperative (except for interruptible service) unless service has first been interrupted to all other customers whose interruption may relieve the emergency or other event.

**II. MORATORIUM ON NON-COAL MINING PERMITS**

A. **Background**

- Non-coal mining in the state includes limestone quarries, sand and gravel operations, and clay pits. These include 211 permitted sites that cover 37,809 acres.
• Environmentalists have criticized the non-coal program as its requirements are less stringent than the requirements placed on the coal industry pursuant to SMCRA.

• On September 21, 2001, Governor Patton imposed a moratorium on issuance of non-coal permits through July 15, 2002 and required review of all oil and gas permits. The Governor directed the Department of Mines & Minerals to review applications for new wells in the vicinity of Breaks Interstate Park, Cumberland Gap, and Pine Mountain. The Governor also directed the agencies to review permitting and reclamation requirements for non-coal mining operations and oil and natural gas wells.

• The NREPC’s December, 2001 report identified areas where the non-coal program is less stringent than requirements imposed on coal operations.

B. Changes under consideration for the non-coal program.

• More stringent bonding requirements

• Highwall elimination for quarries

• Contemporaneous reclamation

• Lands unsuitable for mining

• Pre-blasting surveys

• Fugitive dust control

C. Action Anticipated in the Future

• The NREPC is currently pursuing a dialogue with stakeholders on potential revisions to the non-coal permitting program.

• Emergency regulations are anticipated prior to expiration of the permitting moratorium on July 15, 2002.
SURETYSHIP, BONDING COMPANY AND BANKRUPTCY LAW ISSUES IN ENVIRONMENTAL LAW PRACTICE

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SECTION E
OPTIMIZING LAND RECLAMATION AND ENVIRONMENTAL PROTECTION:

MAKING THE MOST OUT OF SURETY AGREEMENTS

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OPTIMIZING LAND RECLAMATION AND ENVIRONMENTAL PROTECTION:
MAKING THE MOST OUT OF SURETY AGREEMENTS

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SECTION E(a)
I. INTRODUCTION - SMCRA AND SURETYSHIP

A. SMCRA

- The regulation of coal mining in the United States is governed by the federal Surface Mining Control and Reclamation Act,¹ ("SMCRA"). Several purposes of SMCRA include the establishment of a nationwide program to protect society and the environment from the adverse effects of surface coal operations;² assuring the rights of surface landowners and other persons with a legal interest in the land are fully protected³ and assuring that adequate procedures are undertaken to reclaim surface areas as contemporaneously as possible with the surface coal operations.⁴

- Under SMCRA a mining company must file an application for a surface mining permit which includes detailed operations and reclamation plans and the posting of reclamation performance bonds.⁵

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¹ 30 U.S.C. § 1201 et seq.
² 30 U.S.C. § 1202(a)
³ 30 U.S.C. § 1202(b)
⁴ 30 U.S.C. § 1202(e)
⁵ 30 U.S.C. § 1256; 30 C.F.R. § 800 et seq. There has been confusion in the regulatory arena as to whether reclamation are "penal bonds" or "performance bonds." OSM has stated, "OSM views a reclamation bond as one guaranteeing the performance of reclamation work. Therefore it is not a penal bond." See 48 Fed. Reg. § 32932, July 19, 1983

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SMCRA has specific regulatory frameworks for bonding the reclamation plans and performance of the coal mine permittee. Bonds may be in the form of a corporate surety bond, cash collateral or securities.\(^6\)

The bonded obligations include compliance with other environmental laws and regulations often including laws related to water quality, coal refuse disposal, mine subsidence and waste management.

B. **Suretyship** - Very few outside of the surety industry (including judges), fully understand exactly what a surety bond is. Many mistakenly regard "bonds" as insurance policies. **Suretyship is not insurance.**\(^7\) The distinction between the two concepts is as follows:

- **In suretyship:** There is a three party contract where a surety provides a financial guarantee, only if the principal (permittee) fails to meet its obligation to the obligee (regulatory agency). The principal is required to reimburse the surety,\(^8\) therefore a surety expects no loss. The principal is the primary obligor and the surety is the secondary obligor.

- **In insurance:** There is a two-party contract where an insurance company spreads the risk of losses over a group of insureds and expects to take a loss during the policy period. If an insured event occurs, the insurance company pays with no recourse against the insured.

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\(^6\) 30 C.F.R. § 800.12


\(^8\) See *The Law of Suretyship* 2d Ed. 1993 Edward Gallagher. In the underwriting analysis, the principal's financial and performance capability is assessed; risk is not spread as in insurance.

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• Many principles of surety law apply along with the regulatory framework. For example: "Subrogation" is an important concept that allows the surety to "step into the shoes" of either the permittee or the regulatory agency depending on the situation. A surety is entitled to assert all of the defenses of its principal. A surety who pays the debts of another is entitled to all the rights of the person he paid (obligee) to enforce his rights to be reimbursed. The doctrine of subrogation also allows a surety to step into the shoes of the government for whom the job was completed.

Often there are conflicts between secured creditors (lenders) who want money from the bankrupt estate and the regulatory agency, permittee and surety who all want reclamation accomplished. The surety, for example, can argue the state’s position regarding the need for compliance with state law under § 959 of the bankruptcy code.

C. Reclamation surety bonds fit into the special category of "statutory bonds" and as such encompass the requirements of the regulatory program itself.

II. BOND FORFEITURE

A. Due in large part to the adverse economic climate surrounding the coal and steel industries, (notwithstanding the recent up-tic in the coal market and subsequent plummet)
numerous companies with large coal mine environmental obligations have been dissolved or become bankrupt in the last ten years including most recently Lodestar Energy, LTV Steel, Bethlehem Steel, AEI Resources, Quaker Coal, Pen Holdings and others. In such an event, notwithstanding a potential successful reorganization, coal operations that have stopped in mid-operation become "problem mines," and may be subject to bond forfeiture for various reasons.\(^\text{13}\)

B. From our experience the first sign that a company is strapped for cash, is lack of environmental compliance. Often, the field inspectors are the first to notice "short cuts" by a company.

C. Under SMCRA, the regulatory agency must notify the permittee and surety of its intent to forfeit the bonds and advise of conditions under which forfeiture may be avoided.\(^\text{14}\) By this time, however, it is usually very late in the game for the surety to be able to have significant influence over its bonded principal. Earlier notice to the surety when the agency anticipates a problem may have a more positive result and may avoid forfeiture altogether. As a matter of fact, during the rulemaking process OSM recognized that "adequate latitude is available for the regulatory authority to withhold forfeiture if an operator or a surety agree to a compliance schedule for completing reclamation successfully."\(^\text{15}\)

D. Under SMCRA the agency can generally proceed to collect the bonds unless there have been actions to avoid forfeiture or an appeal has been filed,\(^\text{16}\) however some states (e.g., Kentucky) require a pre-payment of the bond in order to pursue the appeal.\(^\text{17}\)

\(^{13}\) 30 C.F.R. § 800.50
\(^{14}\) 30 C.F.R. § 800.50(a)(1) & (2)
\(^{16}\) 30 C.F.R. § 800.50(b)
\(^{17}\) KRS 350.032(3).
E. Principles of surety law ordinarily allow a surety to either perform the bonded obligation in the event of a default or to pay the bond amount. Under SMCRA and most state programs surety reclamation is allowed.\textsuperscript{18} Based on our experience in the field, under the most complicated technical and legal scenarios, surety reclamation should be encouraged.

III. SURETY RECLAMATION WORKOUTS

A. Many of the most complicated matters facing the regulatory agencies and sureties have involved the large company bankruptcies or dissolutions with numerous sites involving all aspects of mining. The handling of these matters particularly by the agency, affects other interests including landowners, neighbors, communities and environmental interests.

B. If the bond is forfeited and collected by the agency, the agency, usually through its AML program, may conduct reclamation under specific, time consuming and more expensive state procurement procedures ("AML Dollars").

C. It has been our experience that surety reclamation can provide more reclamation on the ground per dollar by using private sector resources, expediency and experience in bidding and contracting.

D. Recent successful surety reclamation projects have included:

- Open dragline pits
- Acid mine drainage passive system development
- Burning refuse piles
- Mine shaft closures
- Borehole sealing

\textsuperscript{18} 30 C.F.R. § 800.50(a)(2)(ii).
• Prime farm land restoration
• Wetlands/habitat enhancement
• Preparation plant demolition
• Coal refuse/slurry impoundment reclamation
• PCB removal
• Aerial tram removal
• Contour mine reclamation
• Hydraulic seals to flooding deep mines.

E. Reclamation is conducted under a Consent Order and Agreement, Consent Agreement or Settlement Agreement which defines the scope of work, work schedule and bond release or "waiver of collection" schedule where the bond remains technically "forfeited."

- A critical factor to the surety is "certainty" as to performance requirements since it will have conducted its own engineering/economic analysis regarding the project prior to signing an agreement to perform.

F. The surety is not the permittee and is not subject to permitting requirements as is an operator.\(^\text{19}\)

G. Many of the larger cases are also subject to U.S. Bankruptcy Court jurisdiction therefore the surety, permittee and agencies must deal with a Trustee or Debtor in Possession and

\(^{19}\) See 48 Fed. Reg. 32932, July 19, 1983 where OSM in discussing its final federal rules regarding bonding requirements stated in response to a state agency question as to "whether in accepting a permittee's obligation for reclamation after forfeiture, the state or surety assumes the obligation for phase releases, water quality control, NPDES monitoring and revegetation" OSM stated, "All plans and specifications found in the permit must be met in contracting for completion of reclamation. However, neither the regulatory authority nor the contractor assumes the liability of the permittee." (emphasis added)
other creditors. Most real legal conflicts occur here due to the intersection of environmental law, surety law and bankruptcy law. There are inherent competing interests:

- **Goals of bankruptcy law:** get funds back to creditors;
- **Goals of SMCRA:** get land reclaimed (i.e. put $ in the dirt)

H. The surety and agency interests are usually aligned in bankruptcy proceedings, however, often the agency takes a back seat in the proceedings.

IV. **PROBLEMS IN NEGOTIATING SURETY AGREEMENTS**

A. Large multi-mine bankruptcies create very complicated situations - technically and legally and require significant time and effort to understand relevant relationships and prospects for successful emergence from bankruptcy in order to develop strategy, e.g. Quaker Coal, AEI Resources.

B. Due to usual negative history with the permittee leading to bond forfeiture, the surety is often faced with an irritated audience at the agency and with landowners.

- Very often, the principal/permittee is in arrears regarding royalty payments to the mineral owners, has left surface owner’s property in disrepair and has created bad relations with the regulatory agency.
- More often that not, regulatory staff does not understand suretyship and often confuses the surety as a surrogate coal operator.
- Regulatory staff often view the bond amounts as “agency money.”
- It is not uncommon for the bond amount to not cover full reclamation since the operation was stopped in mid-stream.
- Bankruptcy court jurisdiction may overlay the entire matter.
- Landowners can be recalcitrant and litigious.
C. Bankruptcy court approval of any workout is necessary (remember, the primary environmental obligation is that of the bankrupt company).

V. WHEN RECLAMATION EXCEEDS THE BOND AMOUNT

A. SMCRA allows the agency to pursue the permittee for excess costs if the bond amounts do not cover the reclamation costs.20 This provision is probably moot since the permittee is bankrupt.

B. If the bond amounts go to the agency, then using "AML Dollars" and government contracting procedures, less work gets accomplished and it takes longer.

C. In recent experiences with a few states we were told "OSM won't let the state enter surety agreement if it's for less than the entire reclamation plan" even though there are discreet, identifiable reclamation tasks that must be accomplished: e.g.s, eroding hollow fill on steep slopes; acid filled pits, where the surety would have been able to abate the hazard or make a substantial contribution to reclamation within the bond amount, but not reclaim the entire site.

D. In other cases, in resolution of appeals filed with the administrative hearing officers under SMCRA or in the bankruptcy cases we have been able to identify key tasks in the reclamation plan that required immediate attention or high priority and come to an agreement on scope of work and waiver of bond collection.

E. In those cases, it's a win for all parties and the states AML funds are preserved.

20 30 C.F.R. § 800.50(d)(1)
VI. **BENEFITS OF SURETY RECLAMATION**

A. Facilitates the purposes of SMCRA in addressing the adverse effects of surface coal mining operations, protection of the environment and the rights of landowners.

B. Land gets stabilized; pollution gets abated using private sector resources instead of limited government resources (agency still has jurisdiction).

C. More actual reclamation activity can be conducted on a per dollar basis since there are no government procurement requirements in private contracts between the surety and contractors.

D. Surety can mitigate its loss.

E. Landowner gets property returned to stable status.

F. Surety is additional advocate for environmental protection in bankruptcy proceedings.
ENFORCEMENT OF STATE BONDING REQUIREMENTS AS EXERCISE OF POLICE OR REGULATORY POWER IN BANKRUPTCY PROCEEDINGS - RECENT OBSERVATIONS

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1. Overview

A. Operators in industries subject to environmental regulations, are required to post bonds in order to commence and continue operations.

[1] KRS KRS 350.060 conditions the issuance of a surface coal mining and reclamation permit upon the filing of a reclamation bond for performance, "payable to the Commonwealth of Kentucky...conditioned upon the faithful performance of the requirements set forth in this chapter and of the administrative regulations of the Cabinet."

[2] 405 KAR Chapter 10 sets forth the regulatory scheme for surface mining performance bond and liability requirements.

B. Insurance Law


[2] As a result of Frontier’s placement in rehabilitation, the Kentucky Department of Insurance suspended its certificate of authority in Kentucky pursuant to KRS 304.
This course of events, coupled with an apparent incongruence between Frontier’s ability to honor its bonds under KRS 304, although its certificate of authority has been suspended, and surface mining regulations requiring replacement of Frontier bonds, led to particularly well-publicized problems in coal surface mining, involving several large coal companies.

C. Bankruptcy

[1] Debtors in bankruptcy are protected by the automatic stay provisions of 11 U.S.C. §362, which preclude “the commencement or continuation . . . of each judicial, administrative, or other action or proceeding against” debtors.

[2] States may avoid the protections of the automatic stay pursuant to its police and regulatory exception in §362(b)(4), which exempts from the stay “the commencement or continuation of an action or proceeding by a government unit . . . to enforce such governmental unit’s . . . police or regulatory power . . . other than [the enforcement of] a money judgment.”

D. Issue/Problem

[1] Is state action forcing the replacement of bonds violative of the automatic stay or does it fall within the police or regulatory power exception?

2. Objective or Subjective Test—Chao or Safety Kleen?

A. Chao v. Hospital Staffing Services, Inc., 270 F.3d 374 (6th Cir. 2001)

[1] Facts of the case

[b] HSSI files for Chapter 11 protection, but converted to Chapter 7.

c] In the last two weeks of its operations, HSSI did not pay employees’ wages, and thus, the goods produced by their labor were considered “hot goods” for purposes of the Fair Labor Standards Act’s minimum wage provisions.

d] The United States Secretary of Labor sought an injunction in the Western District of Tennessee to stop transportation of the “hot goods.”

e] The district court issued a preliminary injunction and ordered the trustee of HSSI’s bankruptcy estate to pay approximately $615,000.00 in order to purge the taint of hot goods. These funds came from the creditor pool of HSSI’s Chapter 7 liquidation assets, as determined in the parallel Florida bankruptcy action.

f] After the district court’s ruling on the issue, the bankruptcy court held that Secretary’s suit was an action to collect a debt rather than an exercise of police power, taking it out of the automatic stay exception, supra. However, the bankruptcy court did not enter the order because of the contemporaneous proceedings in district court and corresponding jurisdictional concern.

[g] Thereafter, the trustee appealed from district court’s denial of its motion to dismiss, the court’s grant of a preliminary injunction, and the order directing the deposit of funds purging the taint of the hot goods.
Looking behind the stated legislative Purpose -- Chao's subjective 
tests for purpose of the police power or regulatory exception to the automatic stay—primary 
purpose of the governmental unit’s (state or federal) enforcement action. ¹

Court applies two tests: the pecuniary purpose test and the public 
policy test.

[a] Pecuniary Interest test

[i] “Reviewing courts focus on whether the governmental 
proceeding relates primarily to the protection of the government’s pecuniary 
interest in the debtor’s property, and not to matters of public safety. Those 
proceedings which relate primarily to matters of public safety are excepted 
from the stay.” Id. at 387.

[ii] “We join the Eighth Circuit in refining the “pecuniary 
interest test to focus our inquiry on whether the enforcement action would 
result in a pecuniary advantage to the government vis-a-vis other creditors 
of the bankruptcy estate.” Id. at 389 n. 9 (italics in original, emphasis 
otherwise added).

¹
As discussed infra, Safety-Kleen’s analysis of the exception relies on the stated Congressional or 
legislative purpose for the law pursuant to which enforcement is sought. This test is 
characterized as the “primary purpose test,” i.e., what is the primary purpose of the law being 
enforced. On the other hand, Chao retains the pecuniary interest and public policy tests and 
emphasizes the fact that their analyses are to be conducted subjectively to determine the motive 
behind the government’s particular enforcement action. Thus, although Safety Kleen and Chao 
probably can’t be reconciled, Chao’s tests can also involve the examination of the “primary 
purpose” behind an action, but do so by looking behind the cloak of the government’s stated 
policy.
Chao explained that a subjective case-by-case analysis is required for the analysis under both tests. The Court reasoned that although all acts of Congress declare national policy, the "public policy test calls upon courts to analyze whether a particular lawsuit is undertaken by a government entity in order to effectuate public policy . . . ." * * * "This court's pecuniary interest and public policy tests recognize this limitation and are designed to sort out cases in which the government is bringing suit in furtherance of either its own or certain private individuals' interest in certain private parties' interest in obtaining a pecuniary advantage over other creditors." * * * "Accordingly, courts should examine the type of enforcement action brought and the relationship between a particular suit and Congress's (or a state's) declared public policy." Id. 389, 390. (underline added, emphasis otherwise in original).

Although Chao went to great lengths to explain the pecuniary interest test, the court held that it was inapplicable because the Secretary was seeking a pecuniary advantage for private citizens, not itself, per public policy test, as explained infra.

Public Policy test

"Under the public policy test, the reviewing court must distinguish between proceedings that adjudicate private rights and those that effectuate public policy. Those proceedings that effectuate a public policy are excepted from stay."
As explained above, *Chao* held that the court should not rely blindly upon the stated policy of the law being enforced. All laws by definition declare public policy, so courts applying the tests must look at the particular motive behind the state or federal government’s action.

In *Chao*, the Secretary of Labor was enforcing FLSA provisions primarily to have HSSI’s employees paid for the work conducted in its last weeks’ existence.

Accordingly, the court held “[W]hen the action incidentally serves the public interest but more substantially adjudicates private rights, courts should regard the suit as outside the police power exception, particularly when a successful suit would result in a pecuniary advantage to certain private parties vis-a-vis other creditors of the estate, contrary to the Bankruptcy Code’s priorities.”

Analysis/Conclusions—*Chao* sets forth subjective and flexible tests that prevent the governmental unit from hiding behind the veil of its stated public policy.


Facts of the Case

Safety Kleen (“SK”), which operated hazardous waste facilities in South Carolina, had purchased performance bonds from Frontier. On June 1, 2000 the United States Treasury removed Frontier from its list of approved sureties, triggering South Carolina requirements that hazardous waste performance bonds issued by an insurance company which is not on the approved list, be replaced.
[b] On June 9, 2000, the South Carolina Department of Health and Environmental Control ("DHEC") ordered SK to replace its bonds. SK filed Chapter 11 that day.

[c] SK filed an adversary proceeding against DHEC in district court seeking a preliminary injunction against DHEC closing its facility.

[d] The district court denied the preliminary injunction but held that forcing bond replacement violated the automatic stay.

[e] SK appealed the denial of the preliminary injunction and DHEC cross-appealed the court’s determination that its actions violated the automatic stay.


[a] Primary Purpose Test

[i] The Court explained the considerations due when applying the police or regulatory power exception to the automatic stay as follows:

The difficulty in applying [the police and regulatory power] exception comes in distinguishing between situations in which the state acts pursuant to its ‘police and regulatory power’ and situations in which the state acts merely to protect its status as a creditor. To make this distinction, we look to the purpose of the law that the state is attempting to enforce. If the purpose of the law is to promote ‘public safety and welfare’ or to ‘effectuate public policy,’ then the exception applies. On the other hand, if the purpose of the law relates ‘to the protection of the
government's pecuniary interest in the debtor's property,' then the exception is inapplicable.

*Id.* at 865 (citations omitted).

[ii] The most important aspect of the court's analysis stated: "[t]he inquiry is objective: we examine the purpose of the law that the state seeks to enforce rather than the state's intent in enforcing the law in a particular case." *Id.* (emphasis added).

[iii] In this regard, *Safety Kleen*’s analysis of the issue appears to diverge from the analysis required in this circuit by *Chao*.

[iv] The difference in application is evidenced by the following statement by the court: "[t]he fact that one purpose of the law is to protect the state’s pecuniary interest does not necessarily mean that the exception is inapplicable. Rather, we must determine the primary purpose of the law that the state is attempting to enforce." *Id.* (emphasis in original).

[v] "In considering whether the regulatory exception applies to environmental laws, courts often focus on whether deterrence is the primary purpose of the law." *Id.*

[vi] With regard to South Carolina’s bonding requirements for hazardous waste facilities the court reasoned as follows:

The financial assurance regulations are within the regulatory exception because they serve the primary purpose of deterring environmental misconduct. Stated more positively, the regulations serve to promote environmental safety *in the design and*
operation of hazardous waste facilities. The incentive for safety is obvious: the availability and cost of a bond will be tied directly to the structural integrity of a facility and the soundness of its day-to-day operations...Id. at 866 (emphasis added).

The court did not further explain the link between the availability and costs of bonds and hazardous waste facilities’ structural integrity and the soundness of its day-to-day operations, but its focus on costs suggests the logic that if the facility cannot afford bonds or afford to replace them, it probably cannot afford to operate with the level of safety demanded by state regulations.

[vii] The EPA and South Carolina hazardous waste financial assurance regulations examined in Safety Kleen spell out “how the regulations would promote environmental protection at active hazardous waste facilities . . . ,” by creating incentives “‘to locate, design, and operate facilities to minimize closure and post-closure costs’ and to ‘improve operating procedures and reduce the risk of accidents’. ” Id.

[viii] The court holds that South Carolina’s assurance requirements are an exercise of state’s regulatory power because they have the primary purpose of deterring environmental misconduct and safe design and operation. Accordingly, the stay was not violated.

[b] Analysis

[i] The particular policies and concerns at issue in Safety Kleen may be peculiar to hazardous waste facilities.

[ii] In the case of coal surface mining, such as the Lodestar case, discussed infra, location (one of the factors relied upon by the Safety
Kleen court) is dictated by the presence of coal, i.e., coal is generally in seams beneath the earth’s surface whereas the location of a hazardous waste facility is usually a controversial process involving considerations highly sensitive to public safety and often fraught with public concern regarding alternative placements.

[iii] Likewise, the link between financial assurance requirements and day-to-day operations is not as evident in the coal industry as in the hazardous waste industry.

[iv] Safety Kleen’s instruction on how the primary purpose test should be applied is opposed to the tests set forth in Chao.

3. Lodestar– Chao and Safety Kleen

A. Facts and Kentucky law

[1] On March 30, 2001 involuntary petitions were filed against Lodestar, and it entered Chapter 11 bankruptcy on April 27, 2001, maintaining operations as a debtor in possession.

[2] When Frontier lost its certificate of authority under KRS 304.3-220, it maintained its ability to “service its business already in force in this state.” Id.

[3] The Cabinet filed a notice of replacement under 405 KAR 10:030, which required Lodestar to replace its Frontier bonds within 90 days or stop operating and begin reclamation, also conditioning any resumption of operations on bond replacement.

[4] The notice was failed on August 28, 2001 creating a November 26, 2001 deadline.
Lodestar did not seek review of the Cabinet’s determination.

On November 16, 2001, Lodestar filed an adversary proceeding to enjoin the Cabinet from enforcing the replacement of the Frontier bonds.

Lodestar also filed a Motion for an Order Determining that Certain Threatened Actions Would Violate the Automatic Stay in its main bankruptcy action.


The court, relying in part on *Chao* and applying the pecuniary interest test found for Lodestar on both.

**B. Analysis**

- The court relied on *Chao* and its tests.
- Pecuniary interest found—“The Defendants demand replacement of bonds be primarily an action to preserve the private rights and interests of Kentucky as a potential creditor of Lodestar and not to effectuate public policy. The adverse actions are pecuniary in nature and not being undertaken to effectuate public policy. Adverse actions do not constitute actions to enforce the Commonwealth’s police and/or regulatory power within the meaning of 11 U.S.C. Section 362(b)(4).”

  - The court relied heavily on the continued validity of Frontier bonds—under KRS 304, and the apparent incongruence between those provision and the replacement requirement under 405 KAR 10:030 §2(5)(c)3. Transcript at 55, See *In re Lodestar Adversary Proceeding No. 01-5248*, November 21, 2001.
[b] Unlike the 4th Circuit in Safety Kleen, the bankruptcy court found that "Lodestar’s inability to comply with the rebonding demand does not create . . . an imminent threat to public health, safety, or welfare, and that there is no current threat to the environment arising from the uncertainties associated with the Frontier bonds.” Transcript at 57.

[c] The court noted that Lodestar has performed the reclamation efforts comprehended by its permits, or substantially performed them...and intends to continue doing so, unless forced to cease operation by enforcement of rebonding demands. Transcript at 57.

[d] The court also found that "the practical significance of enforcement of the – rebonding demand would be to compel Lodestar to cease operations and immediately terminate all of its eight hundred and fifty to nine hundred employees. The officers and directors at Lodestar could possibly be the subject of civil and criminal liability, and may, therefore, be required to resign rather than subject it to those potential liabilities.” Transcript at 57.

C. Safety Kleen

[1] The state is now seeking to have the bankruptcy court set its previous order aside, relying, in part, upon Safety Kleen, which was decided after Chao and after the issuance of the bankruptcy court’s injunction orders.

[2] The analyses in these cases may not be reconcilable. Chao is the law of this circuit and Safety Kleen is not.
304.3-220. Duration of suspension - Insurer's obligation during suspension period - Reinstatement.

(1) Suspension of an insurer's certificate of authority shall be for such period as the commissioner specifies in the order of suspension, but not to exceed one (1) year. During the suspension the commissioner may rescind or shorten the suspension by his further order.

(2) During the suspension period the insurer shall not solicit or write any new business in this state, but shall file its annual statement, pay fees, licenses, and taxes as required, and may service its business already in force in this state, as if the certificate of authority had continued in full force.

(3) Upon expiration of the suspension period, if within such period the certificate of authority has not terminated, the insurer's certificate of authority shall be automatically reinstated unless the commissioner finds that the causes of the suspension have not terminated, or that the insurer is otherwise not in compliance with the requirements of this code, and of which the commissioner shall give the insurer notice not less than thirty (30) days in advance of the expiration of the suspension period. If not so automatically reinstated the certificate of authority shall be deemed to have terminated as of the end of the suspension period.

(4) Upon reinstatement of the insurer's certificate of authority, the authority of its agents in this state to represent the insurer shall likewise be reinstated. The commissioner shall promptly notify the insurer and its agents in this state of record in the department, of such reinstatement. If pursuant to subsection (3) of KRS 304.3-210, the commissioner has published notice of such suspension he shall in like manner publish notice of the reinstatement.


COLLATERAL REFERENCES

350.060. Permit requirement — Contents of application — Fee — Bond — Exemptions — Administrative regulations — Successive renewal — Auger mining of previously mined area — Exempt operations.

(1) (a) No person shall engage in surface coal mining and reclamation operations without having first obtained from the cabinet a permit designating the area of land affected by the operation. Permits shall authorize the permittee to engage in surface coal mining and reclamation operations upon the area of land described in his application for a period not to exceed five (5) years. However, if an applicant demonstrates that a specified longer term is reasonably needed to obtain necessary financing for equipment and the opening of the operation and if the application is full and complete for the specified longer term, the cabinet may grant a permit for the longer term. No mining shall be permitted beyond the time period obligations of the initial or extended bond coverage.

(b) Subject to the provisions of KRS 350.010(1) and (2), no person shall knowingly and willfully receive, transport, sell, convey, transfer, trade, exchange, donate, purchase, deliver, or in any way derive benefit from coal removed from any surface mining operation which does not have a permit as required under this section.

(2) No permit or revision application shall be approved unless the application affirmatively demonstrates, and the cabinet finds in writing on the basis of the information set forth in the application or from information otherwise available, that the permit application is accurate and complete and that all the requirements of this chapter have been complied with.

(3) A person desiring a permit to engage in surface coal mining operations shall file an application which shall state:

(a) The location and area of land to be affected by the operation, with a description of access to the area from the nearest public highways;

(b) The owner or owners of the surface of the area of land to be affected by the permit and the owner or owners of all surface area adjacent to any part of the affected area;

(c) The owner or owners of the coal to be mined;

(d) The source of the applicant's legal right to mine the coal on the land affected by the permit;

(e) The permanent and temporary post office addresses of the applicant, which shall be updated immediately if changed at any point prior to final bond release;

(f) Whether the applicant or any person, partnership, or corporation associated with the applicant holds or has held any other permits under this chapter, and an identification of the permits;

(g) The names and addresses of every officer, partner, director, or person performing a function similar to a director of the applicant, together with the names and addresses of any individual owning of record ten percent (10%) or more of any class of voting stock of the applicant, and whether the applicant or any person is subject to any of the provisions of subsection (3) of KRS 350.130 and he shall so certify. The permittee shall submit updates of this information as changes occur or as otherwise provided by administrative regulation; however, failure to submit updated information shall constitute a violation of this chapter only upon the permittee's refusal or failure to timely submit the information to the cabinet upon request. Upon receipt of updated information satisfactory to the cabinet, the cabinet shall promptly update its computer system containing the information;
(h) A listing of any violations of this chapter, Public Law 95-87, and any law, rule, or regulation in effect for the protection of air or water resources incurred by the applicant in connection with any surface coal mining and reclamation operation during the three (3) year period prior to the date of an application. The list shall indicate the final resolution of the violations; and

(i) Whether the area of land to be affected by the operation has been previously mined and is in compliance with current reclamation standards, and, if not, identify the needed reclamation work.

(4) The application for a permit shall be accompanied by an official document, and an affidavit attesting to the document's authenticity, which will evidence what particular business entity the applicant is, whether a domestic corporation, a partnership, an entity whether a foreign or domestic corporation, a partnership, an entity doing business as another, or, if sole proprietorship, an affidavit so stating.

(5) The application for a permit shall be accompanied by copies, in numbers satisfactory to the cabinet, of a United States Geological Survey topographic map or other map acceptable to the cabinet on which the applicant has indicated the location of the operation, the course which would be taken by drainage from the operation to the stream or streams to which the drainage would normally flow, the name of the applicant and date, and the name of the person who located the operation on the map.

(6) The application for a permit shall be accompanied by copies, in numbers satisfactory to the cabinet, of an enlarged United States Geological Survey topographic map or other map acceptable to the cabinet meeting the requirements of paragraphs (a) to (i) of this subsection. The map shall:

(a) Be prepared and certified by a professional engineer registered under the provisions of KRS Chapter 322. The certification shall be in the form as provided in subsection (8) of this section, except that the engineer shall not be required to certify the true ownership of property under paragraph (d) of this subsection;

(b) Identify the area to correspond with the application;

(c) Show adjacent deep mining;

(d) Show the boundaries of surface properties and names of owners of the affected area and adjacent to any part of the affected area;

(e) Be of a scale of 1:24,000 or larger;

(f) Show the names and locations of all streams, creeks, or other bodies of public water, roads, buildings, cemeteries, oil and gas wells, and utility lines on the area of land affected and within five hundred (500) feet of the area;

(g) Show by appropriate markings the boundaries of the area of land affected, the cropline of the seam or deposit of coal to be mined, and the total number of acres involved in the area of land affected;

(h) Show the date on which the map was prepared, the north point, and the quadrangle name; and

(i) Show the drainage plan on and away from the area of land affected. The plan shall indicate the directional flow of water, constructed drainways, natural waterways used for drainage, and the streams or tributaries receiving the discharge.

(7) Each application shall include a determination of the probable hydrologic consequences of the mining and reclamation operations, both on and off the mine site, with respect to the hydrologic regime, quantity and quality of water in surface and groundwater systems, including the dissolved and suspended solids under seasonal flow conditions, and the collection of sufficient data for the mine site and surrounding areas so
that an assessment can be made by the cabinet of the probable cumulative impacts of all anticipated mining in the area upon the hydrology of the area and particularly upon water availability. This determination shall not be required until the time hydrologic information on the general area prior to mining is made available from an appropriate federal or state agency. The permit shall not be approved until the information is available and is incorporated into the application.

(8) All certifications required by this chapter to be made by professional engineers shall be done in the form prescribed by the cabinet and shall be reasonably specific as to the work being certified. The cabinet may reject any document or map as incomplete if it is not properly certified.

(9) In addition to the information and maps required above, each application for a permit shall be accompanied by detailed plans or proposals showing the method of operation; the manner, time, and distance for backfilling; grading work; and a reclamation plan for the affected area, which proposals shall meet the requirements of this chapter and administrative regulations adopted pursuant thereto.

(10) The application for a permit shall be accompanied by proof that the applicant has public liability insurance coverage satisfactory to the cabinet for the surface mining and reclamation operations for which the permit is sought, or proof that the applicant has satisfied self-insurance requirements as provided by administrative regulations of the cabinet. The coverage shall be maintained in full force and effect during the terms of the permit and any permit renewal, and until reclamation operations are completed.

(11) A basic fee set by administrative regulation, and bearing a reasonable relationship to the cost of processing the permit application but not to exceed three hundred seventy-five dollars ($375), plus a fee set by administrative regulation but not to exceed seventy-five dollars ($75), for each acre or fraction thereof of the area of land to be affected by the operation, shall be paid before the permit required in this section shall be issued; provided that if the cabinet approves an incremental bonding plan submitted by the applicant, the acreage fees may be paid in increments and at times corresponding to the approved plan. The applicant shall file with the cabinet a bond payable to the Commonwealth of Kentucky with surety satisfactory to the cabinet in the sum to be determined by the cabinet for each acre or fraction thereof of the area of land affected, with a minimum bond of ten thousand dollars ($10,000), conditioned upon the faithful performance of the requirements set forth in this chapter and of the administrative regulations of the cabinet. The cabinet shall forfeit the entire amount of the bond for the permit area or increment in the event of forfeiture. In determining the amount of the bond, the cabinet shall take into consideration the character and nature of the overburden; the future suitable use of the land involved; the cost of backfilling, grading, and reclamation to be required; and the probable difficulty of reclamation, giving consideration to such factors as topography, geology, hydrology, and revegetation potential. The bond amount shall initially be computed to be sufficient to assure completion of reclamation if the work had to be performed by the cabinet in the event of forfeiture. The cabinet shall promulgate administrative regulations setting forth bonding requirements including, but not limited to, requirements for the amount, duration, release, and forfeiture of bonds.

(12) Surface coal mining and reclamation operations which affected two (2) acres or less, as defined by administrative regulations of the cabinet, which were conducted pursuant to two (2)-acre-or-less permits issued...
by the cabinet, which were commenced on or before June 5, 1987, and on which mining ceased on or before November 7, 1987, shall be exempt from the requirements of this chapter, except as follows. Reclamation of the operations shall be accomplished in accordance with administrative regulations promulgated by the cabinet for operations of two (2) acres or less. The cabinet shall not require that the highwalls left by the operations be eliminated. Bond shall be maintained until reclamation is successfully completed. All procedural provisions and the penalty provisions of KRS 350.990 shall apply to operations conducted pursuant to this subsection. The cabinet shall enforce this subsection consistent with this chapter, except that the cabinet shall not issue orders requiring cessation of operations for mere failure to abate a violation.

(13) The cabinet shall promulgate administrative regulations for the permitting of operations with surface effects of underground mining and other surface coal mining and reclamation operations consistent with this section. The cabinet shall recognize the distinct differences between the surface effects of underground mining and strip mining, as also provided in KRS 350.151, in promulgating permitting requirements for these operations; provided, that the cabinet shall require that all the areas overlying underground workings be permitted but that the areas overlying underground workings not affected by operations and facilities occurring on the surface shall not be subject to the payment of acreage fees or bond requirements of subsection (11) of this section, KRS 350.070, or KRS 350.151.

(14) Any valid permit issued pursuant to this chapter shall carry with it the right of successive renewal upon expiration with respect to areas within the boundaries of the existing permit. An applicant for renewal of a permit shall pay a basic fee set by regulation, not to exceed three hundred seventy-five dollars ($375). The holders of the permit may apply for renewal and the renewal shall be issued, provided that on application for renewal the burden shall be on the applicant to establish that the terms and conditions of the existing permit are being satisfactorily met; the present surface coal mining and reclamation operation is not in compliance with the environmental protection standards of this chapter; the renewal requested substantially jeopardizes the applicant’s continuing responsibility on existing permit areas; the applicant has not provided evidence that the performance bond in effect for the operation will continue in full force and effect for any renewal requested in the application as well as any additional bond the cabinet might require; or any additional revised or updated information required by the cabinet has not been provided. Prior to the approval of any renewal of permit, the cabinet shall provide notice to the appropriate public authorities.

(15) If an application for renewal of a valid permit includes a proposal to extend the mining operation beyond the boundaries authorized in the existing permit, the portion of the application for renewal of a valid permit which addresses any new areas of surface disturbance shall be subject to the full standards applicable to new applications under this chapter.

(16) Any permit renewal shall be for a term not to exceed the period of the original permit. Application for permit renewal shall be made at least
one hundred twenty (120) days prior to the expiration of the valid
permit. However, if a permit has expired or if a permit renewal
application has not been timely filed, and the operator or permittee
desires to continue the surface coal mining operation, the cabinet shall
forthwith cause a notice of noncompliance to be issued. The notice of
noncompliance shall be deemed to have been complied with, and the
permit may be renewed, if the cabinet receives a permit renewal
application within thirty (30) days of the receipt of the notice of
noncompliance. Upon the submittal of a permit renewal application, the
operator or permittee shall be deemed to have timely filed the permit
renewal application and shall be entitled to continue, under the terms
of the expired permit, the surface coal mining operation, pending the
issuance of the permit renewal. Failure to comply with the remedial
measures of the notice of noncompliance shall result in the cessation of
the surface coal mining operation.

(17) Notwithstanding any of the provisions of this section, a permit shall
terminate if the permittee has not commenced the surface coal mining
operations covered by the permit within three (3) years of the issuance
of the permit. However, the cabinet may grant reasonable extensions of
time upon a showing that the extensions are necessary by reason of
litigation precluding commencement of operations, or threatening
substantial economic loss to the permittee, or by reason of conditions
beyond the control and without the fault or negligence of the permittee.
With respect to coal to be mined for use in a synthetic fuel facility or
specific major electric generating facility, the permittee shall be deemed
to have commenced surface mining operations at the time the construc-
tion of the synthetic fuel or generating facility is initiated.

(18) Each application for a permit or revision for auger mining on a
previously mined area shall contain information to describe the area to
be affected, to show that the proposed method of operation will result in
stable post-mining conditions, and reduce or eliminate adverse environ-
mental conditions created by previous mining activities. If the cabinet
determines that the affected area cannot be stabilized and reclaimed
subsequent to augering or that the operation will result in an adverse
impact to the proposed or adjacent area, the permit or revision shall not
be issued. The cabinet shall, consistent with all applicable require-
ments of this chapter, issue a permit or revision if the applicant
demonstrates that the proposed coal mining operations will provide for
reduction or elimination of the highwall, or reduction or abatement of
adverse impacts resulting from past mining activities, or stabilization
or enhancement of a previously mined area. The cabinet shall insure
that all reasonably available spoil material will be used to backfill the
highwall to the extent practical and feasible; provided, however, that in
all cases the holes be properly sealed and backfilled to a minimum of
four (4) feet above the coal seam being mined.

(19) All operations involving the loading of coal which do not separate the
coal from its impurities, and which are not located at or near the mine
site, shall be exempt from the requirements of this chapter.

ch. 143, § 4; 1962, ch. 105, § 4; 1964, ch. 61, § 3; 1966, ch. 4, § 7; 1972, ch.
270, § 3; 1972 (1st Ex. Sess.), ch. 3, § 65; 1974, ch. 69, § 1; 1974, ch. 74, Art.
III, § 13(7); 1974, ch. 258, § 1; 1974, ch. 373, § 2; 1976, ch. 291, § 1; 1978,
ch. 330, § 23, effective May 3, 1978; 1978, ch. 322, § 4, effective June 17,
March 21, 1980; 1982, ch. 266, § 10, effective July 15, 1982; 1982, ch. 283,
§ 3, effective April 2, 1982; 1984, ch. 111, § 144, effective July 13, 1984;
1984, ch. 145, § 2, effective March 28, 1984; 1984, ch. 358, § 1, effective July
6. Cabinet's Jurisdiction.
   The Cabinet's jurisdiction to order mining company to reclaim permitted sites did not expire on the dates when its mining permits expire, for although the right to mine may expire, both the obligation to reclaim the permit site and the Cabinet's enforcement jurisdiction continue until such time as the required reclamation is complete. Natural Resources & Envtl. Protection Cabinet v. Whitley Dev. Corp., 940 S.W.2d 904 (Ky. Ct. App. 1997).

350.064. Reclamation bond to be filed by applicant.


350.090. Method of operation, grading, backfilling, and reclamation plans — Funding from reclamation development fund — Waste materials in permit area only.


NOTES TO DECISIONS

3. Remedies Not Mutually Exclusive.
   The remedy of bond forfeiture and the remedy of ordering a permittee to reclaim a site are not mutually exclusive; nothing in the statutes providing for forfeiture of bond if a reclamation violation is not abated, that authorize the cabinet to order that a permittee undertake certain abatement obligations or that authorize the cabinet to seek injunctive relief suggest that these remedies are intended to be mutually exclusive; on the contrary the cabinet's ability to seek remedies of both bond forfeiture and injunctive relief afford it protection in those cases in which the amount of the bond is inadequate to pay for the cost of completing reclamation. Natural Resources & Envtl. Protection Cabinet v. Whitley Dev. Corp., 940 S.W.2d 904 (Ky. Ct. App. 1997).

350.131. Use of forfeited reclamation bond funds — Contract to reclaim overlapped disturbed area for which bond has been forfeited and collected.

(1) When a bond for an interim or preinterim program permit was forfeited prior to July 15, 1988, by the cabinet, and the entire forfeited amount is not necessary to establish proper drainage and revegetation on the permit area for which it was submitted, the cabinet may use any
CHAPTER 10
BOND AND INSURANCE REQUIREMENTS
001. Definitions for 405 KAR Chapter 10.
010. General requirements for performance bond and liability insurance.
020. Amount and duration of performance bond.
030. Types, terms and conditions of performance bonds and liability insurance.
035. Procedures, criteria and hearing requirements for cancellation of surety bonds after notice of noncompliance issued for failure to maintain contemporaneous reclamation.
040. Procedures, criteria and schedule for release of performance bond.
050. Bond forfeiture.
060. Kentucky bond pool.

405 KAR 10:001. Definitions for 405 KAR Chapter 10.
NECESSITY, FUNCTION, AND CONFORMITY: KRS Chapter 350 in pertinent part requires the cabinet to promulgate rules and administrative regulations pertaining to surface coal mining and reclamation operations under the permanent regulatory program. This administrative regulation provides for the defining of certain essential terms used in 405 KAR Chapter 10.

Section 1. Definitions. (1) "Adjacent area" means land located outside the affected area or permit area, depending on the context in which "adjacent area" is used, where air, surface or groundwater, fish, wildlife, vegetation or other resources protected by KRS Chapter 350 may be adversely impacted by surface coal mining and reclamation operations.

(2) "Administrator" or "bond pool administrator", as used in 405 KAR 10:200, means the cabinet employee named by the secretary to assist the commission and to perform certain administrative functions in connection with the bond pool, as required by KRS 350.715.

(3) "Affected area" means any land or water area which is used to facilitate, or is physically altered by, surface coal mining and reclamation operations. The affected area includes the disturbed area; any area upon which surface coal mining and reclamation operations are conducted; any adjacent lands the use of which is incidental to surface coal mining and reclamation operations; all areas covered by new or existing roads used to gain access to, or for hauling coal to or from, surface coal mining and reclamation operations, except as provided in this definition; any area covered by surface excavations, workings, impoundments, dams, ventilation shafts, entryways, refuse banks, dumps, stockpiles, overburden piles, spoil banks, culm banks, tailings, holes or depressions, repair areas, storage areas, shipping areas; any areas upon which are sited structures, facilities, or other property or material on the surface resulting from, or incident to, surface coal mining and reclamation operations; and the area located above underground workings associated with underground mining activities, auger mining, or in situ mining. The affected area shall include every road used for the purposes of access to, or for hauling coal to or from, surface coal mining and reclamation operations, unless the road:

(a) Was designated as a public road pursuant to the laws of the jurisdiction in which it is located;

(b) Is maintained with public funds, and constructed in a manner similar to other public roads of the same classification within the jurisdiction; and

(c) There is substantial (more than incidental) public use.

(4) "Applicant", as used in 405 KAR 10:010, means any person seeking a permit, permit revision, permit amendment, permit renewal, or transfer, assignment, or sale of permit rights from the cabinet to conduct surface coal mining and reclamation operations pursuant to KRS Chapter 350 and all applicable administrative regulations.

(5) "Bond" or "Kentucky Bond Pool" means the voluntary alternative bonding program established at KRS 350.700 through 350.755.

(6) "Cabinet" is defined in KRS 350.010.

(7) "CFR" means Code of Federal Regulations.

(8) "Coal" means combustible carbonaceous rock, classified as anthracite, bituminous, subbituminous, or lignite by ASTM Standard D 388-77.

(9) "Collateral bond" means an indemnity agreement in a sum certain payable to the cabinet executed by the permittee and which is supported by the deposit with the cabinet of cash, negotiable certificates of deposit, or an irrevocable letter of credit of any bank organized and authorized to transact business in the United States.

(10) "Commission" or "bond pool commission" means the body established at KRS 350.705.

(11) "Cropland" means land used for the production of adapted crops for harvest, alone or in a rotation with grasses and legumes, and includes row crops, small grain crops, hay crops, nursery crops, orchard crops, and other similar specialty crops.

(12) "Day" means calendar day unless otherwise specified to be a working day.

(13) "Department" means the Department for Surface Mining Reclamation and Enforcement.

(14) "Disturbed area" means an area where vegetation, topsoil, or overburden is removed or upon which topsoil, spoil, coal processing waste, underground development waste, or noncoal waste is placed by surface coal mining operations. Those areas are classified as "disturbed" until reclamation is complete and the performance bond or other assurance of performance required by 405 KAR Chapter 10 is released.

(15) "FDIC" means Federal Deposit Insurance Corporation.

(16) "Federal lands" means any lands, including mineral interests, owned by the United States, without regard to how the United States acquired ownership of the lands or which agency manages the lands. It does not include Indian lands.

(17) "FSLIC" means Federal Savings and Loan Insurance Corporation.

(18) "Historically used for cropland." (a) "Historically used for cropland" means that lands have been used for cropland for any five (5) years or more out of the ten (10) years immediately preceding:

1. The application; or

2. The acquisition of the land for the purpose of conducting surface coal mining and reclamation operations.

(b) Lands meeting either paragraph (a)1 or 2 of this subsection shall be considered "historically used for cropland.

(c) In addition to the lands covered by paragraph (a) of this subsection, other lands shall be considered "historically used for cropland" as described below:

1. Lands that would likely have been used as cropland for any five (5) out of the last ten (10) years immediately preceding the acquisition or the application but for some fact of ownership or control of the land unrelated to the productivity of the land; and

2. Lands that the cabinet determines, on the basis of additional cropland history of the surrounding lands and the lands under consideration, are clearly cropland but fail outside the specific five (5) years in ten (10) criterion.

(d) Acquisition includes purchase, lease, or option of the land for the purpose of conducting or allowing through resale, lease or option, the conduct of surface coal mining and reclamation operations.

(19) "Impoundment" means a closed basin, naturally formed or artificially built, which is dammed or excavated for the retention of water, sediment, or waste.

(20) "KAR" means Kentucky administrative regulations.

(21) "KRS" means Kentucky Revised Statutes.

(22) "Land use" means specific functions, uses, or management-related activities of an area, and may be identified in combination when joint or seasonal uses occur and may include land used for support facilities that are an integral part of the use. In some instances, a specific use can be identified without active management.

(23) "Month of operation," as used in 405 KAR 10:200, Section 7, means a calendar month in which a duty exists to reclaim a disturbed area for which a permit was issued under KRS Chapter 350. It is not necessary that coal extraction occur during the month.

(24) "Notice of noncompliance and order for remedial measures" means a written document and order prepared by an authorized rep-

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responsible of the cabinet which sets forth with specificity the violations of KRS Chapter 350, 405 KAR Chapters 7 through 24, or permit conditions which the authorized representative of the cabinet determines to have occurred based upon his inspection, and the necessary remedial actions, if any, and the time schedule for completion thereof, which the authorized representative deems necessary and appropriate to correct the violations.

(25) "Operations" is defined in KRS 350.010.

(26) "Operator" is defined in KRS 350.010.

(27) "Order for cessation and immediate compliance" means a written document and order issued by an authorized representative of the cabinet when:
(a) A person to whom a notice of noncompliance and order for remedial measures was issued has failed, as determined by a cabinet inspection, to comply with the terms of the notice of noncompliance and order for remedial measures within the time limits set therein, or as subsequently extended; or
(b) The authorized representative finds, on the basis of a cabinet inspection, any condition or practice or any violation of KRS Chapter 350, 405 KAR Chapters 7 through 24, or any condition of a permit or exploration approval which:
1. Creates an imminent danger to the health or safety of the public, or
2. Is causing or can reasonably be expected to cause significant, imminent environmental harm to land, air or water resources.

(28) "Owned or controlled" and "owns or controls" mean any one (1) or a combination of the relationships specified in paragraphs (a) and (b) of this definition:
(a) 1. Being an owner of a surface coal mining operation;
2. Based on instruments of ownership or voting securities, owning of record in excess of fifty (50) percent of an entity; or
3. Having any other relationship that gives one (1) person authority directly or indirectly to determine the manner in which an applicant, an operator, or any other entity conducts surface coal mining operations.
(b) The following relationships are presumed to constitute ownership or control unless a person can demonstrate that the person subject to the presumption does not in fact have the authority directly or indirectly to determine the manner in which the relevant surface coal mining operation is conducted:
1. Being an officer or director of an entity;
2. Being the operator of a surface coal mining operation;
3. Having the ability to commit the financial or real property assets or working resources of an entity;
4. Being a general partner in a partnership;
5. Based on the instruments of ownership or the voting securities of a corporate entity, owning of record ten (10) through fifty (50) percent of the entity; or
6. Owning or controlling coal to be mined by another person under a lease, sublease, or other contract and having the right to receive the coal after mining or having authority to determine the manner in which that person or another person conducts a surface coal mining operation.

(29) "Performance bond" means a surety bond, a collateral bond, or a combination thereof, or bonds filed pursuant to the provisions of the Kentucky Bond Pool Program (405 KAR 10:200, KRS 350.595, and KRS 350.700 through 350.755), by which a permittee or applicant is required to conduct surface coal mining and reclamation operations under that permit.

(30) "Permit" means written approval issued by the cabinet to conduct surface coal mining and reclamation operations.

(31) "Permit area" means the area of land and water within boundaries designated in the approved permit application, which shall include, at a minimum, all areas which are or will be affected by surface coal mining and reclamation operations under that permit.

(32) "Permittee" means an operator or a person holding or required by KRS Chapter 350 or 405 KAR Chapters 7 through 24 to hold a permit to conduct surface coal mining and reclamation operations during the permit term and until all reclamation obligations imposed by KRS Chapter 350 and 405 KAR Chapters 7 through 24 are satisfied.

(33) "Person" is defined in KRS 350.010.

(34) "Person having an interest which is or may be adversely affected" or "person with a valid legal interest" shall include any person:
(a) Who uses any resource of economic, recreational, aesthetic, or environmental value that may be adversely affected by coal exploration or surface coal mining and reclamation operations, or by any related action of the cabinet; or
(b) Whose property is or may be adversely affected by coal exploration or surface coal mining and reclamation operations, or by any related action of the cabinet.

(35) "Prime farmland" means those lands which are defined by the Secretary of Agriculture in 7 CFR 657 and which have been "historically used for cropland" as that phrase is defined above.

(36) "Reclamation" is defined in KRS 350.010.

(37) "Secretary" is defined in KRS 350.010.

(38) "SMCRA" means Surface Mining Control and Reclamation Act of 1977 (PL 95-87), as amended.

(39) "Surety bond" means an indemnity agreement in a sum certain, payable to the cabinet and executed by the permittee, which is supported by the performance guarantee of a corporation licensed to do business as a surety in the Commonwealth of Kentucky.

(40) "Surface coal mining and reclamation operations" is defined in KRS 350.010.

(41) "Surface coal mining operations" is defined in KRS 350.010.

(42) "Suspended solids" or nonfilterable residue, expressed as milligrams per liter, means organic and inorganic materials carried or held in suspension in water which are retained by a standard glass fiber filter in the procedure outlined by the U.S. EPA's regulations for waste water and analyses (40 CFR 136).

(43) "Ton" means 2000 pounds avoirdupois (.90718 metric ton).

(44) "Topsoil" means the A and E soil horizon layers of the four (4) major soil horizons.

(45) "U.S. EPA" means United States Environmental Protection Agency.

(46) "Willfully" and "willful violation" mean that a person acted either intentionally, voluntarily, or conclusively, and with intentional disregard or plain indifference to legal requirements, in authorizing, ordering, or carrying out an act or omission that constituted a violation of SMCRA, KRS Chapter 350, 405 KAR Chapters 7 through 24, or a permit condition, or that constituted a failure or refusal to comply with an order issued pursuant to SMCRA, KRS Chapter 350, or 405 KAR Chapters 7 through 24. (18 Ky.R. 2468; Am. 2842; eff. 4-3-92.)

405 KAR 10:010. General requirements for performance bond and liability insurance.

RELATES TO: KRS 350.020, 350.060, 350.062, 350.064, 350.151, 350.465, 30 CFR Parts 730-733, 735, 800.11, 800.60, 917, 30 USC 1253, 1255


NECESSITY, FUNCTION, AND CONFORMITY: KRS 350.028(1), (5), 350.151(1), and 350.465(2) authorize the cabinet to promulgate administrative regulations relating to surface and underground coal mining operations. This administrative regulation establishes the requirements for filing and maintaining performance bonds and liability insurance, and bonding methods.

Section 1. Applicability. This chapter sets forth the minimum requirements for filing and maintaining performance bonds and assurance for surface coal mining and reclamation operations under KRS Chapter 350.

Section 2. Requirement to File a Bond. (1) An applicant shall not disturb surface acreage or extend any underground shafts, tunnels, or operations prior to receipt of approval from the cabinet of a performance bond covering areas to be affected by surface operations and facings.

(2) After an application for a new, amended, revised or renewed permit to conduct surface coal mining and reclamation operations has been approved under 405 KAR Chapter 8, but before the permit is issued, the applicant shall file with the cabinet, on a form prescribed and furnished by the cabinet, a performance bond payable to the cabinet. The applicant shall file the form designated at Section 5(1)(g) of this administrative regulation for operations on lands other than
TITLE 405, CHAPTER 10 - BOND AND INSURANCE REQUIREMENTS

Section 1. Determination of Bond Amount. The standard applied by the cabinet in determining the amount of performance bond shall be the estimated cost to the cabinet if it had to perform the reclamation, restoration, and abatement work required of a person who conducts surface coal mining and reclamation operations under KRS Chapter 350, 405 KAR Chapters 7 through 24 and the permit. This amount shall be based on, but not limited to:

(1) The estimated costs submitted by the permittee in accordance with 405 KAR 8:030, Section 24(4) and 405 KAR 8:040, Section 24(4);

(2) The additional estimated costs to the cabinet which may arise from applicable public contracting requirements or the need to bring personnel and equipment to the permit area after its abandonment by the permittee to perform reclamation, restoration, and abatement work.

(3) All additional estimated costs necessary, expedient, and inci-
TITLE 405, CHAPTER 10 - BOND AND INSURANCE REQUIREMENTS

Section 2. Minimum Bond Amount. The minimum amount of the bond for surface coal mining and reclamation operations at the time the permit is issued or amended shall be $10,000 for the entire area under one (1) permit.

Section 3. Period of Liability. (1) Liability under performance bond(s) applicable to an entire permit area or increment thereof shall continue until all reclamation, restoration and abatement work required of persons who conduct surface coal mining and reclamation operations under requirements of KRS Chapter 350, 405 KAR Chapters 7 through 24 and the provisions of the permit have been completed, and the permit or increment terminated by release of the permittee from any further liability in accordance with 405 KAR 10:040.

(2) In addition to the period necessary to achieve compliance with all requirements of KRS Chapter 350, 405 KAR Chapters 7 through 24 and the permit including the standards for the success of revegetation as required by 405 KAR 16:200 and 405 KAR 18:200, the period of liability under performance bond shall continue for a period of five (5) years after the last year of augmented seeding, fertilizing, irrigation or other work. The period of liability shall begin again whenever augmented seeding, fertilizing, irrigation or other work is required or conducted on the site prior to bond release. Isolated and clearly defined portions of a bonded area requiring extended liability because of augmentation may be separated from the original area and bonded separately upon approval by the cabinet. Such areas shall be limited in extent, and not constitute a scattered, intermittent, or checkerboard pattern of failure. Access to the separated areas for remedial work may be included in the area under extended liability if deemed necessary by the cabinet.

(3) If the cabinet approves a long-term intensive agricultural post-mining land use in accordance with 405 KAR 15:210, augmented seeding, fertilization, irrigation or other husbandry practices normally associated with the approved postmining land use shall not require restarting the five (5) year period of liability.

(4) The bond liability of the permittee shall include only those actions which the permittee is required to take under the permit, including completion of the reclamation plan in such a manner that the land will be capable of supporting a postmining land use approved under 405 KAR 16:210. Actions of third parties which are beyond the control and influence of the permittee and for which the permittee is not responsible under the permit shall not be covered by the bond.

Section 4. Adjustment of Amount. (1) The amount of the performance bond liability applicable to a permit or increment shall be adjusted by the cabinet:

(a) When the acreage in the permit area or increment is either increased or decreased;

(b) When the cabinet determines that the cost of future reclamation, restoration or abatement has changed. When it is determined that an adjustment under this paragraph is necessary, the cabinet shall:

1. Notify the permittee, the surety, and any person with a property interest in collateral who has previously requested such notification in writing;

2. Provide the permittee an opportunity for an informal conference on the adjustment. The requirements of 405 KAR 7:091 and 405 KAR 7:092 shall not apply to the conduct of the conference.

(2) The cabinet shall assess reduction due to such deletion of acreage which is not affected by the surface coal mining and reclamation operation. The provisions of 405 KAR 10:040, Section 2(3) shall apply. however, a reduction due to such deletion of acreage shall not constitute a bond release and shall not be subject to the procedures of 405 KAR 10:040, Section 1.

(3) The cabinet may grant reduction of the required performance bond amount if the permittee’s method of operation or other circumstances will reduce the maximum estimated cost to the cabinet to complete the reclamation responsibilities and therefore warrant a reduction of the bond amount. The request shall not be considered as a request for partial bond release subject to the procedures of 405 KAR 10:040, Section 1.

(4) The cabinet shall refuse to approve any reduction of the performance bond liability amount if an action for revocation or suspension of the permit covered by the bond is pending, if there is a pending action for forfeiture of the bond, or if the permittee is currently in violation of 405 KAR on that permit. (8 Ky.R. 1417; eff. 1-6-83; Am. 15 Ky.R. 441; eff. 12-13-88.)

405 KAR 10:030. Types, terms and conditions of performance bonds and liability insurance.

RELATES TO: KRS 350.020, 350.060, 350.064, 350.100, 350.110, 350.465


NECESSITY, FUNCTION, AND CONFORMITY: KRS Chapter 350 in pertinent part requires the cabinet to specify types, terms, and conditions for performance bonds and liability insurance. This administrative regulation sets forth the various types and conditions which the cabinet will accept in satisfaction of the bonding requirements. This administrative regulation sets forth that bonds shall be payable to the cabinet and other conditions. This administrative regulation specifies certain alternative types of bonds, in addition to the surety bond, and the conditions upon which the cabinet will accept them. This administrative regulation specifies the terms and conditions of liability insurance.

Section 1. Types of Performance Bond. (1) The cabinet shall approve performance bonds of only those types which are set forth in this section.

(2) The performance bond shall be either:

(a) A surety bond;

(b) A collateral bond;

(c) A combination of the above bonding types;

(d) Bonds filed pursuant to the provisions of the Kentucky Bond Pool Program (405 KAR 10:200, KRS 350.595, and 350.700 through 350.755).

Section 2. Terms and Conditions of Performance Bond. (1) The performance bond shall be in an amount determined by the cabinet as provided in 405 KAR 10:020, Sections 1 and 2.

(2) The performance bond shall be payable to the cabinet.

(3) The performance bond shall be conditioned upon faithful performance of all of the requirements of KRS Chapter 350, 405 KAR Chapters 7 through 24 and the conditions of the permit and shall cover the entire permit area or such incremental area as the cabinet has approved pursuant to 405 KAR 10:010, Section 3(2).

(4) The duration of the bond shall be for a time period provided in 405 KAR 10:020, Section 3.

(5) Surety bonds shall be subject to the following conditions:

(a) The cabinet shall not accept the bond of a surety company unless the bond shall not be cancelable by the surety at any time for any reason including, but not limited to, nonpayment of premium or bankruptcy of the surety during the period of liability. Surety bond coverage for permitted lands not disturbed may be cancelled with the written approval of the cabinet, provided the surety gives written notice to both the permittee and the cabinet of the intent to cancel prior to the proposed cancellation. Such notice shall be by certified mail. Cancellation shall not be effective for lands subject to bond coverage which are affected after receipt of notice, but prior to approval by the cabinet. The cabinet may approve such cancellation only if a replacement bond has been filed by the permittee, or if the permit area has been reduced by revision to the extent that the remaining bond amount, after cancellation, is sufficient to cover all the costs attributable to the completion of reclamation operations on the reduced permit area in accordance with 405 KAR 10:020. The cabinet shall advise the surety, within thirty (30) days after receipt of a notice to cancel bond, whether
the bond may be cancelled on an undisturbed area.

(b) The bond shall provide that the surety and the permittee shall be jointly and severally liable.

(2) The issuer of any notice shall give prompt notice to the permittee and the cabinet of any notice received or action filed alleging the insolvency or bankruptcy of the surety, or alleging any violations of regulatory requirements which could result in suspension or revocation of the surety's license to do business.

2. In the event the surety becomes unable to fulfill its obligations under the bond for any reason, the surety shall promptly provide written notice to the permittee and the cabinet.

3. Upon the incapacity of a surety by reason of bankruptcy, insolvency, or suspension or revocation of its license or certificate of authority, the permittee shall be deemed to be without proper performance bond coverage and shall promptly notify the cabinet. However, nothing herein shall relieve the permittee of responsibility under the permit if the issue of liability on the letter of credit does not exceed ninety (90) days. An adequate bond is not posted by the end of the period allowed, the permittee shall cease coal extraction and coal processing operations and shall comply with the provisions of 405 KAR 16:010, Section 6 or 405 KAR 18:010, Section 4 and shall immediately begin to conduct reclamation operations in accordance with the reclamation plan. Coal extraction and coal processing operations shall not resume until the permit has been posted. If an acceptable bond has not been posted by the end of the period allowed, the cabinet may suspend the permit until an acceptable bond is posted.

(8) When a permittee chooses to combine two (2) or more bonds for one (1) permit area or increment, the bonds may be accompanied by a schedule, acceptable to the cabinet and agreed to be all parties, which sets forth the agreed distribution of bond amounts to be released or reduced under 405 KAR 10:040 and 405 KAR 10:020, Section 2, respectively. If a schedule is submitted, the cabinet may release equal percentages of each bond.

Section 3. Substitution of Bonds. (1) The cabinet may allow permittees to substitute existing surety or collateral bonds for equivalent surety or collateral bonds, if the liability which has accrued against the permittee on the permit area or increment is transferred to such substitute bonds.

(2) The cabinet shall not release existing performance bonds until the permittee has submitted and the cabinet has approved acceptable substitute performance bonds. A substitution of performance bonds pursuant to this section shall not constitute a release of bond under 405 KAR 10:040.

(3) The cabinet may refuse to allow substitution of bonds if an action for revocation or suspension of the permit covered by the bond is pending or if there is a pending action for forfeiture of the bond.

Section 4. Terms and Conditions for Liability Insurance. (1) The applicant shall submit, as a part of the permit application at the time of bond submission, a certificate issued by an insurance company authorized to do business in Kentucky certifying that the applicant has a public liability insurance policy in force for the surface coal mining and reclamation operations for which the permit is sought. The certificate shall be on a form prescribed by the cabinet. The policy shall provide for personal injury and property damage protection in an amount adequate to compensate for all personal injury and property damage resulting from surface coal mining and reclamation operations, including damage caused by the use of explosives and damage to water wells. Minimum insurance coverage for bodily injury and property damage shall be $300,000 for each occurrence and $500,000 aggregate.

(2) The policy shall be maintained in full force during the term of the permit or any renewal thereof, and during the liability period necessary to complete all reclamation operations under 405 KAR Chapters 7 through 24, until full bond release has been granted.

(3) The policy shall include a clause requiring that the insurer notify the cabinet whenever substantive changes are made in the policy, including any termination or failure to renew.

(4) In the event the insurer becomes unable to fulfill its obligations under the policy, notice shall be given immediately to the permittee and the cabinet.

(5) Upon the incapacity of an insurer by reason of bankruptcy, insolvency, or suspension or revocation of its license or certificate of authority, the permittee shall be deemed to be without insurance coverage and shall promptly notify the cabinet. However, nothing herein shall relieve the insurer of liability on its policy. The cabinet shall issue a notice to the permittee specifying a reasonable period to replace such coverage, not to exceed ninety (90) days. If an adequate insurance coverage is not posted by the end of the period allowed, the permittee shall cease coal extraction and coal processing operations and shall comply with the provisions of 405 KAR 16:010, Section 6 or 405 KAR 18:010, Section 4 and shall immediately begin to conduct reclamation operations in accordance with the reclamation plan. Coal extraction and coal processing operations shall not resume until the permit has been posted. If an acceptable bond has not been posted by the end of the period allowed, the cabinet may suspend the permit until an acceptable bond is posted.
cabinet has determined that an acceptable insurance coverage has been posted. If an acceptable insurance coverage has not been posted by the end of the period allowed, the cabinet may suspend the permit until acceptable insurance coverage is posted. (8 Ky.R. 1518; eff. 1-6-83; Am. 12 Ky.R. 579; eff. 12-10-85; 15 Ky.R. 443; 1070; eff. 12-13-88.)

405 KAR 10:035. Procedures, criteria and hearing requirements for cancellation of surety bonds after notice of noncompliance issued for failure to maintain contemporaneous reclamation.


NECESSITY, FUNCTION, AND CONFORMITY: KRS Chapter 350 in pertinent part provides authority for the cabinet to approve the cancellation of surety bonds upon notice by the surety when a notice of noncompliance is issued for failure to maintain contemporaneous reclamation. This administrative regulation specifies the procedures and criteria for surety bond cancellation. This administrative regulation also sets forth certain notice and hearing requirements relating to surety bond cancellation.

Section 1. Procedures for Request for and Notice of Surety Bond Cancellation. (1) Notice of intent to cancel.

(a) After the issuance, on or after July 13, 1984, of a notice of noncompliance for failure to maintain contemporaneous reclamation, the surety obligated on the performance bond for the permit or any increment thereof may send notice to the insured and to the department, of its intent to request cancellation of bond coverage on any area disturbed after thirty (30) days from the effective date of the surety's notice of intent to cancel, if the violation is not abated.

(b) The notice of intent to cancel shall be sent by certified mail, return receipt requested, to the insured, and a copy to the Director of the Division of Field Services, of the department. The effective date of the notice of intent to cancel shall be the date on which it is received by the insured or seven (7) days after mailing of the notice by certified mail, return receipt requested, to the address contained on the permit application and any other address known to the insurer, whichever occurs first.

(c) The notice of intent to cancel shall be signed by an officer, director, or attorney-in-fact of the surety company and contain at a minimum the following:
1. Name of permittee;
2. Permit number and increment number, if applicable;
3. Name of surety;
4. Bond number and amount;
5. Date of issuance of notice of noncompliance and noncompliance number;
6. Date of notice of intent to cancel; and
7. A copy of a power-of-attorney, if applicable.

(2) Notice of cancellation.

(a) If the surety elects to cancel pursuant to its notice of intent to cancel, the surety shall send a notice of cancellation to the insured by certified mail, return receipt requested. A copy of said notice shall also be sent to the Director of the Division of Field Services by certified mail, return receipt requested.

(b) The notice of cancellation shall be on a form specified by the cabinet and shall be sworn to by an officer, director or attorney-in-fact of the surety, notarized and contain at a minimum the following:
1. Name of permittee and permit number;
2. Increment number, if applicable;
3. Name of surety and bond number;
4. Date of issuance of notice of noncompliance and noncompliance number;
5. Date the notice of intent to cancel was received by permittee;
6. Date of notice of cancellation;
7. A statement that the violation has not been abated within thirty (30) days of the effective date of the notice of intent to cancel;
8. A statement that the surety acknowledges that it will not be relieved of its liability for areas disturbed prior to the department's approval of cancellation;
9. A request for the cabinet to approve the notice of cancellation; and
10. A copy of a power-of-attorney, if applicable.

(c) The notice of cancellation shall become effective upon the cabinet's approval.

(3) Cabinet approval of cancellation. Within thirty (30) days of receipt of the notice of cancellation, the cabinet shall approve the surety's notice of cancellation in writing, only if the following conditions exist:

(a) The violation has not been abated by the permittee; and
(b) The surety has complied with the notice requirements of subsection (1) and (2) of this section; and

(c) The cabinet has:
1. Revoked the permit by order of the commissioner of the department; or
2. Deleted the area subject to the cancellation by order of the commissioner of the department; or
3. Accepted and approved a substitute bond submitted by the permittee.

Section 2. Procedures for Permit Revocation or Deletion of the Areas Subject to Cancellation. The cabinet shall by order delete the areas subject to bond cancellation or revoke the permit for the entire permit area within thirty (30) days from receipt of the surety's notice of cancellation, without prior hearing, unless an acceptable substitute bond has been submitted to the cabinet.

(1) The order shall be issued by the commissioner of the department, without prior hearing, based upon information available to the cabinet and the surety's notice of cancellation.

(2) The permittee may request a hearing on the order of the commissioner pursuant to KRS 224.081(2).

(a) A hearing requested pursuant to KRS 224.081(2) shall be requested within thirty (30) days of entry of the order of the commissioner.

(b) The order of the commissioner shall be affirmed unless the permittee can affirmatively establish that bond coverage was not cancelled and the violation was abated at the time of entry of the commissioner's order, or that substitute bond was approved by the cabinet.

(c) Within thirty (30) days after entry of the order of the commissioner, the order may be rescinded if the permittee can demonstrate that a substitute bond has been accepted and approved by the cabinet and the violations have been abated.

Section 3. Procedures for Bond Release or Forfeiture After Approval of Cancellation. (1) The cabinet shall not release any portion of a bond for a permit area or increment thereof, including but not limited to undisturbed acreage, after cancellation, unless and until all disturbed areas on the permit or increment have been reclaimed in accordance with the standards set forth in KRS Chapter 350 and the administrative regulations promulgated pursuant thereto, or substitute bond has been filed and approved by the cabinet and the substitute surety has expressly assumed liability for all disturbed areas of the permit or increment.

(2) In the event of bond forfeiture the entire bond held by the cabinet shall be forfeited upon order of the secretary pursuant to KRS Chapter 350 and the administrative regulations pursuant thereto. (11 Ky.R. 331; Am. 577; eff. 10-9-84.)


NECESSITY, FUNCTION, AND CONFORMITY: KRS Chapter 350 in pertinent part requires the cabinet to set out by regulation procedures and criteria for the release of performance bond. This administrative regulation specifies the procedures, criteria, and schedule, including reclamation phases, for the release and partial release of liability under performance bonds. This administrative regulation also

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sets forth certain notice and hearing requirements pertinent to bond release.

Section 1. Procedures for Release of Performance Bond. (1) Application for bond release. The permittee or any person authorized to act on his or her behalf may or the cabinet shall, initiate an application for release of all or part of the performance bond liability applicable to a permit or an increment after the bond has been scheduled for a hearing and the abatement work in a reclamation phase as defined in Section 2(4) of this administrative regulation has been completed on the entire permit area or increment.

(a) Bond release applications may only be filed at times or seasons that allow the cabinet to evaluate properly the reclamation operations alleged to have been completed.

(b) Within thirty (30) days of the initiation of any bond release request, the permittee shall submit copies of letters which it has sent to adjoining property owners, surface owners (their agents and lessees), local governmental bodies, planning agencies, sewage and water treatment authorities, and water companies in the locality in which the surface coal mining and reclamation operation took place, notifying them of the intention to seek release from the bond. For bond releases initiated by the cabinet, the cabinet shall undertake the notification requirements set forth in this subsection. The notices shall also state that these individuals and their representatives may participate in a bond release inspection by contacting the cabinet. These notices shall be sent at the time the permittee initiates the application for release.

(c) Upon the filing of an application for bond release by a permittee, or the initiation of such release by the cabinet, the cabinet shall notify, within thirty (30) days of such filing or initiation, the municipality or county judge-executive where the surface coal mining operation is located.

(d) Within thirty (30) days after advertising an application for bond release as per the requirements of subsection (2) of this section, the permittee, or the cabinet if it elected to advertise as per subsection (2) of this section, shall submit proof of said publication. Proof of publication shall be placed, by the cabinet, with the bond release application. Such proof of publication shall be considered part of the bond release application.

(2) Public notice. At the time of initiating an application for bond release under this section, the permittee shall, and the cabinet may at permittee expense, advertise the filing of the application in the newspaper of largest bona fide circulation according to the definition in KRS 424.110 to 424.120 in the county or counties in which the permit area is located. Said advertisement shall begin within sixty (60) days of the initiation of any application for bond release whether said bond release applies to an incremental permit or the entire permit. Said advertisement shall contain all of the following:

(a) The name of the permittee, the permit number and the date of issuance or renewal of the permit or increment;

(b) The precise location and the number of acres of the lands subject to the application;

(c) The type and total amount of bond filed for the permit area or increment and the reclamation phase for which release is sought;

(d) The type and approximate dates of reclamation work performed;

(e) A description of the results achieved as they relate to the permittee's approved reclamation plan;

(f) A statement that written comments, objections, and requests for a public hearing may be submitted to the cabinet, provide the appropriate address of the cabinet, and the closing date by which comments, objections, and requests must be received;

(g) A statement that a public hearing has been scheduled, including the date and location of the hearing; and

(h) A statement that the schedule public hearing shall be cancelled if the cabinet does not receive a request for the public hearing by the closing date for requests for hearing.

(3) Objections, comments or requests for public hearing prior to bond release.

(a) Any person with a valid legal interest which might be adversely affected by release of the bond, or the responsible officer or head of any federal, state, or local governmental agency which has jurisdiction by law or special expertise with respect to any environmental, social, or economic impact involved in the operation or which is authorized to develop and enforce environmental standards with respect to such operations, shall have the right to file written objections or requests for a proposed release from bond and, if desired, file a request for a public hearing with the cabinet within thirty (30) days after the last publication of the notice required by subsection (2) of this section.

(b) The cabinet shall schedule a public hearing for each request for bond release, such hearing to be scheduled within five (5) working days of the end of the public comment period. If the cabinet does not receive a request for a public hearing by the end of the public comment period, the cabinet shall cancel the public hearing. The public hearing shall be held in the locality of the surface coal mining operation for which bond release is sought. The person requesting the release shall contact the cabinet prior to beginning advertisements under subsection (2) of this section to obtain the date and location of the public hearing in order to include this information in the advertisement.

(c) The hearing under paragraph (b) of this subsection shall be legislative in nature and the provisions of 405 KAR 7:091 and 405 KAR 7:092 shall not apply. The cabinet shall have the authority to advertise for, receive, review, consider, and act upon any written objections or requests for a public hearing. The cabinet may advertise for a public hearing in lieu of the public hearing under paragraph (b) of this subsection. The informal conference shall be held at the same time and location as was scheduled for the public hearing. The cabinet shall make a record of the informal conference unless waived by all parties, which shall be accessible to all parties. The cabinet shall also furnish all parties of the informal conference with a written finding of the cabinet on the informal conference, and the reasons for said finding.

(4) Inspection and evaluation. The cabinet shall inspect and evaluate the reclamation work involved within thirty (30) days after initiation of a bond release request by the permittee, or any person authorized to act on its or his behalf, or as soon thereafter as weather conditions shall permit. The cabinet shall consider, among other factors, the degree of difficulty to complete any remaining reclamation, whether pollution of surface and subsurface water is occurring, the probability of future occurrence of such pollution, and the estimated cost of abating such pollution. The surface owner, agent, or lessee liable to the cabinet shall be given notice of such inspection and may participate with the cabinet in making the bond release inspection. The cabinet may arrange with the permittee to allow access to the permit area, upon request by any person with an interest in bond release, for the purpose of gathering information relevant to the proceeding.

(5) Notice of decision. The cabinet shall as described in paragraph (b) of this subsection provide notification in writing of its decision to release or not to release all or part of the performance bond within five (5) days following receipt of proof of public advertisement as required in this section, or within five (5) days of the end of the thirty (30) day public comment period provided for in subsection (3) of this section, whichever is later. Provided, however, that if an informal conference for public hearing has been scheduled pursuant to subsection (3) of this section, the cabinet shall provide its notice of decision after thirty (30) days following said informal conference or public hearing.

(b) The notice of the decision shall state the reasons for the decision, recommend any corrective actions necessary to secure the release, and notify the permittee, the surety, any person with an interest in collateral who has previously requested such notification in writing, persons who filed objections in writing, and objectors who were a party to the informal conference or public hearing of their right to request, within thirty (30) days of notice, a formal hearing as provided for by subsection (6) of this section. Where the decision is to release all or
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part of the performance bond, the notice shall state that the release shall occur fourteen (14) days after the date of the decision unless temporary relief is granted under 405 KAR 7:092, Section 12. (c) In no event shall the cabinet disapprove an application for reclamation phase I or II release of a surety bond or a bond secured by a letter of credit solely upon the permittee’s failure to pay penalties or fines, if applicable reclamation requirements for the requested release have been met.

(6) Requests for formal hearing after bond release or denial. Any person aggrieved by the decision of the cabinet to approve or disapprove a bond release application, in whole or in part, shall have the right to request a formal hearing pursuant to 405 KAR 7:092, Section 9. (a) If the cabinet has decided to release all or part of the performance bond, the release shall not occur until fourteen (14) days after the date of the decision. At the end of that fourteen (14) days, the cabinet shall effect the release unless temporary relief is granted under 405 KAR 7:092, Section 12.

Section 2. Criteria and Schedule for Release of Performance Bond. (1) Monies pledged under performance bonds shall not be eligible for release until the permittee has met the requirements of the applicable reclamation phase as defined in subsection (4) of this section. The cabinet may release portions of the monies pledged under performance bonds applicable to a permit or increment following completion of reclamation phases on the entire permit area or entire increment.

(2) The maximum portion of the monies pledged under performance bonds applicable to a permit area which may be released shall be calculated on the following basis:

(a) Release an amount not to exceed sixty (60) percent of the total original bond amount on the permit area, section, or increment upon completion of phase I reclamation.

(b) Release an additional amount not to exceed twenty-five (25) percent of the total original bond amount on the permit area or increment upon completion of phase II reclamation, but in all cases the amount remaining shall be sufficient to reestablish vegetation and reconstruct any drainage structures.

(c) Release the remaining portion of the total performance bond on an entire permit area or increment after standards of phase III reclamation have been attained on the entire permit area or increment and final inspection and procedures of Section 1 of this administrative regulation have been satisfied. After the final bond release for phase III reclamation on an increment, the increment shall be deleted from the permit area.

(3) The cabinet shall not release any monies pledged under performance bonds applicable to a permit if such release would reduce the total remaining monies pledged under performance bonds to an amount less than that necessary for the cabinet to complete the approved reclamation plan, achieve compliance with the requirements of KRS Chapter 350, 405 KAR Chapters 7 through 24 or the permit, and abate any significant environmental harm to air, water or land resources or danger to the public health and safety which might occur prior to the release of all performance bond liability for the permit area.

(4) Reclamation phases are defined as follows:

(a) Reclamation phase I shall be deemed to have been completed on the entire permit area or increment when the permittee completes backfilling, regrading, topsoil replacement, and drainage control including soil preparation and initial seeding and mulching in accordance with the approved reclamation plan and a report for the area has been submitted to the cabinet in accordance with 405 KAR 16:200, Section 8 or 405 KAR 18:200, Section 8;

(b) Reclamation phase II shall be deemed to have been completed on the entire permit area or increment when:

1. Revegetation has been established in accordance with the approved reclamation plan and the standards for the success of revegetation, except productivity standards, have been met;

2. The lands are not contributing suspended solids to stream flow or run off outside the permit area or increment in excess of the requirements of KRS 350.420, 405 KAR Chapters 18 or 18, or the permit;

3. With respect to prime farmlands, soil productivity has been restored as required by 405 KAR 20:040, Section 6 and the plan approved under 405 KAR 8:050, Section 3; and

4. The provisions of a plan approved by the cabinet for the sound future management of any permanent impoundment by the permittee or landowner have been implemented to the satisfaction of the cabinet.

(c) Reclamation phase III will be deemed to have been completed on the entire permit area or increment when the permittee has successfully completed all surface coal mining and reclamation operations in accordance with the approved reclamation plan, such that the land is capable of supporting the postmining land use approved pursuant to 405 KAR 16:210 or 405 KAR 18:220; and has achieved compliance with the requirements of KRS Chapter 350, 405 KAR Chapters 7 through 24, and the permit; and the applicable liability period under 405 KAR 10:020, Section 3(2) has expired. (8 Ky.R. 1519; eff. 1-6-83; Am. 15 Ky.R. 447; 2016; eff. 1-25-86; 17 Ky.R. 2498; eff. 4-24-91.)

405 KAR 10:050. Bond forfeiture.


NECESSITY, FUNCTION, AND CONFORMITY: KRS Chapter 350 in pertinent part requires the cabinet to regulate surface coal mining and reclamation operations in a manner as to insure that satisfactory reclamation is accomplished. This administrative regulation sets forth the procedures and criteria by means of which a bond may be forfeited to the cabinet. This administrative regulation sets forth that certain violations of KRS Chapter 350 and administrative regulations promulgated pursuant to that chapter may cause a bond to be forfeited. This administrative regulation sets forth that a hearing may be requested before forfeiture can be effected. This administrative regulation specifies a method to determine the amount of bond forfeiture. This administrative regulation establishes criteria under which unused forfeited bond funds shall be returned to the person from whom they were collected.

Section 1. General. (1) The cabinet shall forfeit all of the remaining bond amount for any permit or increment pursuant to the procedures and criteria of this administrative regulation.

(2) The cabinet may withhold forfeiture if the permittee or the surety agrees to a compliance schedule to correct the violations of the permit or bond conditions.

(3) The cabinet shall withhold forfeiture and allow the surety or other financial institution providing bond to complete the reclamation plan if the surety or other financial institution can demonstrate the ability to complete the reclamation plan, including achievement of the capability to support the postmining land use approved by the cabinet, and will undertake to do so within a reasonable time frame and agrees to a compliance schedule. Neither the surety company nor other financial institution shall employ anyone to perform the measures who has been barred from mining pursuant to the provisions of KRS Chapter 350.

Section 2. Procedures. (1) If forfeiture of the bond is required by Section 3 of this administrative regulation, the cabinet shall:

(a) Send written notification by certified mail, return receipt requested, to the permittee, and to the surety on the bond, if applicable, of the cabinet’s determination to initiate forfeiture of the bond and the reasons for the forfeiture;

(b) Advise the permittee and surety, if applicable, of their right to challenge the determination pursuant to 405 KAR 7:092, Section 9; and

(c) If no hearing is requested within thirty (30) days following notification and the bond proceeds are not received, the secretary shall enter a final order of forfeiture and the cabinet shall proceed in an action for collection on the bond.

(2) The cabinet may, as an alternative to following the procedures of subsection (1) of this section, initiate formal hearing procedures concerning forfeiture of the bond alone or in conjunction with the cabinet’s action for other appropriate remedies against the permittee pursuant to 405 KAR 7:092, Section 5.

(3) The cabinet shall utilize funds collected from bond forfeiture to
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complete the reclamation plan on the permit area or increment on which bond coverage applied, and to cover associated administrative expenses. The funds shall be deposited in an appropriate account for the payment of these costs. Funds remaining after reclamation shall be returned to the person from whom the forfeiture proceedings were received, subject to the cabinet's right to attach or setoff the proceeds under state law.

(4) In the event the amount forfeited is insufficient to pay for the full cost of reclamation, the permittee or operator shall be liable for remaining costs. The cabinet may complete, or authorize completion of, reclamation of the bonded area and may recover from the permittee or operator all costs of reclamation in excess of the amount forfeited.

(5) Return of unused forfeited bond funds for interim or permanent program permit area overlapped by permanent program permit area. If the cabinet has not completed the reclamation plan on a permit area under 405 KAR Chapter 1 or 3 for which the bond was forfeited on or after July 15, 1988, or if the cabinet has not completed the reclamation plan on a permit area under 405 KAR Chapters 7-24 for which the bond was forfeited, and if the permit area and any related off-permit disturbances are entirely contained within the permit area of a subsequent valid permit under 405 KAR Chapters 7-24 for which the bond is in force, the cabinet shall retain the funds from the forfeited bond until the entire overlapped permit area and any related off-permit disturbances have been disturbed by the overlapping permittee and then shall return the unused funds to the person from whom the forfeiture proceeds were received, subject to the cabinet's right to attach or set off the proceeds under state law.

Section 3. Criteria for Forfeiture. (1) A bond for a permit area or increment shall be forfeited if the cabinet finds that:

(a) The permittee has violated any of the terms or conditions of the bond and has failed to take corrective action;

(b) The permittee has failed to conduct the surface mining and reclamation operations in accordance with KRS Chapter 350, the conditions of the permit or 405 KAR Chapters 7 through 24 within the time required;

(c) The permit for the area or increment under bond has been revoked or the operation terminated, unless the permittee, surety, or other financial institution providing bond assumes liability pursuant to an agreement for the completion of reclamation; or

(d) The permittee, surety, or other financial institution providing bond has failed to comply with a compliance schedule approved pursuant to Section 1(2) or (3) of this administrative regulation.

(2) A bond may be forfeited if the cabinet finds that:

(a)1. The permittee has become insolvent; or

2. A creditor of the permittee has attached or executed judgment against the permittee's equipment, materials, or facilities, at the permit area; and

(b) The permittee cannot demonstrate or prove the ability to continue to operate in compliance with KRS Chapter 350, 405 KAR Chapters 7 through 24, and the permit.

(3) The cabinet may forfeit a bond solely upon the permittee's failure to pay penalties or fines (if all reclamation requirements have been fully met) and retain the bond proceeds, or portion thereof as necessary to offset the penalty or fine owed (including administrative costs incurred by the cabinet), but the cabinet shall forfeit a bond under this circumstance only after the five (5) year liability period has expired; except that for surety bonds or bonds secured by a letter of credit:

(a) In no event shall the cabinet take any action to forfeit a surety bond or bond secured by a letter of credit under this circumstance until reclamation phase I and II monies have been released and the five (5) year liability period has expired; and

(b) If a forfeiture of a surety bond or a bond secured by a letter of credit under this circumstance has occurred, the cabinet shall not retain the surety bond or bond secured by letter of credit or any proceeds thereof and the permittee shall continue to be responsible for payment of the penalties or fines as well as administrative costs incurred by the cabinet.

Section 4. Forfeiture Amount. The cabinet shall forfeit the entire amount of the bond for the permit area or increment (8 Ky.R. 1521; eff. 1-6-83; Am. 15 Ky.R. 451; 1073; eff. 12-13-88; 20 Ky.R. 132; 544; eff. 9-22-93.)


NECESSITY, FUNCTION, AND CONFORMITY: KRS Chapter 350 in pertinent part requires the cabinet to regulate surface coal mining and reclamation operations, including requiring bond sufficient to ensure satisfactory reclamation. KRS Chapter 350 further authorizes the cabinet to establish alternative methods of meeting bonding requirements. This administrative regulation implements an alternative bonding program known as a bond pool. This administrative regulation establishes requirements for applications for membership in the bond pool; procedures for submittal of, review of, and decisions on applications, including determinations of financial standing and reclamation compliance records of applicants; procedures for acceptance of specific permit areas into coverage by the bond pool; and procedures for keeping of production records, reporting of production, and payment of fees based on coal production.

Section 1. Applicability. This administrative regulation applies only to the voluntary alternative bonding program known as the Kentucky Bond Pool, as established at KRS 350.700 through 350.755, and to permanent program permits or increments covered under that pool.

Section 2. Forms. (1) The following forms, which are required to be submitted by applicants and members, are hereby incorporated by reference:

(a) Application for Membership, BP-01, revised September 1, 1988; and

(b) Monthly Production Report, BP-02.

(2) These forms may be reviewed or obtained at the Department for Surface Mining Reclamation and Enforcement, #2 Hudson Hollow, Frankfort, Kentucky 40601, Monday through Friday, 8 a.m. to 4:30 p.m.

Section 3. Review of Decisions. There shall be no administrative appeal under 405 KAR 7:092 from a decision of the commission. However, the applicant or member may, within sixty (60) days after notice of the decision, request the commission to reconsider its decision. The commission may, at its discretion, grant or deny the request for reconsideration.

Section 4. Applications for Membership. (1) Any person desiring membership in the bond pool shall submit an application for membership to the commission at the address established by the administrator.

(2) The application shall be submitted on forms provided by the commission and shall be of the form, content, and number of originals and copies as the commission may require. The application shall be typed or printed, and shall be legible throughout.

(3) Financial statements required with the application shall be prepared by a certified public accountant. Financial statements shall be kept confidential to the commission, the administrator, and cabinet personnel authorized by the administrator.

(4) The application shall include an application fee of $100 by cash or by certified check, cashier's check or money order made payable to "Kentucky State Treasurer." The fee shall not be refunded in any circumstances, but shall be applied toward the membership fee if the applicant is accepted for membership.

(5) The application shall be complete in all respects.

Section 5. Review of Applications. (1) As soon as practicable after
A KENTUCKY GOVERNMENT PERSPECTIVE ON BONDING COMPANY FAILURES AND MINING INDUSTRY BANKRUPTCIES IN 2000-2002

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and
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Office of Legal Services
Kentucky Natural Resources and Environmental Protection Cabinet
Frankfort, Kentucky

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SECTION E(c)
This outline is an attempt to provide a government perspective on two tumultuous years in the mining industry. The tumult was the result of a combination of the failures of three companies that provided millions of dollars in workmen’s compensation and mining reclamation bonds, an unforgiving coal market, and some promising business decisions that did not live up to their promise. These factors drove three of the state’s largest mining enterprises into bankruptcy over the last two years. Two of them emerged from the bankruptcy process in significantly different form, while the other is still in the court.

The first section of the outline deals with the facts and figures relating to the three bonding company failures. The second portion of the outline deals with the bankruptcies of Quaker Coal Company, Inc. ("Quaker"), Lodestar Energy, Inc. and Lodestar Holdings, Inc. (collectively referred to as "Lodestar"), along with AEI Resources Holding, Inc. ("AEI"). We readily admit that there is not as much discussion of legal issues and theories as we would like, particularly in the first section. This is a function of the fact that many issues are still in litigation and caution must be exercised.

One of the things that occurred during this period, was an increased level of communication and cooperation between our agency and other agencies. The events of the last two years spawned weekly, and sometimes daily, conferences between the Natural Resources and Environmental Protection Cabinet (KNREPC), the Department of
Insurance ("KDOI"), and the Department of Workers’ Claims ("KWC"). When appropriate, these meetings included members of Governor Patton’s staff and the Governor’s Office of Policy and Management ("GOPM"). Many of the other states adversely effected by these events also conferred with us, as did the United States Office of Surface Mining ("OSM"). There were also many meetings and conferences with the parties directly effected, as well as representatives of their industries.

Much of the information contained in this outline came from these meetings and their participants. Several individuals deserve special recognition for their contributions of data and information over the course of these events. While they did not participate directly in the preparation of this outline, we wish to acknowledge contributions by the following people: Julie M. McPeak, Acting General Counsel of the Department of Insurance and her predecessor, Gale Pearce; Mark Thompson, Director of the Division of Field Services, Department for Surface Mining Reclamation and Enforcement; and Gary W. Davis, Director of Security and Compliance, Department of Workers’ Claims.

I. THE BONDING PROBLEMS

The outline and our presentations will not deal with the fundamentals of bonding, i.e., the why it’s done and how we do it. It is enough to say that the laws of the Commonwealth require mining and environmental companies to post bonds to cover the performance of their remedial work, should they fail to do it. The laws also require businesses to post bonds to cover their obligations to the workmen’s compensation programs. The laws require that these bonds be issued in particular forms, subject to relevant statutes and regulations, and be issued by entities capable of paying the obligations when called upon to do so.
Much of the information in this portion concerns the problems of Frontier Insurance Company ("Frontier"), simply because of the magnitude of its impact. Its impact was so great that the bankruptcies discussed in the second section of this outline were either caused or severely complicated by it. The problems of the other two companies, Cumberland Surety Insurance Company ("CSIC"), based in Lexington, and Reliance Insurance Company ("Reliance"), based in Pennsylvania, had less impact because their bonding business was quickly taken over by other companies.

The following are background facts necessary to an understanding of the magnitude of the bonding problem:

**The Surety Companies**

- As of April 2000, KNREPC held approximately 8,300 surface mining bonds totaling $780 million.
- In April of 2000, Frontier had issued approximately $339 million in reclamation bonds, $80 million worth of workers compensation bonds, and $12 million worth of bonds on hazardous waste facilities and landfills.
- In April of 2000, CSIC had issued approximately $73 million in surface mining bonds.
- In April of 2000, Reliance and its subsidiaries had issued approximately $20 million in surface mining bonds.

**The Mining Companies**

- In April of 2000, AEI had posted approximately $226 million worth of surface mining bonds issued on Frontier paper.
• In April of 2000, Lodestar had posted approximately $28 million worth of surface mining bonds issued on Frontier paper.

• In April of 2000, Quaker had posted approximately $38 million worth of surface mining bonds issued on Frontier paper.

As you can see, approximately 40% of all surface mining bonds and a large amount of workmen’s compensation bonds were impacted during this time period. The companies put at risk by the Frontier failure represented more than 25% of the coal produced in Kentucky.

A. What Happened and When

What follows is a timeline of the events over the last two years that will allow the reader to gain a better understanding of how the saga unfolded. The daily and weekly internal agency meetings are not included. Only those meetings where multiple agencies were involved are included. However, this lengthy list of events will give the reader some idea of how much time and effort were expended by the agencies involved. There were some times where not much happened, but there were others when things happened at a fast pace:

• February 2000: OSM sends material to KNREPC indicating mounting financial troubles for Frontier and financial problems faced by its largest Kentucky customer, AEI.

• April 10, 2000: (1) Cumberland Surety is taken over by KDOI. Cumberland had suffered financially since the entry of Frontier into the Kentucky reclamation bonding business. (2) KNREPC learns that KWC is refusing Frontier bonds as acceptable bonding for that program.
• April 20, 2000: US Treasury Dept. gives Frontier ultimatum to sell its surety business or face loss of its certificate of authority for federal programs.

• April 28, 2000: (1) AM Best lowers its rating of Frontier from B- to C++. (2) OSM advises KNREPC that it will no longer allow the issuance of permits with Frontier bonds, in accordance with Treasury Dept. rules.

• May 31, 2000: The US Treasury Dept. revokes Frontier's certificate of authority to provide surety in federal programs.

• June 14, 2000: Frontier and the state of New York agree on a corrective action plan.

• June 19, 2000: Quaker files for bankruptcy with $38 million in Frontier bonds.

• June 28, 2000: KDOI signs an agreed order with Frontier that stops the writing of any new business in Kentucky on all lines of insurance, but allows the renewal of surface mining permits with Frontier bonds already in place. The order also directed Frontier to insure that all bonds were adequately capitalized and priced and imposed additional financial reporting requirements.

• August 2, 2000: Representatives of insurance brokers and an insurance company meet with representatives of KNREPC, KDOI, and KWC to discuss possible bonding solutions. While their solution wouldn't meet program requirements, they were willing to consider issuing bonds themselves.

• September 19, 2000: Representatives of the insurance brokers and insurance companies meet again with representatives from KNREPC, KDOI, GOPM, and KWC to discuss other bonding solutions.

• September 21, 2000: KNREPC furnishes Willis and AIG with documentation pertaining to the causes of, and procedures for, bond forfeiture.
• September 28, 2000: Frontier negotiates the purchase of a reinsurance agreement with National Indemnity, a Berkshire Hathaway company. The agreement covers those policies/bonds issued prior to 1/1/2000.

• December 29, 2000: Frontier stock value is at 6 cents per share.

• January 2001: National Indemnity and Frontier attempt to provide verification of bonds covered by the reinsurance by executing an endorsement to the prior bulk reinsurance agreement. The companies assure KNREPC that Frontier’s obligations can be met in the event bonds are forfeited.

• February 28, 2001: New York directs Frontier not to write any new or renewal business in that state, without prior written approval from the state.

• March 28, 2001: KDOI modifies its agreed order with Frontier by ordering the company to cease the writing of all new and renewal business, except for in-force, non-cancelable bonds covered by the reinsurance agreement with National Indemnity. Surface mining bonds are non-cancelable and excluded from the order.

• April 3, 2001: Lodestar Energy, Inc. is taken into bankruptcy by its creditors. Lodestar carried approximately $28 million in Frontier bonds.

• August 21, 2001: A KDOI financial examiner arrives at Frontier to ascertain the financial condition of the company, due to a lack of information from the company or New York.

• August 24, 2001: New York begins rehabilitation proceedings in their state courts. New York's Petition for Rehabilitation finds Frontier to be insolvent. Payments to workers comp claimants are stopped. The New York DOI discovers that all other
claims payments were suspended by Frontier on August 5, 2001, due to a lack of available funds.

- August 27, 2001: (1) New York Supreme Court issues order granting the state insurance department's petition to begin the voluntary rehabilitation of Frontier. (2) KDOI issues an order suspending Frontier's certificate of authority. A copy of the order follows this outline.

- August 28, 2001: KDSMRE issues a letter to all permittees with Frontier bonds demanding replacement of those bonds within 90 days (November 26, 2001), pursuant to 405 KAR 10:030.

- September 10, 2001: A Pennsylvania court orders regulators to either rehabilitate Reliance or liquidate it. Reliance and its subsidiaries have issued approximately $20 million in reclamation bonds.

- September 13, 2001: Representatives from New York and National Indemnity participate in a conference call with KDOI, KNREPC and KWC. New York states that it has no authority to pay claims under its current order and National Indemnity will not pay unless New York/Frontier pays first. They are not willing to cover the $1.8 million owed to the Coal Guaranty Fund, nor are they willing to begin payments to workers comp recipients.

- September 28, 2001: KNREPC learns that Frontier, New York and National Indemnity have renegotiated the reinsurance agreement following the seizure of Frontier by New York to take away payment for forfeitures resulting from the demand for replacement. The renegotiated agreement segregates a portion of the reinsurance for claimants residing in California. Additionally, the reinsurance
agreement was altered to provide operating capital for Frontier, with those sums acting as an offset to the reinsurance aggregate.

- October 1-2, 2001: Representatives of various coal and insurance companies meet with KDOI, KNREPC, GOPM and KWC concerning the status of efforts to replace bonds for mining and workers comp.

- October 5, 2001: A Pennsylvania court orders the liquidation of Reliance. Notices for replacement are mailed to all Reliance-bonded permittees by KNREPC. Reliance bonds are to be replaced by Travelers Group pursuant to its purchase of the Reliance surety line.

- October 11, 2001: Quaker subsidiaries file a Petition for Hearing under KRS 304.2-310, seeking review of the KDOI suspension of Frontier's certificate of authority.

- October 12, 2001: Hearing in bankruptcy court on reorganization plans for Quaker Coal.

- October 13, 2001: KDOI Commissioner rejects the petition of the Quaker subsidiaries. A copy of this order follows the outline.

- October 16, 2001: KDOI learns from California insurance regulators that New York entered a formal rehabilitation order for Frontier on October 10. The order finds, among other things, that Frontier is insolvent.

- October 18, 2001: New York and Frontier representatives meet with KNREPC and KDOI to discuss alternatives to replacement on November 26. They propose that KNREPC give another 90 days with firm milestones for partial replacement, until all are replaced.
October 19, 2001: The bankruptcy court enters an order accepting the AEP plan for the reorganization of Quaker Coal.

October 26, 2001: (1) At another hearing in the Quaker bankruptcy, the AEP and Quaker reach an agreement on a division of the company's assets. (2) AEI files a Petition for Hearing and Motion for Stay of the KDOI order suspending Frontier's certificate of authority, pursuant to KRS 304.2-310, challenging KDOI's authority to order replacement of Frontier bonds.

November 1, 2001: West Virginia Department of Environmental Protection begins issuing NOV's to Frontier-bonded permittees for inadequate bonds because of the finding of insolvency by the New York court.

November 2, 2001: (1) OSM meets with representatives of KNREPC and KDOI to discuss replacement schedule. (2) KDOI Commissioner rejects the petition of the Quaker subsidiaries. A copy of this order follows the outline.

November 5, 2001: KDOI and KNREPC personnel meet with representatives of the insurance industry and the Kentucky Coal Council to discuss a way to provide companies with the collateral necessary to replace Frontier bonds. $279,148,015 in reclamation bonds remain on Frontier paper.

November 16, 2001: (1) Lodestar files an adversary action in bankruptcy court seeking an injunction against KNREPC. (2) OSM notifies Tennessee companies that less than full replacement of Frontier bonds is acceptable.

November 21, 2001: (1) OSM agrees that Kentucky can follow its lead and demand less than full replacement of Frontier bonds. (2) KNREPC notifies coal industry associations that it has altered its demand for replacement to allow replacement over a
90-day period with 1/3 of “active” permits covered at 30, 60, 90-day intervals. (3) Bankruptcy court grants Lodestar’s request for an injunction preventing KNREPC from shutting down its operations for failure to replace Frontier bonds.

- November 26, 2001: KNREPC alters its replacement schedule again, following an OSM change of opinion on what constituted sufficient replacement, and notifies coal industry association that it will allow 5% of active site replacement on December 5, and 1/3 remainders at the 30, 60 and 90 day intervals.

- December 5, 2001: All active bonds are replaced in accordance with the decisions of November 26.

- December 21, 2001: Deputy Secretary of the US Interior Department, Steven Griles, sends a letter to the OSM office in Knoxville outlining reasons supporting an extension of time to March 1, 2002, for AEI to replace its Frontier bonds.

- December 27, 2001: AEI files suit in Boyd Circuit Court to enjoin KNREPC from requiring further bond replacement under its November 26 plan. The Court issued a temporary restraining order.

- January 28, 2002: AEI, KNREPC and KWC reach agreement on a plan to allow AEI to replace its bonds in accordance with its plan to file a prepackaged Chapter 11 bankruptcy in late February and to provide for dismissal of the Boyd Circuit Court action and TRO.


- March 15, 2002: All Frontier bonds posted by AEI are replaced.

B. Remaining Issues
• There are approximately 450 increments still bonded with Frontier bonds, representing approximately $70 million. This figure includes the bonds covered by the Lodestar injunction and those being replaced under the AEP reorganization plan. The majority of these bonds are on increments that are in phase 1 or phase 2 bond release status. What happens with these increments will largely be determined by the outcome of the Frontier rehabilitation process.

• There is no clear sense of how the Frontier rehabilitation process will turn out. New York has pledged that it intends to bring Frontier out of the process and not take it to liquidation. There are plenty of skeptics among insurance and coal industry people. We must admit some skepticism on our own part, but are hopeful that New York can make that happen.

• It is safe to say that Frontier still disputes KNREPC’s assertion that it is “incapacitated” within the meaning of 405 KAR 10:030 Sec. 2(c). The language of the regulation makes it clear that its “bankruptcy, insolvency, or revocation or suspension of its license or certificate of authority” causes the incapacity of an insurer. Here, KDOI has suspended Frontier’s certificate of authority to operate in Kentucky, rendering it “incapacitated” under the regulation. Further, the New York superintendent of insurance alleged in court pleadings that Frontier is insolvent and the court entered an order finding that Frontier is insolvent.

• The agencies involved in this matter are concerned that modifications to the reinsurance agreement made by New York, National Indemnity, and Frontier are allowing the reinsurance cap to be diminished to the detriment of Kentucky.
Another area of concern, is Frontier’s willingness, or unwillingness, depending upon one’s point of view, to meet its obligation to pay claims that come due. Frontier has said that it will not pay bonds that are forfeited due to violations for failure to replace Frontier bonds. However, it has said that it will pay on those bonds forfeited by reason of outstanding unabated violations. To date, KNREPC has been unsuccessful in making a claim to Frontier/New York in a manner that has resulted in payment. This is one of those areas where the prospect of litigation probably requires us to exercise the better part of valor and say no more.

II. BANKRUPTCY CASES AND ISSUES

The Frontier surety problems have had an impact in the bankruptcy forum. In the past year, there have been three prominent chapter 11 bankruptcy cases in the Eastern District of Kentucky, in which Frontier reclamation bonds have played a significant role. Set forth below is a brief discussion of these cases and some of the issues that have been raised as a result of the Frontier bonds.

A. Quaker Coal Company, Inc., et al., Case Nos. 00-51374 and 00-51376 through 00-51394

Quaker Coal Company, Inc. and nineteen of its subsidiaries filed Chapter 11 Bankruptcy Petitions in the Eastern District of Kentucky on June 16, 2000. The Debtors had approximately $45.5 million in Frontier reclamation bonds on their mining permits. The Debtors filed a Disclosure Statement with respect to their proposed Joint Plan of Reorganization on June 1, 2001. The Motion to Approve the Disclosure Statement was continued from time to time. During this period America Electric Power Company, Inc.
and its subsidiaries (AEP) and Wexford Capital, LLC (Wexford) both sought to file their
own Plans of Reorganization.

On August 27, 2001, the Department of Insurance entered an Order suspending
Frontier's Certificate of Authority, and on August 28, 2001 the Cabinet sent out ninety
(90) day letters requiring the replacement of the Frontier bonds pursuant to 405 KAR
10:030, Section 2(5)(c)3. On August 29, 2001, the Bankruptcy Court entered an Order
denying an extension of Quaker's exclusivity period for filing a plan and on September
21, 2001 the court entered an Order approving the Disclosure Statements of the Debtors,
AEP, and Wexford. Numerous objections to the Disclosure Statements and the proposed
plans were filed including objections by the State of Colorado, Frontier Insurance
Company and the Commonwealth of Kentucky based on issues relating to the Debtors’
Frontier surety bonds and their reclamation obligations. Ultimately, the Bankruptcy
Court entered an Order confirming the AEP Plan over the Debtors’ Plan. At the
Confirmation Hearing, Wexford withdrew its plan due to its failure to obtain sufficient
votes.

Set forth below, are brief discussions of how each of the plans proposed to deal
with the Frontier bonds, and some of the issues raised by these proposed treatments.

1. Quaker's Plan: The Debtors proposed to continue mining operations with the
Frontier bonds in place. They proposed to place fifty cents (50¢) per ton of coal sold by
the Reorganized Debtors into a bond reserve that would be used to replace the Frontier
bonds over time. The Cabinet objected to the Debtors' plan pursuant to 11 U.S.C. Section
1129(a)(11) (feasibility) and 11 U.S.C. Section 1129(a)(3) (the plan was not proposed in
good faith or by any means forbidden by law). The Cabinet's objection was based on the
fact that the Debtors' reorganization plan relied on their ability to continue mining operations on their Kentucky permits while Frontier bonds remained in place. However, pursuant to 405 KAR 10:030, Section 2(5)(c) 3, the Debtors would be required to cease all coal extraction and coal processing operations on said permits once the ninety (90) day period set forth in said regulation and the Cabinet's August 28, 2001 letters ran.

2. The Wexford Plan: Under this Plan, Wexford would own 100% of the stock of Quaker Coal Company, Inc., the current Board of Directors of the Debtors would be replaced by a new Board of Directors appointed by Wexford. (The Wexford Plan specifically indicated that three of the former directors and officers would not be retained by the Reorganized Debtors.) Wexford also proposed that it would replace all of the Frontier bonds on the active mining operations, but would have the option of not replacing Frontier bonds on inactive mining operations. The Cabinet objected to Wexford's plan pursuant to 11 U.S.C., Section 1129(a)(3) and (11). The basis for the Cabinet's objection was that a transfer of the Debtors' Kentucky permits to the Reorganized Debtors as envisioned by the Wexford Plan would constitute a transfer, assignment, or sale of permit rights. Therefore, all of the Debtors' permits would have to be transferred and bonds satisfactory to the Cabinet be filed with the transfer application for each permit.

- 405 KAR 8:001, Section 1(132) defines a transfer, assignment, or sale of permit rights as "a change in ownership or other effective control over the right to conduct surface coal mining operations under a permit issued by the cabinet." In order for a transfer of a permit to occur, the Cabinet must approve the transfer pursuant to
KRS 350.135(1). In the case of Com. Natural Resources and Environmental Protection Cabinet v. Neace, 14 S.W.3rd 15 (Ky. 2000), the Kentucky Supreme Court held that a change in ownership or other effective control over the rights to conduct surface coal mining operations constitutes a transfer which must be approved by the Cabinet.

- KRS 350.135(1) requires that a transferee must file with the transfer application a bond satisfactory to the Cabinet. Additionally, KRS 350.135(3) provides that "[t]he cabinet shall not release the first permittee from bond liability...until the transferee, having filed a bond satisfactory to the cabinet, receives written approval from the cabinet for the transfer". Therefore, under the Wexford Plan all Frontier bonds would have to be replaced on all of the Debtors' Kentucky permits as a result of the corporate restructuring.

3. **The AEP Plan:** AEP proposed to purchase all of the assets of the Debtors except for certain specifically excluded assets. AEP would replace all of the Frontier bonds on the permits that it purchased. However, among the assets that AEP would not purchase were five Kentucky permits with Frontier bonds totaling $4.2 million. The Cabinet, therefore, objected to AEP's plan. As the basis for its objection, the Cabinet asserted that AEP's plan would constitute an impermissible de facto abandonment of these excluded permits.
Various pleadings filed by Frontier Insurance, the State of Colorado and the Commonwealth of Kentucky dealt with this issue of abandonment and the corollary issue of whether the cost of reclamation would be an administrative expense. Although the court never specifically ruled on these issues, various proposed Plans and Disclosure Statements were amended to try to address these concerns. In the case of the Cabinet's Objection, AEP removed three of the five Kentucky permits from the excluded asset list, and provided that the Cabinet could seek to recover reclamation liabilities from AEP as an administrative expense on the remaining two excluded permits if certain preconditions were met. As a result, the Cabinet withdrew its objection to AEP's plan.

- **Abandonment**: 28 U.S.C., Section 959(b) provides as follows:

  a trustee, receiver or manager appointed for any cause pending in any court of the United States, including a debtor in possession shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner the owner or possessor thereof would be bound to do if in possession thereof.


- **Administrative Expense**: The Sixth Circuit has addressed the interplay between Section 959(b), state environmental laws and the Bankruptcy Code. In the case of In re Wall Tube & Metal Products Co., 831 F.2d 118...
(6th Cir. 1987), the Sixth Circuit determined that a state was entitled to recover as an administrative expense its costs of responding to improper disposal of hazardous substances. The Sixth Circuit, in relying on Midlantic, found that:

[i]f the Wall Tube trustee could not have abandoned the estate in contravention of the state's environmental law, neither then should he have maintained or possessed the estate in continuous violation of the same law. Otherwise, the result avoided in Midlantic would...remain an ongoing, potentially disastrous health hazard without remedy from those at fault. The only difference here is that the danger arose because of the trustee's and the debtor's failure to correct the violation, not because of the trustee's exercise of the abandonment power as in Midlantic.

Wall Tube at 122 (emphasis original).

The case of In re Coal Stripping, Inc., 222 B.R. 78 (Bankr. W.D. Pa. 1998) also held that actual reclamation costs on a mine site incurred post-petition were entitled to administrative expense priority. This was so even though the debtor ceased its mining operations prior to filing its Chapter 11 Bankruptcy. The Court held that "[b]ecause this is a chapter 11 with a debtor-in-possession, to the extent [the state] expended money to perform post-petition clean-up, it would have an administrative expense. This is so, even though [d]ebtor did not operate in the chapter 11." In re Coal Stripping, at 82.

B. Lodestar Energy, Inc. and Lodestar Holdings, Inc., Case Nos. 01-50969 and 01-50972
1. Factual Background

On March 30, 2001, involuntary petitions were filed against Lodestar Energy, Inc. and Lodestar Holdings, Inc. (Lodestar) under Chapter 11 of the United States Bankruptcy Code. On April 27, 2001, Lodestar consented to the Chapter 11 and an Order for Relief was entered by the court. Lodestar has continued to operate as debtor-in-possession, and continues to operate its mining operations. Lodestar has approximately 68 Kentucky surface mining permits, and Frontier Insurance Company issued all of their reclamation bonds. To date the exclusivity period for filing a plan has run, but no Plan of Reorganization has been proposed.

On November 16, 2001 Lodestar filed an Adversary Proceeding (Adv. Pro. No. 01-5248) against Cabinet officials requesting a temporary restraining order and/or preliminary injunction to enjoin them from requiring that Lodestar either cease coal extraction and processing operations or replace its Frontier bonds in compliance with the requirements set forth in the Cabinet’s August 28, 2001, ninety day letters. Additionally, Lodestar filed a Motion for an Order Determining that Certain Threatened Actions Would Violate the Automatic Stay. (i.e. the Cabinet's efforts to enforce Kentucky law as it pertained to Lodestar's Frontier bonds would violate the automatic stay.)

A hearing was held on November 19, 2001 and continued to November 21, 2001, on Lodestar’s Motions. On November 21, 2001 the Bankruptcy Court issued oral findings and fact and conclusions of law and entered two orders, one in the main bankruptcy case determining that certain threatened actions by the Cabinet would violate the automatic stay, and the second order in the Adversary Proceeding granting Lodestar’s Motion for Preliminary Injunction. The Cabinet and its officers filed Motions to (1) Alter
or Amend Judgment and/or (2) Amend the Courts Findings in both the main bankruptcy action and the Adversary Proceeding. These Motions were subsequently held in abeyance to allow the parties time for settlement negotiations. However, no agreement was reached and a briefing schedule on the Cabinet’s Motions is now in effect. It is anticipated that the matter will be submitted to the court for its decision by June 7, 2002.

Subsequent, to the Bankruptcy Court’s November 21, 2001 rulings, the Fourth Circuit decided the case of Safety-Kleen Inc., (Pinewood) v. Wyche, 274 F.3d 846 (4th Cir. 2001) on December 19, 2001. As discussed below, Safety-Kleen should have a significant impact on the Bankruptcy Court’s determination that the Cabinet and its officials’ actions were subject to the automatic stay set forth in 11 U.S.C. Section 362(a).

On January 2, 2002, Lodestar brought an adversary proceeding (Adv. Pro. No. 02-5001) against the State of Utah and its officers, and brought a Motion to determine that actions threatened by the State of Utah would violate the automatic stay. These actions were based on the same Frontier bonding issues that had been raised in Lodestar's actions against the Cabinet. On January 31, 2002, a hearing was held on this matter. However, prior to Judge Scott rendering a decision, the parties reached an agreement resolving the matter. On February 25, 2002, Agreed Orders were entered in the Adversary Proceeding and the main bankruptcy case dismissing the adversary complaint and the motion to determine that the State of Utah had violated the automatic stay.

2. Issues Raised in the Lodestar Case
In Lodestar's actions against Kentucky, Utah and their officials, several issues have been raised regarding the states' ability to require Lodestar to replace its Frontier bonds in light of Lodestar's bankruptcy. The Kentucky officers were enjoined under the Ex parte Young doctrine. The Cabinet raised sovereign immunity as a defense to the injunctive relief granted by the court to Lodestar. Although, the importance of the sovereign immunity issue cannot be understated it is not germane to the scope of this outline and therefore will not be discussed. Set forth below is a brief discussion of some of these issues.


In its November 21, 2002 Orders, the bankruptcy court held that the actions of the Cabinet to require Lodestar to replace its Frontier bonds or cease mining activities and commence reclamation would be a violation of the automatic stay set forth in 11 U.S.C., Section 362(a). In its oral findings of fact and conclusions of law the court found that these actions did not fall within the police power exception to the automatic stay set forth 11 U.S.C. Section 362(b)(4) and relied on the case of Chao v. Hospital Staffing Services, Inc., 270 F.3d 374 (6th Cir. 2001) for support.

• The Automatic Stay. Under 362(a) the filing of a bankruptcy petition creates an automatic stay. Among the actions stayed are: the commencement or continuation of a judicial or administrative action against the debtor that was, or could have been commenced prior to the bankruptcy (11 U.S.C., Section 362(a)(1)); any act to obtain possession of property of the estate or to exercise control over property of the estate (11 U.S.C. Section 362(a)(3)); and any
act to collect, assess, or recover a claim against the Debtor that arose before the commencement of the bankruptcy (11 U.S.C. Section 362(a)(6)). The court in the Lodestar Case found that the Cabinet's threatened actions would violate each of these provisions.

- **The Police Power Exception.** Pursuant to 11 U.S.C. Section 362(b)(4), the automatic stay provision of Section 362(a)(1), (2), (3) and (6) does not operate as a stay to the "commencement or continuation of any action or proceeding by a governmental unit...to enforce such governmental unit's...police and regulatory power, including the enforcement of a judgment other than a money judgment, obtained in an action or proceeding by the governmental unit to enforce such governmental unit's...police or regulatory power."

- The police power exception generally applies to a governmental unit's enforcement of the environmental laws enacted to protect public health and safety. See *Midlantic*, 474 U.S. 494; *Penn Terra Ltd. v. Department of Environmental Resources, Commonwealth of Pennsylvania*, 733 F.2d 267 (3rd Cir. 1984); *In re Commonwealth Oil Refining Co., Inc.*, 805 F.2d 1175; *In re Commerce Oil Co.*, 847 F.2d 291 (6th Cir. 1988); and *United States v. Nicolet, Inc.*, 857 F.2d 202 (3rd Cir. 1988).
Chao v. Hospital Staffing Services, Inc., 270 F.3d 374 (6th Cir. 2001). The Chao case involved the Department of Labor's filing of a "hot goods" action under the Federal Fair Labor Standards Act to prevent a Chapter 7 trustee from conducting the sale of the debtor's assets in interstate commerce, reasoning that the debtor's assets were produced by employees who were not compensated in accordance with the minimum wage and overtime standard. The Sixth Circuit adopted a two-prong test to determine whether the police power exception to the automatic stay applied. These two tests are:

1. Pecuniary purpose test. Under this test the court focuses "on whether the governmental proceeding relates primarily to the protection of the government's pecuniary interest in the debtor's property, and not to matters of public safety. Those proceedings which relate primarily to matters of public safety are excepted from stay." Chao at 385.

2. Public policy test. Under this test the court "must distinguish between proceedings that adjudicate private rights and those that effectuate public policy." Chao at 385-386.

The Chao court determined that the Department was attempting to collect unpaid wages for the employees of the debtor (or the private rights of third parties) and therefore
the police power exception did not apply under the public policy test.

It should be noted that Lodestar's argument for why the police power exception did not apply was based on their assertion that the Cabinet's actions to require adequate bonding is primarily an action to preserve the private rights and interests of the Commonwealth as a potential creditor and not to effectuate a public policy. The Chao court did not address this pecuniary interest argument in any detail as it found that the government was not attempting to protect its pecuniary interest in the debtor's property. Rather, the Chao court looked to the public policy test and whether the government's actions would result in a pecuniary advantage to third private parties. Chao at 388-389.


In this case the Fourth Circuit analyzed the question of whether South Carolina's efforts to require Safety-Kleen to replace its Frontier bonds on an operating landfill fell within the police power exception set forth in Section 362(b)(4). The Fourth Circuit conducted and extensive analysis of whether this was an action to promote public safety and welfare or an action to protect the state's pecuniary interest. In holding that South Carolina's actions fell within the police power exception set forth in Section 362(b)(4) the
Fourth Circuit found that South Carolina's "financial assurance regulations are within the regulatory exception because they serve the primary purpose of deterring environmental misconduct." Safety-Kleen at 866. The recent cases analyzing the police power exception to the automatic stay make it clear that the reviewing court should look to any legislative intent (In Kentucky the importance of reclamation is addressed at KRS 350.020) and defer to that legislative intent when making the determination as to whether the Police Power Exception applies.

(b) Pre-Petition verses Post-Petition Obligations

In its oral findings of fact and conclusions of law the Bankruptcy Court held that Lodestar's reclamation obligations were pre-petition matters and the Cabinet was required to file a proof of claim. The Court cited no authority for this proposition. The Cabinet's position on this matter is that Lodestar continues to operate its surface mining permits and has an on-going post-petition reclamation obligation. Furthermore, as demonstrated in this outline's discussion of the Quaker bankruptcy, the post-petition reclamation of pre-petition disturbance is an administrative expense and not a pre-petition claim. See: In re Wall Tube & Metal Products Co., 831 F.2d 118 (6th Cir. 1987); and In re Coal Stripping, Inc., 222 B.R. 78 (Bankr. W.D. Penn. 1998).

(c) Violations of federal law and duty to comply with state law under 11 U.S.C., Section 959(b).

In its Motions, Lodestar argued that the threatened actions by the Cabinet would violate 11 U.S.C., Section 363, 365, 507, 541 and the Supremacy Clause of the
United States Constitution. Section 363 deals with the use, sale or lease of property of the estate; Section 365 deals with executory contracts and unexpired leases; Section 541 deals with property of the estate; and Section 507 deals with the priority scheme under the Bankruptcy Code. In essence, Lodestar claims that the requirement to replace its Frontier bonds or cease mining activities is an attempt to restructure the priority scheme of the Bankruptcy Code. Furthermore, Lodestar also claims that the bonding requirement improperly interferes with Lodestar's rights to use, sell or lease its property, and to perform, assume, or assign its executory contracts, because bond replacement requires Lodestar to devote its resources to that end. Lodestar further argued that the Supremacy Clause of the Constitution would be violated by the Cabinet in that the state law requiring them to replace the Frontier bonds would reorder the priorities established by the bankruptcy code.

The Cabinet's position is that the requirement that Lodestar replace its Frontier bonds or cease operation would not violate any of these federal provisions. As already discussed, the Cabinet believes that its actions clearly fall within the police power exception to the automatic stay set forth in 11 U.S.C., Section 362(b)(4). As also discussed above, Lodestar's reclamation obligation is not merely a pre-petition claim but an ongoing post-petition matter that may be entitled to administrative expense status. Finally, federal law (28 U.S.C. Section 959(b)) specifically requires that the debtor-in-possession comply with valid state laws in the operation of its mine sites. This includes maintaining adequate bonds on its mining permits. In light of this duty and the police power exception to the automatic stay, the Cabinet believes that any impact that the Frontier bond may have on its use, sale, or lease of assets, its executory contracts, and the
property of the estate are appropriate and proper. Numerous courts have noted that a
debtor-in-possession is required to operate its ongoing business in compliance with state
law. See In re Baker & Drake, Inc., 35 F.3d 1348, 1353-1354 (9th Cir. 1994); Wilner
Oil, Inc., 70 B.R. 786, 796 (Bankr. N.D. Cal. 1987); and In re Grace Coal Company, Inc.,
155 B.R. 5, 6 (Bankr. E.D. Ky. 1993).

C. **AEI Resources Holding, Inc. et al., Case Nos. 02-10150 through 02-10224**

AEI Resources Holding, Inc. and 73 of its subsidiaries (AEI) filed prepackaged
Chapter 11 Bankruptcy Petitions on February 28, 2002. One of the driving factors behind
AEI filing bankruptcy was the $533 million in Frontier bonds that AEI had
(approximately $360 million of these were reclamation bonds). AEI had been given
March deadlines by several governmental agencies including a March 1, 2002 deadline
by the Cabinet for replacing its Frontier bonds. Prior to filing its bankruptcy, AEI had
obtained commitments from companies to replace the Frontier bonds, and received
sufficient votes to get its plan confirmed by the Bankruptcy Court. On the same day that
it had filed its Bankruptcy Petitions, AEI also filed an adversary proceeding against
officials from OSM, Kentucky, Illinois, Indiana, Tennessee and West Virginia seeking a
preliminary injunction on the same basis as Lodestar had in its bankruptcy. However,
prior to the hearing on its Motion for Temporary Restraining Order, AEI reached an
agreement with all of the various government agencies giving them an additional period
of time to get the substitute bonds in place. AEI subsequently replaced all of its Frontier
bonds, and on April 17, 2002 the Bankruptcy Court entered an Order confirming its Plan
of Reorganization.
II. ACKNOWLEDGEMENTS
In the Matter of:

Frontier Insurance Company
195 Lake Louise Marie Road
Rock Hill, New York 12775-8000

ORDER SUSPENDING CERTIFICATE OF AUTHORITY

WHEREAS, KRS 304.3-190(1) empowers the Commissioner of Insurance to immediately suspend or revoke a foreign insurer’s Certificate of Authority to transact business in the Commonwealth of Kentucky, if the insurer’s Certificate of Authority is suspended or revoked by its state or country of domicile;

WHEREAS, 806 KAR 3:150 empowers the Commissioner of Insurance to immediately suspend the certificate of authority of any insurer found to be in such condition as to render the continuance of their business hazardous to policyholders, creditors or the public; and,

WHEREAS, the Supreme Court of New York, New York County, has ordered Frontier Insurance Company into rehabilitation, as of August 27, 2001.

NOW, THEREFORE, pursuant to KRS 304.190(1)(b) and (d), 806 KAR 3:150, and all other applicable law IT IS HEREBY ORDERED that:

1. The Certificate of Authority of Frontier Insurance Company to transact insurance business in Kentucky is suspended;

2. Frontier Insurance Company shall cease writing any and all new and renewal business in Kentucky;
3. All appointments of agents with Frontier Insurance Company are suspended.

Effective this 27th day of August, 2001.

JANIE A. MILLER, Commissioner
Kentucky Department of Insurance

CERTIFICATE OF SERVICE

I hereby certify that an accurate copy of this Order was served by first-class U.S. mail, postage prepaid, on:

Attn: Mark H. Mishler, Pres. and Joseph P. Loughlin, Process Agent
Frontier Insurance Company
195 Lake Louise Marie Road
Rock Hill, New York 12775-8000

Liquidation Bureau
New York Department of Insurance
160 West Broadway
New York, New York 10013

this 27th day of August, 2001.

Russell R. Coy II, Counsel
Kentucky Department of Insurance
RE: Replacement of Performance Bond Coverage
Permit Number(s) and Accompanying Frontier Insurance Company Bond Number(s):

Dear Permittee:

It has come to our attention that New York, the home state of Frontier Insurance Company, has entered an "Order of Rehabilitation" as to this insurance company. As a consequence thereof, the Kentucky Department of Insurance has suspended Frontier's Certificate of Authority to do business in the Commonwealth of Kentucky.

As a result of the incapacity of Frontier Insurance Company, the performance bond(s) which you filed for the above-referenced permit(s) is (are) inadequate and you are deemed to be without performance bond coverage. You must obtain new performance bond coverage for the above-referenced permit(s), including for all disturbances that have been made in connection with each permit. You shall continue to be responsible under the permit(s). Frontier Insurance shall continue to remain liable on the existing bond(s) until you file a new performance bond(s) with the Department for Surface Mining Reclamation and Enforcement.

This letter constitutes official notice that you must obtain new performance bond coverage within ninety (90) days from the date of this letter. Pursuant to 405 KAR 10:030, Section 2(5)(c)3, if an adequate replacement bond is not posted within ninety (90) days, you shall: 1) cease coal extraction and coal processing operations; 2) comply with the provisions of 405 KAR 16:010, Section 6 (or 405 KAR 18:010, Section 4); and 3) immediately begin to conduct reclamation operations in accordance with your reclamation plan. Coal extraction and
coal processing operations shall not resume until the Cabinet has determined that an acceptable bond has been posted. Failure to comply with these requirements will result in the issuance of a Notice of Non-Compliance or Cessation Order.

Any new performance bond(s) obtained for the above-referenced permit(s) should be filed with this office. If you have any questions, please contact Connie Downey at (502) 564 2340.

Sincerely,

Mark W. Thompson, Director
Division of Field Services

MWT/cs

x: Permit Application File
   Bond File
   Office of Legal Services
   Frontier Insurance Company
   Gregory V. Serio, Superintendent of Insurance for the State of New York
ORDER

WHEREAS, the New York Department of Insurance requested and received approval from Frontier Insurance Company's Board of Directors to proceed with voluntary rehabilitation, which action was filed into the New York Supreme Court, New York County on August 24, 2001;

WHEREAS, the New York Department of Insurance was granted temporary rehabilitation of Frontier Insurance Company on August 27, 2001, and all persons, with the exception of the New York Superintendent, were restrained from taking possession of the company's assets and transacting its business;

WHEREAS, the Kentucky Department of Insurance issued an Order suspending Frontier Insurance Company's certificate of authority to transact the business of insurance within the Commonwealth on August 27, 2001, pursuant to KRS 304.3-190 and 806 KAR 3:150; and
WHEREAS, the Petitioners herein filed a Petition for Hearing under KRS 304.2-310 on October 11, 2001;

NOW, THEREFORE, as a basis for her Order, Janie A. Miller, Commissioner, finds as follows:

1. The Petition for Hearing was not filed in good faith as it contains material misstatements of law and fact. Specifically in paragraph 7(a), Petitioners claim the Commissioner's suspension order was not issued "in accordance with KRS Chapter 304 and corresponding regulations." In fact, the statutory provision upon which the Commissioner relied in issuing her August 27th Order was KRS 304.3-190, entitled "Suspension or evocation of certificate of authority; mandatory grounds" (emphasis added.)

In paragraph 7(b), Petitioners remarkably claim that Frontier Insurance Company ("Frontier") "does not have a 'deficiency of capital or surplus,' nor is the continuance of Frontier's business in Kentucky 'hazardous to policyholders, creditors or the public' as Frontier meets minimum required capital and surplus requirements required of insurers by KRS Chapter 304 [sic] and corresponding regulations, and otherwise meets the requirement for a certificate of authority."

At the very least, a reasonable inquiry into the facts of this case and a review of public documents would evidence such a statement to be baseless in fact. Frontier was removed from the U.S. Department of Treasury's list of approved sureties, due to its financial condition, on July 1, 2000. Additionally, immediately following the seizure of Frontier by the New York Department of Insurance, the two major insurer rating agencies substantially downgraded the company. On
August 28, 2001, Standard & Poor's assigned an "R" rating to Frontier, following a Credit Watch ratings withdrawal five months earlier and based on weakened capitalization and weak earning levels. A.M. Best downgraded Frontier to an "E" rating on August 30, 2001, on the basis of poor operating results, a massive deterioration in overall capitalization and below-average liquidity, and following repeated incremental downgrades through the prior five months. Finally, the New York Department of Insurance included language in its annexed petition for rehabilitation, filed in New York County, New York, that it believed Frontier to be insolvent.

Paragraph 7(c) states that "Frontier's certificate of authority has not been 'suspended or revoked' by order of the New York Department of Insurance." Admittedly, while the New York Department of Insurance has not issued an order suspending or revoking Frontier's certificate of authority in New York, the Department has taken possession of the certificate of authority in the same manner that the Department has taken possession of every other asset of the insurer.

Finally, in paragraph 7(d), the Petitioners allege that the New York County Supreme Court has "not ordered Frontier into rehabilitation as of the date this Petition was filed." In fact, as evidenced by Petitioners' Exhibit 1 to the Petition, the Supreme Court of New York County, New York, has appointed the New York Superintendent as temporary rehabilitator of Frontier as of August 27, 2001, and in compliance with §7409 of the New York Insurance Law, as the proper manner...
to commence delinquency proceedings against an insurer within the state of New York.

2. The Petitioners are not “aggrieved persons” as contemplated by KRS 304.2-310(2)(b) and the Commissioner of Insurance is without the authority to grant the relief requested by the Petitioners in the event they should successfully prove their specious allegations. As the sole basis for considering themselves to be “aggrieved” by the Commissioner’s order suspending Frontier’s certificate of authority, the Petitioners state that replacement coverage, as required by the Natural Resources & Environmental Protection Cabinet, will be more costly or require collateral not presently required by Frontier.

The fact that a policyholder finds substitute coverage to be available at a higher premium or collateral amount does not constitute a basis for considering the person to be “aggrieved” under KRS 304.2-310(2)(b) and therefore eligible to request an administrative hearing on the Commissioner’s order and postpone the effective date of the company’s suspension. In fact, these “aggrieved” Petitioners are precisely the consumers to be protected from the issuance of the Commissioner’s suspension order to Frontier. If replacement coverage is priced at premium and collateral levels substantially different than was required by Frontier, the value of the present coverage should be somewhat suspect. Clearly, if Frontier is, or is found to be, insolvent, the coverage provided by Frontier has only minimal value.

The seizure by New York, coupled with the Kentucky Department’s knowledge regarding the seriously hazardous financial condition of the company,
required the Commissioner to suspend the certificate of authority issued to Frontier in Kentucky. Although this action is alleged to have "aggrieved" the Petitioners, it was designed to allow policyholders to quickly replace their coverage prior to the occurrence of a claim that could not be adequately covered by Frontier. Also, the Kentucky Department of Insurance undertook all incremental action possible, issuing an Agreed Order to cease writing all new business on June 28, 2000, and an Order to cease writing all renewal business, with the exception of in-force non-cancelable bonds, on March 28, 2001. Accordingly, policyholders of Frontier had more than seventeen months notice that the Kentucky Department was concerned about Frontier and they should consider replacing their coverage.

Even assuming the Petitioners are truly "aggrieved," the Kentucky Department of Insurance has yet to require the replacement of the Petitioner's bonds issued by Frontier. If the Petitioners are "aggrieved" by any action described in their Petition, it would necessarily be the action of the Natural Resources & Environmental Protection Cabinet in requiring the Frontier bonds to be replaced within ninety days, an action outside the purview of the Commissioner of Insurance. Accordingly, in the event the Petitioners were successful in proving each allegation contained in their Petition, the Commissioner is without the authority to obviate the replacement requirement issued by the Natural Resources cabinet pursuant to its regulatory authority.

3. KRS 304.2-310(2)(b) is not applicable to the suspension of certificates of authority as the controlling statute is KRS 304.3-190(2), which
limits the entity eligible to appeal an insurer's certificate suspension to be only the insurer. Additionally, KRS 304.3-190(2) further limits an insurer's ability to request an administrative hearing on its suspension to within twenty days of its notice as provided by the Department of Insurance in cases without an impairment of capital or surplus. Therefore, as KRS 304.2-310(2)(b) specifically states:

Any application for a hearing shall be filed in the department within sixty (60) days after the person knew or reasonably should have known, of the act, threatened act, failure, report, administrative regulation, or order, unless a different period is provided for by other laws applicable to the particular matter, in which case the other law shall govern

(emphasis added.)

As the language contained in KRS 304.2-310(2)(b) clearly defers to a more specific statute on the matter, KRS 304.3-190 controls in this instance. Accordingly, only an insurer is eligible to request an administrative hearing on the suspension of its certificate of authority, and as Frontier, under the management and control of the New York Department, has failed to do so, a mere policyholder is not entitled to delay the effective date of the suspension on the basis that it believes itself to be "aggrieved."

In addition, the Commissioner has discretion to suspend Frontier's certificate of authority, without any notice or hearing, pendent to the action of the New York Department, according to KRS 304.2-200(4).
THEREFORE, pursuant to KRS 304.2-065, KRS 304.2-310(4), KRS 304.3-190(2), KRS 304.99-015, 806 KAR 3:150, and all other applicable law, it is hereby ORDERED that the Petition for Hearing filed on behalf of Branham & Baker Coal Company, Panther Land Corporation, and Millard Processing Corporation is DENIED.

This is a final and appealable Order, with no just cause for delay.

Done and effective this 13 day of October, 2001.

JANIE A. MILLER, COMMISSIONER
Kentucky Department of Insurance

Certificate of Service

I certify that a copy of the foregoing Order was served, via U.S. mail, postage prepaid, on this 15th day of October, 2001, upon:

Martin J. Cunningham
Barbara Reid Hartung
Kelly A. Dant
Greenebaum Doll & McDonald PLLC
333 West Vine Street, Suite 1400
Lexington, KY 40601
William T. Gorton III
Frontier Insurance Company
Stites & Harbison
250 West Main Street, Suite 2300
Lexington, KY 40507

Liquidation Bureau
New York Department of Insurance
160 West Broadway
New York, New York 10013

[Signature]

Julie Mix McPeak
Interim General Counsel
WHEREAS, the New York Department of Insurance requested and received approval from Frontier Insurance Company's Board of Directors to proceed with voluntary rehabilitation, which action was filed into the New York Supreme Court, New York County on August 24, 2001;

WHEREAS, the New York Department of Insurance was granted temporary rehabilitation of Frontier Insurance Company ("Frontier") on August 27, 2001, and all persons, with the exception of the New York Superintendent, were restrained from taking possession of the company's assets and transacting its business;

WHEREAS, the Kentucky Department of Insurance issued an Order suspending Frontier Insurance Company's certificate of authority to transact the business of insurance within the Commonwealth on August 27, 2001, pursuant to KRS 304.3-190 and 806 KAR 3:150;
WHEREAS, the Superintendent of the New York Department of Insurance was named Rehabilitator of Frontier by the New York County Supreme Court on October 15, 2001; and

WHEREAS, Petitioner herein filed a Petition for Hearing under KRS 304.2310 on October 26, 2001;

NOW, THEREFORE, as a basis for her Order, Janie A. Miller, Commissioner, finds as follows:

1. The Petition for Hearing does not challenge the Commissioner's authority and obligation to enter the Order of Suspension regarding Frontier, only the effect and interpretation of the Order of Suspension.

2. The Commissioner has neither interpreted the Order of Suspension to require Frontier to cancel the insurance policies and bonds presently in-force, nor has the Commissioner required any policyholder or bondholder of Frontier to replace its coverage with another carrier.

3. By letter dated November 2, 2001, the Kentucky Department of Insurance has notified Frontier, through its rehabilitator, that it acknowledges the Order of Rehabilitation entered by the New York County Supreme Court. Further, the Department recognizes that it is precluded from taking any enforcement action against Frontier pursuant to the rehabilitation order, should the company choose to collect premium from Kentucky insureds during the period of suspension. A copy of the Department's letter to Frontier is attached as Exhibit 1.
4. Petitioner's request for an administrative hearing was premised on the Department's interpretation of Frontier's suspension order and the interpretation has been resolved as requested by the Petitioner.

Now, THEREFORE, pursuant to KRS 304.2-065, KRS 304.2-310(4), KRS 304.3-190(2), KRS 304.99-015, 806 KAR 3:150, and all other applicable law, it is hereby ORDERED that the Petition for Hearing filed on behalf of AEI Resources is DENIED.

This is a final and appealable Order, with no just cause for delay.

Done and effective this 2nd day of November, 2001.

[Signature]
JANIE A. MILLER, COMMISSIONER
Kentucky Department of Insurance

Certificate of Service

I certify that a copy of the foregoing Order was served, via U.S. mail, postage prepaid, on this 2nd day of November, 2001, upon:

Denise H. McClelland
Frost Brown Todd LLC
2700 Financial Center
Lexington, KY 40507-1749

And
Janet Craig  
William T. Gorton III  
Frontier Insurance Company  
Stites & Harbison  
250 West Main Street, Suite 2300  
Lexington, KY 40507

[Signature]
Julie Mix McPeak  
Interim General Counsel
SURVEY OF LOCAL GOVERNMENTAL ENVIRONMENTAL REGULATIONS

Patricia L. Dugger
Director, DEEM
Lexington Fayette Urban County Government
Lexington, Kentucky

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SECTION F
Introduction
- Who has local environmental laws
- What type of issues are regulated at the local level
- Why regulate environmental issues at the local level

Overview
- Many local jurisdictions are wanting to have input in various issues that directly affect their communities
- It is important to understand what communities feel are important to them and what the impact of complying with these ordinances mean
- Examples of what is out there at the local level
Local Jurisdictions with Environmental Laws
- Owensboro
- Paducah
- Hopkinsville
- Florence
- Covington
- Boone County

Local Jurisdictions with Environmental Laws
- Northern KY
- Louisville
- Ohio River
- Lexington
- County health departments with an environmental section

Owensboro
- Stormwater Drainage Municipal Code
  Chapter 26 Article VII
  - Certain acts or conditions that affect stormwater
  - Obstructions and or encroachments
  - Definitions
  - Penalties

SURVEY OF LOCAL GOVERNMENTAL ENVIRONMENTAL REGULATIONS
Owensboro

  Chapter 10 Article III
  - Definitions
  - Preplanning
  - Temporary storage
  - Handler or user responsibility

Chapter XII Fire Prevention Storage of Hazardous Substances and response to

Chapter XXIII Water and Sewer

Chapter XXVI Public Trees
  - Community Tree Advisory Board
  - Tree topping, maintenance and removal

Chapter XXI Streets and Sidewalks
  - Control of erosion and filling or obstruction of natural drainage crevices
  - Sinkholes, ditches and known subterranean water channels

SURVEY OF LOCAL GOVERNMENTAL ENVIRONMENTAL REGULATIONS
Paducah
- Vegetation Chapter 118 Article II
  - Trees on public property
  - City Forester
  - Street tree species and spacing
  - Public tree care, topping, pruning
  - License of tree care business
  - Appeals

Hopkinsville
- Land Usage Title XV
- Chapter 155 Stormwater Management and Control
  - Sinkhole
  - Subterranean
  - Water Channels
  - Requirements for developers

Ohio River
- Ohio River Valley Water Sanitation Commission
- Compact signed in 1948 by the governors of Illinois, Indiana, Kentucky, New York, PA. Virginia, Ohio and West Virginia
- Purpose: To ensure that all waters in the district be placed and maintained in a satisfactory, sanitary condition, available for certain beneficial uses

SURVEY OF LOCAL GOVERNMENTAL ENVIRONMENTAL REGULATIONS
Louisville

- Metropolitan Sewer District (MSD)
  - Wastewater Discharge Regulations
  - Hazardous Materials Ordinance
  - Industrial Compliance and Monitoring
  - Water Quality
  - Erosion Prevention & Sediment Control Ordinance

Louisville MSD

- Hazardous Materials Title IX Chapter 99
  - Definitions
  - Reporting requirements
  - Notification,
  - Cleanup
  - Enforcement
  - Penalties

Louisville

- Development Code (Zoning and Subdivision regulations)
- Currently in the process of reviewing and updating the code to be in compliance with the 2020 Comprehensive Land Use Plan
- Land Development Code Oversight Committees is overseeing the process of revising the code
- Code revisions will be release in sections and each will have a public hearing
- Environmental assessment for development on environmentally constrained sites

SURVEY OF LOCAL GOVERNMENTAL ENVIRONMENTAL REGULATIONS
Development on steep slopes and unstable soil
- Tree canopy regulations
- Outdoor Lighting

Louisville
- Air Pollution Control District
- > 50 years, Citizen board appointed by Mayor and County Judge
- Goals:
  - to ensure healthy air
  - assist local entities to meet air emission standards
- Responsibilities:
  - Permits
  - Monitoring, Louisville
- Air Pollution control District

City of Florence
- Trees Title IX Chapter 99
  - Definition
  - Permissions
  - Exceptions
  - Review of development plans
  - Notification of tree injury
  - Tree planting criteria
  - Tree classifications, penalties
  - Establishment of Urban Forest Commission
City of Florence

- Public Works Title V
  - Provide for use, possession and control of all storm and surface water drainage facilities
  - Maintenance, operation and management of said system
  - Establish a reasonable Storm Water Service Charge

Boone County

- Hazardous Materials Title IX Chapter 95
  - Definitions
  - Reportable quantities
  - Permit for a release
  - Notification and response authority
  - Liability for costs, confidential information
  - Inspections, enforcement

Covington

- Sanitation and Health
  - Uniform litter control
  - Transportation of hazardous waste
  - Hazardous materials spills
- Zoning Code
  - Excavation, movement of soil, tree removal, erosion and sedimentation control
Northern Kentucky

- Boone, Campbell and Kenton Counties
- Vehicle Emissions Testing Program
  - Began in Sept. 1999
  - Deal with ground level ozone or smog
  - Testing is required every other year
  - Exempt vehicles < 1968, alternately fueled vehicles, gross vehicle weight > 18,000 lbs.
  - Cost $20

Lexington - Fayette County

- Hazardous Materials Ordinance Chapter 16A
  - UGST regulations for petroleum
  - USGT for nonpetroleum
  - UGST for farm petroleum tanks
- Mining and Quarrying
- Public Nuisances
- Sewage, Garbage, Refuse and Weeds
Many locales have environmental ordinances or regulations. Look in unusual areas. Talk to health depts, building inspectors, zoning commissions, and others to determine if local regulations exist.
Where to Get More Information

- Search any municipality Code of Ordinances for the following key words:
  - Environment
  - Hazardous
  - Trees
  - Sinkholes
  - Erosion
SMART GROWTH ISSUES

Lloyd R. ("Rusty") Cress, Jr.
Greenebaum Doll & McDonald PLLC
Frankfort and Lexington, Kentucky

Deborah A. Bilitski
Assistant Jefferson County Attorney
Louisville, Kentucky

Robert M. Weiss
Homebuilders Association of Kentucky
Frankfort, Kentucky

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SECTION G
REDEVELOPING BROWNFIELDS:
Smart Growth Tools In Kentucky

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SECTION G(a)
REDEVELOPING BROWNFIELDS: SMART GROWTH TOOLS IN KENTUCKY

The Kentucky Voluntary Environmental Remediation Act ("VERA") was passed by the 2001 General Assembly. The bill establishes a much needed "Brownfields/Voluntary Remediation" program, which will foster environmental cleanup and spur redevelopment of idled and abandoned properties.

I. Purpose.

A. The law states that it is "intended to establish an efficient and predictable process . . . to promote voluntary cleanup and redevelopment of properties suspected of environmental contamination . . . while stimulating economic development and job creation through the construction of new residential, commercial, and industrial facilities." KRS 224.01-510.

B. The law creates a "shell" within which existing environmental remediation statutes may be inserted, and, if followed, results in the issuance of a covenant not to sue.

II Benefits of New Program.

A. Voluntary Environmental Remediation Program ("VERP") provides property owners with certainty in:

1. Natural Resources and Environmental Protection Cabinet remediation time lines; and,

2. Level of comfort following completion of remediation activities, without stymieing remediation management at site.

B. Does not create new technical requirements – merely a process for receiving a covenant not to sue.

III Existing Remedial Statutes.

A. KRS 224.01-400.

1. Any person possessing or controlling a hazardous substance, pollutant, or contaminant which is released to the environment, or any person who caused a release to the environment of a hazardous substance, pollutant, or contaminant, shall characterize the extent of the release as necessary to determine the effect of the release on the environment, and shall take actions necessary to correct the effect of the release on the environment.
2. Four options:
   a. Demonstrating that no action is necessary to protect human health, safety, and the environment;
   b. Managing the release in a manner that controls and minimizes the harmful effects of the release and protects human health, safety, and the environment, provided that the management may include any existing or proposed engineering or institutional controls and the maintenance of those controls;
   c. Restoring the environment through the removal of the hazardous substance pollutant or contaminant; or,
   d. Any combination of paragraphs (a), (b), and (c).

3. No real finality associated with final determination.

B. KRS 224.01-405.

1. For releases of petroleum or petroleum products from sources other than petroleum storage tanks, any person who owns or operates the source from which the release occurred or any person who caused the release shall characterize the extent of the release as necessary to determine the effect of the release on the environment and shall perform corrective action.

2. Corrective action means those actions necessary to protect human health, safety, and the environment, and includes: remedial actions to clean up contaminated media; actions to address residual effects after initial corrective action is taken; actions to restore or replace potable water supplies; and actions necessary to monitor, assess, and evaluate a release, as well as actions necessary to monitor, assess, and evaluate the effectiveness of remedial action.

3. Until regulations are promulgated, same options available under KRS 224.01-400 are available.

4. No real finality.

C. Historical effort to provide finality – 224.01-450 - 465.

1. In 1996, the legislature created a law providing for the issuance of a No Further Remediation Letter to a public entity for a site when a remediation plan has been successfully completed.
2. Letter intended to signify a release from further responsibilities for a remediation plan approved under KRS 224.01-460 and any further responsibilities under KRS 224.01-400 to undertake any other remedial action on the site.

3. Well-intended, but ineffective – not available for private lands and scarcely utilized by public entities.

IV 2001 Senate Bill 2 (Codified at KRS 224.01-510 - 532).

A. Establishes VERP – applies to sites under KRS 224.01-400 and KRS 224.01-405.

B. Ineligible sites.

1. The property is part of or contains a site which is on the National Priorities List established by the United States Environmental Protection Agency;

2. The property is part of or contains a hazardous waste treatment, storage, or disposal facility for which a permit has been issued, or the site is otherwise the subject of hazardous waste closure or corrective action pursuant to KRS 224.46-520 or KRS 224.46-530;

3. The property or site is the subject of state or federal environmental enforcement action relating to the release, for which the application is submitted; or

4. The property or site presents an environmental emergency, as defined in KRS 224.01-400.

C. Program requirements.

1. Application must include:

   a. Form provided on Superfund Branch web page (http://www.nr.state.ky.us/nrepc/dep/waste/programs/sf/vcpguide.htm)

   b. Filing fee:

      i. Site size up to 3 acres = $1,000.

      ii. Site size 3 - 10 acres = $2,500.

      iii. Site size greater than 10 acres = $3,500.
iv. Possible fee waiver.

c. Characterization Plan – Identify any hazardous substance and any petroleum released or believed to be released to the environment at the site and provide a characterization plan for the releases or threatened releases adequate to comply with KRS 224.01-400, 224.01-405, 224.01-510 to 224.01-532, and any administrative regulations promulgated pursuant thereto.

d. Public notice.

i. Upon filing of application, the applicant shall notify the chief executive of local governmental units in which the property or site that is the subject of the application is located and shall provide the chief executives with a copy of the application.

ii. Publish notice of the application in the newspaper of largest circulation in the county in which the site is located.

e. NREPC time for approval or disapproval – 45 days.

2. Voluntary Remediation Agreed Order includes:

a. Agreement to identify and characterize releases at site and submit characterization report.

b. Agreement to submit corrective action plan and final report which certifies that the work has been completed in accordance with the Corrective Action Plan.

c. Listing of costs to be reimbursed to cabinet for oversight and review and a payment schedule (costs must be reasonable, actual, and necessary).

d. Definite remediation schedule.

e. Agreement that applicant may withdraw from agreed order prior to issuance of covenant not to sue (must pay Cabinet costs).

f. Other provisions necessary to protect human health and the environment.
3. Work plans set forth in Agreed Order must be completed.
   a. Submittal of Site Characterization Report and Corrective Action Plan (120 days from entry of Agreed Order) – Site characterization and corrective action must comply with KRS 224.01-400 and KRS 224.01-405.
   b. Must include plan of action to inform public of remediation and provide for public comment.
   c. NREPC review of plan (120 days).
   d. Reasons Cabinet may disapprove Corrective Action Plan:
      i. Failure to comply with KRS 224.01-400 and KRS 224.01-405.
      ii. Failure to respond to request for information.
   e. Implementation of plan on approved schedule.

4. Public notice and participation (includes notice of activities, availability of information, and opportunity for comment).
   a. Publish notice of application in newspaper.
   b. Notification to local government unit officials of filing of application, along with providing copy of application.
   c. Notification to local government unit of corrective action plan.
   d. Publish notice of Corrective Action Plan and request for comment in newspaper.
   e. 30-day comment period and possible public hearing.
   f. Property sign stating that property is undergoing remediation and location of information.
g. Documents to be maintained in local public library:
   i. Agreed Order;
   ii. Characterization Plan;
   iii. Characterization Report;
   iv. Corrective Action Plan;
   v. Corrective Action Completion Report;
   vi. Notices of Deficiency and responses thereto;
   vii. Covenant not to sue.

D. Covenant not to sue.

1. Covers releases identified in Corrective Action Plan for:
   a. No further remediation.
   b. Prosecution of civil or administrative enforcement for:
      i. Failure to perform remediation under state and federal law;
      ii. Injunctive relief;
      iii. Lien assertion;
      iv. Reimbursement of costs;
      v. Civil penalties.

2. Does not cover:
   a. Releases not identified in Corrective Action Plan;
   b. Failure to comply with Agreed Order or plans required;
   c. Exacerbation of releases;
   d. Criminal liability;
   e. Underground storage tanks;
f. Misrepresentation or intentional omissions;

g. Conditions not known to the Cabinet which prevent remedy from being protective;

h. Changes in scientific knowledge indicating that remedy is no longer protective;

i. Environmental emergencies;

j. Natural Resource Damages under CERCLA.

E. Screening levels and remediation standards (applicable to all sites, whether participating in VERP or not).

1. Use of U.S. EPA Region 9 Preliminary Remediation Goals as screening levels.

2. Promulgation of remediation standards.
   a. Residential “walk-away” standards.
   b. Tiered remediation standards based upon land use.
   c. Continued availability of existing standards and procedures.

F. Moneys expended under program are qualifying costs under:

1. Economic development laws;

2. Infrastructure projects.

G. Agricultural Warehousing Sites Cleanup Fund

1. Creates “The Agricultural Warehousing Sites Cleanup Fund” to be administered by the Cabinet for Economic Development.

2. The purpose of the agricultural warehousing sites cleanup fund is to provide financial assistance to persons who did not cause or contribute to the contamination on property used for agricultural warehousing activity, and who propose to undertake a voluntary cleanup of the property.
3. The financial assistance shall be in an amount of up to seventy-five percent (75%) of the costs incurred for completing an environmental study and implementing a cleanup plan by an eligible applicant.

4. Financial assistance may be in the form of grants or low-interest loans, to be lent at a rate not to exceed two percent (2%).

5. Loans may be made to the following categories of applicants:
   a. Local economic development agencies;
   b. Political subdivisions or their instrumentalities; and
   c. Other persons determined to be eligible by the Cabinet for Economic Development.

6. The Cabinet for Economic Development is required to take all of the following factors into consideration when determining which applicants shall receive financial assistance:
   a. The benefit of the remedy to human health, safety, and the environment;
   b. The permanence of the remedy;
   c. The cost-effectiveness of the remedy in comparison with other alternatives;
   d. The financial condition of the applicant;
   e. The financial or economic distress of the area in which the cleanup is being conducted; and
   f. The potential for economic development.

7. Loans may be made based upon the ability to repay from future revenue to be derived from the cleanup, by a mortgage or other collateral, or on any other fiscal matters which the Cabinet for Economic Development deems appropriate.
CONSERVATION EASEMENTS

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SECTION G(b)
Conservation Easements

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Conservation easements in general.

KRS 382.800(1) defines a conservation easement as “a nonpossessory interest of a holder in real property imposing limitations or affirmative obligations, the purposes of which include retaining or protecting natural, scenic, or open-space values of real property, assuring its availability for agricultural, forest, recreational, or open-space use, protecting natural resources, maintaining or enhancing air or water quality, or preserving the historical, architectural, archaeological, or cultural aspects of real property.”

A “holder” is defined as “(a) A governmental body empowered to hold an interest in real property under the laws of this state or the United States; or (b) A charitable corporation, charitable association, or charitable trust, the purposes or powers of which include retaining or protecting the natural, scenic, or open-space values of real property, assuring the availability of real property for agricultural, forest, recreational, or open-space use, protecting natural resources, maintaining or enhancing air or water quality, or preserving the historical, architectural, archaeological, or cultural aspects of real property.” KRS 382.800(2)

Two valuable uses of a conservation easement.

- Land conservation
- Estate planning/tax benefits

In order to qualify for federal tax benefits, a conservation easement must meet the requirements of §170(h) of the Internal Revenue Code:

1. A “qualified conservation contribution” means a contribution –
   
   (A) of a qualified real property interest,
   (B) to a qualified organization,
   (C) exclusively for conservation purposes.
(2) A qualified real property interest means any of the following:

(A) the entire interest of the donor other than a qualified mineral interest,
(B) a remainder interest, and
(C) a restriction granted in perpetuity on the use which may be made of the real property.

(3) A qualified organization means generally a governmental entity or a 501(c)(3) charitable organization in the conservation or historic preservation field (see §170(h)(3) for specific provisions).

(4) Conservation purpose means -

(A) (i) the preservation of land for outdoor recreation by, or the education of, the general public,

(ii) the protection of a relatively natural habitat of fish, wildlife, or plants or similar ecosystem,

(iii) the preservation of open space (including farmland or forest land) where such preservation is for the scenic enjoyment of the general public, or pursuant to a clearly delineated Federal, State, or local governmental conservation policy, and will yield a significant public benefit, or

(iv) the preservation of an historically important land area or a certified historic structure.

(5) A contribution of a conservation easement shall not be treated as exclusively for conservation purposes unless the conservation purpose is protected in perpetuity.

**Tax Benefits.**

**Income tax deduction:** A charitable deduction on income tax may be taken for the gift of a conservation easement that meets the requirements of §170(h) of the Internal Revenue Code up to 30% of donor’s income for the year (5-year carryforward).

- In addition to the income tax benefit of donating a qualified conservation easement, the donor’s estate tax will be less because the value of the land included in the decedent’s estate is reduced by the value of the conservation easement.
- In the case of conservation contributions made after February 13, 1986, no deduction will be permitted under §170 for an interest in property which is subject to a mortgage unless the mortgagee subordinates its rights in the property to the
right of the qualified organization to enforce the conservation purposes of the gift in perpetuity.” Treas. Reg. §1.170A-14(g)(2).

**Estate tax deduction:** If a conservation easement is donated by will or the executor is authorized by will to donate an easement, a deduction on federal estate taxes may be taken for the gift of a conservation easement that meets the requirements of §170(h). See §2055(f). A gift by will is fully deductible, not subject to the 30% of income rule.

**Additional estate tax benefit - §2031(c):** Up to 40% of the value of land subject to conservation easement may be excluded from the decedent’s estate if the easement meets the requirements of §2031(c) of the Internal Revenue Code.

1. Land must be located in or within 25 miles of an area which is a metropolitan area (as defined by the Office of Management and Budget) or a National Park or Wilderness Area, or within 10 miles of an Urban National Forest (as designated by the Forest Service).
2. The easement must meet the requirements of §170(h).
3. The land must be owned by the decedent or a member of the decedent’s family for at least 3 years immediately prior to the decedent’s death.
4. The easement must have been donated by the decedent or a member of the decedent’s family or the executor.
5. The easement must prohibit more than a de minimus use for a commercial recreational activity.

**Valuation of the gift of a conservation easement.**

The value of the charitable contribution of a conservation easement is the fair market value of the conservation restriction at the time of the contribution. Treas. Reg. §1.170A-14(h)(3)(i).

1. If there is a substantial record of sales of easements comparable to the donated easement (such as purchases pursuant to a governmental program), the fair market value of the donated easement is based on the sales prices of such comparable easements. Id.
2. If no substantial record of market-place sales is available to use as a valid comparison, as a general rule the fair market value of a perpetual conservation restriction is equal to the difference between the fair market value of the property it encumbers before the granting of the restriction and the fair market value of the encumbered property after the granting of the restriction. Id.
If, as a result of the donation of a perpetual conservation restriction, the donor or a related person receives, or can reasonably expect to receive, financial or economic benefits that are greater than those that will inure to the general public from the transfer, no deduction is allowable under §170. Thus, a deduction most likely will not be allowed to a developer who donates an easement in exchange for, or as a condition to, development approval. Id.
382.800 Definitions.
As used in KRS 382.810 to 382.860, unless the context otherwise requires:
(1) "Conservation easement" means a nonpossessory interest of a holder in real property imposing limitations or affirmative obligations, the purposes of which include retaining or protecting natural, scenic, or open-space values of real property, assuring its availability for agricultural, forest, recreational, or open-space use, protecting natural resources, maintaining or enhancing air or water quality, or preserving the historical, architectural, archaeological, or cultural aspects of real property.
(2) "Holder" means:
(a) A governmental body empowered to hold an interest in real property under the laws of this state or the United States; or
(b) A charitable corporation, charitable association, or charitable trust, the purposes or powers of which include retaining or protecting the natural, scenic, or open-space values of real property, assuring the availability of real property for agricultural, forest, recreational, or open-space use, protecting natural resources, maintaining or enhancing air or water quality, or preserving the historical, architectural, archaeological, or cultural aspects of real property.
(3) "Third-party right of enforcement" means a right provided in a conservation easement to enforce any of its terms granted to a governmental body, charitable corporation, charitable association, or charitable trust, which, although eligible to be a holder, is not a holder.

Effective: July 15, 1988

382.810 Creation -- Acceptance and recordation necessary -- Duration -- Preexisting property interest.
(1) Except as otherwise provided in KRS 382.810 to 382.860, a conservation easement may be created, conveyed, recorded, assigned, released, modified, terminated, or otherwise altered or affected in the same manner as other easements.
(2) No right or duty in favor of or against a holder and no right in favor of a person having a third-party right of enforcement shall arise under a conservation easement before its acceptance by the holder and a recordation of the acceptance.
(3) Except as provided in KRS 382.820(2), a conservation easement shall be unlimited in duration unless the instrument creating it otherwise provides.
(4) An interest in real property in existence at the time a conservation easement is created shall not be impaired by it unless the owner of the interest is a party to the conservation easement or consents to it.

Effective: July 15, 1988

382.820 Actions affecting easements.
(1) An action affecting a conservation easement may be brought by:
(a) An owner of an interest in the real property burdened by the easement;
(b) A holder of the easement;
(c) A person having a third-party right of enforcement; or
(d) A person authorized by other law.
(2) KRS 382.810 to 382.860 shall not affect the power of a court to modify or terminate a conservation easement in accordance with the principles of law and equity.

Effective: July 15, 1988

382.830 Validity of easement.
A conservation easement shall be valid even though:
(1) It is not appurtenant to an interest in real property;
(2) It can be or has been assigned to another holder;
(3) It is not of a character that has been recognized traditionally at common law;
(4) It imposes a negative burden;
(5) It imposes affirmative obligations upon the owner of an interest in the burdened property or upon the holder;
(6) The benefit does not touch or concern real property; or
(7) There is no privity of estate or of contract.

Effective: July 15, 1988

382.840 Applicability and effect.
(1) KRS 382.800 to 382.860 shall apply to any interest created after July 15, 1988, which complies with KRS 382.800 to 382.860, whether designated as a conservation easement or as a covenant, equitable servitude, restriction, easement, or otherwise.
(2) KRS 382.800 to 382.860 shall apply to any interest created before July 15, 1988, if it would have been enforceable had it been created after July 15, 1988, unless retroactive application contravenes the constitution or laws of this state or the United States.
(3) KRS 382.800 to 382.860 shall not invalidate any interest, whether designated as a conservation or preservation easement or as a covenant, equitable servitude, restriction, easement, or otherwise, that is enforceable under other law of this state.

Effective: July 15, 1988

382.850 Transfer of easement -- Effect on mining operations and on eminent domain powers.
(1) A conservation easement shall not be transferred by owners of property in which there are outstanding subsurface rights without the prior written consent of the owners of the subsurface rights.
(2) A conservation easement shall not operate to limit, preclude, delete or require waivers for the conduct of coal mining operations, including the transportation of coal, upon any part or all of adjacent or surrounding properties; and shall not operate to impair or restrict any right or power of eminent domain created by statute, and all such rights and powers shall be exercisable as if the conservation easement did not exist.

Effective: July 15, 1988

382.860 Application and construction -- Uniformity of interpretation.
KRS 382.800 to 382.860 shall be applied and construed to effectuate its general purpose to make uniform the laws with respect to conservation easements among states enacting them.
382.990 Penalties.

(1) Any grantor of a deed or any holder of a note who lodges for record a deed, instrument, or deed assigning a note or a deed of release or an instrument wherein there is a release, and any county clerk or deputy county clerk who receives and permits to be lodged for record any such instrument or deed contrary to the provisions of KRS 382.110, 382.120, 382.290, or 382.360, shall be guilty of a violation; the clerk or deputy who actually receives and files the instrument for record shall incur the penalty, but no clerk or deputy shall be fined because of any false or erroneous statement in the instrument filed.

(2) Any person who willfully and fraudulently makes affidavit to any statement mentioned in KRS 382.120, which is false, knowing the statement to be false, shall be guilty of a Class A misdemeanor, and in addition shall be liable to any person who may be injured by the making, filing, recording, or use of the affidavit.

(3) Any person who causes to be recorded in a county clerk's office a deed, deed of trust, or mortgage in violation of KRS 382.330, or fails to file the statement required by KRS 382.380, shall be guilty of a Class A misdemeanor.

(4) Any county clerk who records a deed or mortgage in violation of KRS 382.330 shall be guilty of a violation.

(5) Any county clerk who, by himself or deputy, fails to perform any duty enjoined upon him by any of the provisions of KRS 382.110, 382.160, 382.180 to 382.200, 382.210, 382.250, 382.300 to 382.320, 382.360, or 382.370 shall be guilty of a violation.

(6) Any person who knowingly and intentionally gives a false name or address in any instrument or assignment mentioned in KRS 382.430, shall be guilty of a Class A misdemeanor.

(7) Any county clerk who fails to perform his duties under KRS 382.430, shall be guilty of a violation.

(8) Any person who willfully and fraudulently gives a false statement as to the full actual consideration of property or the full estimated value under KRS 382.135, shall be guilty of a Class D felony.

Effective: July 14, 1992

Sec. 170. - Charitable, etc., contributions and gifts

(h) Qualified conservation contribution

(1) In general

For purposes of subsection (f)(3)(B)(iii), the term "qualified conservation contribution" means a contribution -

(A) of a qualified real property interest,

(B) to a qualified organization,

(C) exclusively for conservation purposes.

(2) Qualified real property interest

For purposes of this subsection, the term "qualified real property interest" means any of the following interests in real property:

(A) the entire interest of the donor other than a qualified mineral interest,

(B) a remainder interest, and

(C) a restriction (granted in perpetuity) on the use which may be made of the real property.

(3) Qualified organization

For purposes of paragraph (1), the term "qualified organization" means an organization which -

(A) is described in clause (v) or (vi) of subsection (b)(1)(A), or

(B) is described in section 501(c)(3) and -

(i) meets the requirements of section 509(a)(2), or (ii) meets the requirements of section 509(a)(3) and is controlled by an organization described in subparagraph (A) or in clause (i) of this subparagraph.

(4) Conservation purpose defined
(A) In general

For purposes of this subsection, the term "conservation purpose" means -

(i) the preservation of land areas for outdoor recreation by, or the education of, the general public,

(ii) the protection of a relatively natural habitat of fish, wildlife, or plants, or similar ecosystem,

(iii) the preservation of open space (including farmland and forest land) where such preservation is -

(I) for the scenic enjoyment of the general public, or

(II) pursuant to a clearly delineated Federal, State, or local governmental conservation policy, and will yield a significant public benefit, or

(iv) the preservation of an historically important land area or a certified historic structure.

(B) Certified historic structure

For purposes of subparagraph (A)(iv), the term "certified historic structure" means any building, structure, or land area which -

(i) is listed in the National Register, or

(ii) is located in a registered historic district (as defined in section 47(c)(3)(B)) and is certified by the Secretary of the Interior to the Secretary as being of historic significance to the district.

A building, structure, or land area satisfies the preceding sentence if it satisfies such sentence either at the time of the transfer or on the due date (including extensions) for filing the transferor's return under this chapter for the taxable year in which the transfer is made.

(5) Exclusively for conservation purposes

For purposes of this subsection -

(A) Conservation purpose must be protected

A contribution shall not be treated as exclusively for conservation purposes unless the conservation purpose is protected in perpetuity.

(B) No surface mining permitted
(i) In general

Except as provided in clause (ii), in the case of a contribution of any interest where there is a retention of a qualified mineral interest, subparagraph (A) shall not be treated as met if at any time there may be extraction or removal of minerals by any surface mining method.

(ii) Special rule

With respect to any contribution of property in which the ownership of the surface estate and mineral interests has been and remains separated, subparagraph (A) shall be treated as met if the probability of surface mining occurring on such property is so remote as to be negligible.

(6) Qualified mineral interest

For purposes of this subsection, the term "qualified mineral interest" means -

(A) subsurface oil, gas, or other minerals, and

(B) the right to access to such minerals.
Sec. 2031. - Definition of gross estate

(a) General

The value of the gross estate of the decedent shall be determined by including to the extent provided for in this part, the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated.

(b) Valuation of unlisted stock and securities

In the case of stock and securities of a corporation the value of which, by reason of their not being listed on an exchange and by reason of the absence of sales thereof, cannot be determined with reference to bid and asked prices or with reference to sales prices, the value thereof shall be determined by taking into consideration, in addition to all other factors, the value of stock or securities of corporations engaged in the same or a similar line of business which are listed on an exchange.

(c) Estate tax with respect to land subject to a qualified conservation easement

(1) In general

If the executor makes the election described in paragraph (6), then, except as otherwise provided in this subsection, there shall be excluded from the gross estate the lesser of -

(A) the applicable percentage of the value of land subject to a qualified conservation easement, reduced by the amount of any deduction under section 2055(f) with respect to such land, or

(B) the exclusion limitation.

(2) Applicable percentage

For purposes of paragraph (1), the term "applicable percentage" means 40 percent reduced (but not below zero) by 2 percentage points for each percentage point (or fraction thereof) by which the value of the qualified conservation easement is less than 30 percent of the value of the land (determined without regard to the value of such easement and reduced by the value of any retained development right (as defined in paragraph (5)).

(FOOTNOTE 1) So in original. No closing parenthesis was enacted.

(3) Exclusion limitation
For purposes of paragraph (1), the exclusion limitation is the limitation determined in accordance with the following table: In the case of estates of The exclusion decedents dying during: limitation is: 1998 $100,000 1999 $200,000 2000 $300,000 2001 $400,000 2002 or thereafter $500,000.

(4) Treatment of certain indebtedness

(A) In general

The exclusion provided in paragraph (1) shall not apply to the extent that the land is debt-financed property.

(B) Definitions

For purposes of this paragraph -

(i) Debt-financed property

The term "debt-financed property" means any property with respect to which there is an acquisition indebtedness (as defined in clause (ii)) on the date of the decedent's death.

(ii) Acquisition indebtedness

The term "acquisition indebtedness" means, with respect to debt-financed property, the unpaid amount of -

(I) the indebtedness incurred by the donor in acquiring such property,

(II) the indebtedness incurred before the acquisition of such property if such indebtedness would not have been incurred but for such acquisition,

(III) the indebtedness incurred after the acquisition of such property if such indebtedness would not have been incurred but for such acquisition and the incurrence of such indebtedness was reasonably foreseeable at the time of such acquisition, and

(IV) the extension, renewal, or refinancing of an acquisition indebtedness.

(5) Treatment of retained development right

(A) In general

Paragraph (1) shall not apply to the value of any development right retained by the donor in the conveyance of a qualified conservation easement.
(B) Termination of retained development right

If every person in being who has an interest (whether or not in possession) in the land executes an agreement to extinguish permanently some or all of any development rights (as defined in subparagraph (D)) retained by the donor on or before the date for filing the return of the tax imposed by section 2001, then any tax imposed by section 2001 shall be reduced accordingly. Such agreement shall be filed with the return of the tax imposed by section 2001. The agreement shall be in such form as the Secretary shall prescribe.

(C) Additional tax

Any failure to implement the agreement described in subparagraph (B) not later than the earlier of -

(i) the date which is 2 years after the date of the decedent's death, or

(ii) the date of the sale of such land subject to the qualified conservation easement,

shall result in the imposition of an additional tax in the amount of the tax which would have been due on the retained development rights subject to such agreement. Such additional tax shall be due and payable on the last day of the 6th month following such date.

(D) Development right defined

For purposes of this paragraph, the term "development right" means any right to use the land subject to the qualified conservation easement in which such right is retained for any commercial purpose which is not subordinate to and directly supportive of the use of such land as a farm for farming purposes (within the meaning of section 2032A(e)(5)).

(6) Election

The election under this subsection shall be made on or before the due date (including extensions) for filing the return of tax imposed by section 2001 and shall be made on such return. Such an election, once made, shall be irrevocable.

(7) Calculation of estate tax due

An executor making the election described in paragraph (6) shall, for purposes of calculating the amount of tax imposed by section 2001, include the value of any development right (as defined in paragraph (5)) retained by the donor in the conveyance of such qualified conservation easement. The computation of tax on any retained development right prescribed in this paragraph shall be done in such manner and on such forms as the Secretary shall prescribe.
(8) Definitions

For purposes of this subsection -

(A) Land subject to a qualified conservation easement

The term "land subject to a qualified conservation easement" means land -

(i) which is located -

(I) in or within 25 miles of an area which, on the date of the decedent's death, is a metropolitan area (as defined by the Office of Management and Budget),

(II) in or within 25 miles of an area which, on the date of the decedent's death, is a national park or wilderness area designated as part of the National Wilderness Preservation System (unless it is determined by the Secretary that land in or within 25 miles of such a park or wilderness area is not under significant development pressure), or

(III) in or within 10 miles of an area which, on the date of the decedent's death, is an Urban National Forest (as designated by the Forest Service),

(ii) which was owned by the decedent or a member of the decedent's family at all times during the 3-year period ending on the date of the decedent's death, and

(iii) with respect to which a qualified conservation easement has been made by an individual described in subparagraph (C), as of the date of the election described in paragraph (6).

(B) Qualified conservation easement

The term "qualified conservation easement" means a qualified conservation contribution (as defined in section 170(h)(1)) of a qualified real property interest (as defined in section 170(h)(2)(C)), except that clause (iv) of section 170(h)(4)(A) shall not apply, and the restriction on the use of such interest described in section 170(h)(2)(C) shall include a prohibition on more than a de minimis use for a commercial recreational activity.

(C) Individual described

An individual is described in this subparagraph if such individual is -

(i) the decedent,

(ii) a member of the decedent's family,
(iii) the executor of the decedent's estate, or

(iv) the trustee of a trust the corpus of which includes the land to be subject to the qualified conservation easement.

(D) Member of family

The term "member of the decedent's family" means any member of the family (as defined in section 2032A(e)(2)) of the decedent.

(9) Treatment of easements granted after death

In any case in which the qualified conservation easement is granted after the date of the decedent's death and on or before the due date (including extensions) for filing the return of tax imposed by section 2001, the deduction under section 2055(f) with respect to such easement shall be allowed to the estate but only if no charitable deduction is allowed under chapter 1 to any person with respect to the grant of such easement.

(10) Application of this section to interests in partnerships, corporations, and trusts

This section shall apply to an interest in a partnership, corporation, or trust if at least 30 percent of the entity is owned (directly or indirectly) by the decedent, as determined under the rules described in section 2057(e)(3).

(d) Cross reference

For executor's right to be furnished on request a statement regarding any valuation made by the Secretary within the gross estate, see section 7517.
Internal Revenue Code

26 U.S.C. 2055

Sec. 2055. - Transfers for public, charitable, and religious uses

(a) In general

For purposes of the tax imposed by section 2001, the value of the taxable estate shall be determined by deducting from the value of the gross estate the amount of all bequests, legacies, devises, or transfers -

(1) to or for the use of the United States, any State, any political subdivision thereof, or the District of Columbia, for exclusively public purposes;

(2) to or for the use of any corporation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, including the encouragement of art, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), and the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private stockholder or individual, which is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office;

(3) to a trustee or trustees, or a fraternal society, order, or association operating under the lodge system, but only if such contributions or gifts are to be used by such trustee or trustees, or by such fraternal society, order, or association, exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, such trust, fraternal society, order, or association would not be disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and such trustee or trustees, or such fraternal society, order, or association, does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office;

(4) to or for the use of any veterans' organization incorporated by Act of Congress, or of its departments or local chapters or posts, no part of the net earnings of which inures to the benefit of any private shareholder or individual; or

(5) to an employee stock ownership plan if such transfer qualifies as a qualified gratuitous transfer of qualified employer securities within the meaning of section 664(g).

For purposes of this subsection, the complete termination before the date prescribed for the filing of the estate tax return of a power to consume, invade, or appropriate property for the benefit of an individual before such power has been exercised by reason of the death of such individual or for any other reason shall be considered and deemed to be a qualified disclaimer with the same full force and effect.
as though he had filed such qualified disclaimer. Rules similar to the rules of section 501(j) shall apply for purposes of paragraph (2).

(b) Powers of appointment

Property includible in the decedent's gross estate under section 2041 (relating to powers of appointment) received by a donee described in this section shall, for purposes of this section, be considered a bequest of such decedent.

c) Death taxes payable out of bequests

If the tax imposed by section 2001, or any estate, succession, legacy, or inheritance taxes, are, either by the terms of the will, by the law of the jurisdiction under which the estate is administered, or by the law of the jurisdiction imposing the particular tax, payable in whole or in part out of the bequests, legacies, or devises otherwise deductible under this section, then the amount deductible under this section shall be the amount of such bequests, legacies, or devises reduced by the amount of such taxes.

d) Limitation on deduction

The amount of the deduction under this section for any transfer shall not exceed the value of the transferred property required to be included in the gross estate.

e) Disallowance of deductions in certain cases

(1) No deduction shall be allowed under this section for a transfer to or for the use of an organization or trust described in section 508(d) or 4948(c)(4) subject to the conditions specified in such sections.

(2) Where an interest in property (other than an interest described in section 170(f)(3)(B)) passes or has passed from the decedent to a person, or for a use, described in subsection (a), and an interest (other than an interest which is extinguished upon the decedent's death) in the same property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to a person, or for a use, not described in subsection (a), no deduction shall be allowed under this section for the interest which passes or has passed to the person, or for the use, described in subsection (a) unless -

(A) in the case of a remainder interest, such interest is in a trust which is a charitable remainder annuity trust or a charitable remainder unitrust (described in section 664) or a pooled income fund (described in section 642(c)(5)), or

(B) in the case of any other interest, such interest is in the form of a guaranteed annuity or is a fixed percentage distributed yearly of the fair market value of the property (to be determined yearly).

(3) Reformations to comply with paragraph (2).

(A) In general.
A deduction shall be allowed under subsection (a) in respect of any qualified reformation.

**(B) Qualified reformation.**

For purposes of this paragraph, the term "qualified reformation" means a change of a governing instrument by reformation, amendment, construction, or otherwise which changes a reformable interest into a qualified interest but only if -

**(i)** any difference between -

**(I)** the actuarial value (determined as of the date of the decedent's death) of the qualified interest, and

**(II)** the actuarial value (as so determined) of the reformable interest,

does not exceed 5 percent of the actuarial value (as so determined) of the reformable interest,

**(ii)** in the case of -

**(I)** a charitable remainder interest, the nonremainder interest (before and after the qualified reformation) terminated at the same time, or

**(II)** any other interest, the reformable interest and the qualified interest are for the same period, and

**(iii)** such change is effective as of the date of the decedent's death.

A nonremainder interest (before reformation) for a term of years in excess of 20 years shall be treated as satisfying subclause (I) of clause (ii) if such interest (after reformation) is for a term of 20 years.

**(C) Reformable interest.**

For purposes of this paragraph -

**(i)** In general. -

The term "reformable interest" means any interest for which a deduction would be allowable under subsection (a) at the time of the decedent's death but for paragraph (2).

**(ii)** Beneficiary's interest must be fixed. -

The term "reformable interest" does not include any interest unless, before the remainder vests in possession, all payments to persons
other than an organization described in subsection (a) are expressed either in specified dollar amounts or a fixed percentage of the fair market value of the property. For purposes of determining whether all such payments are expressed as a fixed percentage of the fair market value of the property, section 664(d)(3) shall be taken into account.

(iii) Special rule where timely commencement of reformation. -

Clause (ii) shall not apply to any interest if a judicial proceeding is commenced to change such interest into a qualified interest not later than the 90th day after -

(1) if an estate tax return is required to be filed, the last date (including extensions) for filing such return, or

(2) if no estate tax return is required to be filed, the last date (including extensions) for filing the income tax return for the 1st taxable year for which such a return is required to be filed by the trust.

(iv) Special rule for will executed before January 1, 1979, etc. -

In the case of any interest passing under a will executed before January 1, 1979, or under a trust created before such date, clause (ii) shall not apply.

(D) Qualified interest. -

For purposes of this paragraph, the term "qualified interest" means an interest for which a deduction is allowable under subsection (a).

(E) Limitation. -

The deduction referred to in subparagraph (A) shall not exceed the amount of the deduction which would have been allowable for the reformable interest but for paragraph (2).

(F) Special rule where income beneficiary dies. -

If (by reason of the death of any individual, or by termination or distribution of a trust in accordance with the terms of the trust instrument) by the due date for filing the estate tax return (including any extension thereof) a reformable interest is in a wholly charitable trust or passes directly to a person or for a use described in subsection (a), a deduction shall be allowed for such reformable interest as if it had met the requirements of paragraph (2) on the date of the decedent's death. For purposes of the preceding sentence, the term "wholly charitable trust" means a charitable trust which, upon the allowance of a deduction, would be described in section 4947(a)(1).
(G) Statute of limitations. -

The period for assessing any deficiency of any tax attributable to the application of this paragraph shall not expire before the date 1 year after the date on which the Secretary is notified that such reformation (or other proceeding pursuant to subparagraph (J) [1] has occurred.

(H) Regulations. -

The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this paragraph, including regulations providing such adjustments in the application of the provisions of section 508 (relating to special rules relating to section 501(c)(3) organizations), subchapter J (relating to estates, trusts, beneficiaries, and decedents), and chapter 42 (relating to private foundations) as may be necessary by reason of the qualified reformation.

(I) Reformations permitted in case of remainder interests in residence or farm, pooled income funds, etc. -

The Secretary shall prescribe regulations (consistent with the provisions of this paragraph) permitting reformations in the case of any failure -

(i) to meet the requirements of section 170(f)(3)(B) (relating to remainder interests in personal residence or farm, etc.), or

(ii) to meet the requirements of section 642(c)(5).

(J) Void or reformed trust in cases of insufficient remainder interests. -

In the case of a trust that would qualify (or could be reformed to qualify pursuant to subparagraph (B)) but for failure to satisfy the requirement of paragraph (1)(D) or (2)(D) of section 664(d), such trust may be -

(i) declared null and void ab initio, or

(ii) changed by reformation, amendment, or otherwise to meet such requirement by reducing the payout rate or the duration (or both) of any noncharitable beneficiary's interest to the extent necessary to satisfy such requirement, pursuant to a proceeding that is commenced within the period required in subparagraph (C)(iii). In a case described in clause (i), no deduction shall be allowed under this title for any transfer to the trust and any transactions entered into by the trust prior to being declared void shall be treated as entered into by the transferor.

(4) Works of art and their copyrights treated as separate properties in certain cases.

(A) In general. -
In the case of a qualified contribution of a work of art, the work of art and the copyright on such work of art shall be treated as separate properties for purposes of paragraph (2).

(B) Work of art defined. -

For purposes of this paragraph, the term "work of art" means any tangible personal property with respect to which there is a copyright under Federal law.

(C) Qualified contribution defined. -

For purposes of this paragraph, the term "qualified contribution" means any transfer of property to a qualified organization if the use of the property by the organization is related to the purpose or function constituting the basis for its exemption under section 501.

(D) Qualified organization defined. -

For purposes of this paragraph, the term "qualified organization" means any organization described in section 501(c)(3) other than a private foundation (as defined in section 509). For purposes of the preceding sentence, a private operating foundation (as defined in section 4942(j)(3)) shall not be treated as a private foundation.

(f) Special rule for irrevocable transfers of easements in real property

A deduction shall be allowed under subsection (a) in respect of any transfer of a qualified real property interest (as defined in section 170(h)(2)(C)) which meets the requirements of section 170(h) (without regard to paragraph (4)(A) thereof).

(g) Cross references

(1) For option as to time for valuation for purpose of deduction under this section, see section 2032.

(2) For treatment of certain organizations providing child care, see section 501(k).

(3) For exemption of gifts and bequests to or for the benefit of Library of Congress, see section 5 of the Act of March 3, 1925, as amended (2 U.S.C. 161).

(4) For treatment of gifts and bequests for the benefit of the Naval Historical Center as gifts or bequests to or for the use of the United States, see section 7222 of title 10, United States Code.

(5) For treatment of gifts and bequests to or for the benefit of National Park Foundation as gifts or bequests to or for the use of the United States, see section 8 of the Act of December 18, 1967 (16 U.S.C. 191).
(6) For treatment of gifts, devises, or bequests accepted by the Secretary of State, the Director of the International Communication Agency, or the Director of the United States International Development Cooperation Agency as gifts, devises, or bequests to or for the use of the United States, see section 25 of the State Department Basic Authorities Act of 1956.

(7) For treatment of gifts or bequests of money accepted by the Attorney General for credit to "Commissary Funds, Federal Prisons," as gifts or bequests to or for the use of the United States, see section 4043 of title 18, United States Code.

(8) For payment of tax on gifts and bequests of United States obligations to the United States, see section 3113(e) of title 31, United States Code.

(9) For treatment of gifts and bequests for benefit of the Naval Academy as gifts or bequests to or for the use of the United States, see section 6973 of title 10, United States Code.

(10) For treatment of gifts and bequests for benefit of the Naval Academy Museum as gifts or bequests to or for the use of the United States, see section 6974 of title 10, United States Code.

(11) For exemption of gifts and bequests received by National Archives Trust Fund Board, see section 2308 of title 44, United States Code.

(12) For treatment of gifts and bequests to or for the use of Indian tribal governments (or their subdivisions), see section 7871
SMART GROWTH

The Home Builder’s Perspective

Robert M. Weiss
Executive Vice President
Home Builders Association of Kentucky
Frankfort, Kentucky

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SMART GROWTH: The Home Builder’s Perspective

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SECTION G(c)
Future Housing Needs for Kentucky
2001 – 2020

Housing and the Economy in Kentucky in the 1990’s

During the decade of the 90’s Kentucky’s growth was greater than the past three decades combined.

According to the latest census reports the state’s population grew from 3.5 million people to 4,041,769, a gain of 9.6%. This growth in population was unexpected as the Kentucky either lost population or remained stagnant during the past three decades. Even though the growth rate was strong for Kentucky it was still less than the national population growth rate of 13.1%.

From 1992 to 1998 Kentucky attracted 300,000 jobs for a 15% gain. The growth rate in manufacturing jobs was twice the national average, according to Dr. Paul Coomes of the University of Louisville. Most of these jobs were created in the middle of the state in areas along and between Interstates 75 and 65.

One down note is that although the creation of new jobs was strong the state still lags behind the national average in earnings per job.

The ability to attracting new jobs has been tied to the flourishing airports in Louisville and Northern Kentucky – Cincinnati.

The Census Report also cites the need for housing as extremely strong in Kentucky. In 1999 the Census report indicates that 21,581 new homes were built. This figure is somewhat conservative since the statistics were based on the number of building permits issued, and only 48 counties issue building permits.

New housing units increased at a rate of 18%, almost double the population increase. This statistic exemplifies the change in the average household which in the past consisted of a husband, wife and children.

Today we are seeing more one person households, and single parent households as the Kentucky income continues to rise in certain sectors.

All of this created a huge demand for new homes in the past decade.
Looking Forward

As we move into the new millennium the population of the state is predicted to increase at a rate equal to that of the last decade.

National Economists predict the need for between 1.3 and 1.5 million new housing starts per year for the next ten years. In fact a panel of eight economists recently predicted that housing starts will rise in the next three years from 1.55 million in 2001 to 1.60 million in 2002 to 1.64 million in 2003.

Looking at how that affects Kentucky we see that historically the Bluegrass State produces between one and two percent of the nation’s housing needs.

This would mean that in during the period between 2000 and 2010 Kentucky would see the need for approximately 25,000 homes each year.

The panel of economists were surprised that the new housing figures for the first part of this year were so strong given the slowing economy. They cite falling interest rates as the reason housing remained strong.

The Joint Center for Housing Studies of Harvard University agrees with the strength of the housing industry. In a report called “The State of the Nation’s Housing – 2001”, Nicolas P. Retsinas, Director of the Joint Center said, “Normally sharp drops in housing production and slowing home sales, take the wind out of the economy ahead of other sectors, but low interest rates and a strong demand have helped housing markets stay strong.

The future of housing is strong, according to the Harvard study. “Although no longer adding net new households, the baby boomers will continue to swell the ranks of homeowners during the next decade. As they reach the ages of 45 to 64, over 3 million baby boom households will likely make the shift from renter to owner. This growth will be fueled by delayed home buying among married and remarried couples, financial windfalls from inheritances, and rising homeownership rates among the never married and divorced.”

The largest increases in owner households, however, will come from the echo boomers as they move into the prime homebuying ages of 25 to 34. These children of the baby boomers will be between the ages of 15 and 34 in the year 2010.

The study points out that even if homeownership rates held at late 1990’s levels, the age structure of the population alone would keep the number of homeowners rising steadily for the next 20 years. A large portion of the new echo boomers creating the housing demand will be minorities and immigrants.
Where we are choosing to live

The Harvard study points out that the population growth is still moving toward the suburbs. Even though cities, as a group experienced their strongest population growth in decades, the study notes that for every three households that moved to central cities in 1999, five departed for the suburbs.

The group perceived to be leading the back to the city movement, the 25 to 34 year olds, twice as many individuals left the cities as moved in.

The study cites the intense development pressures in less populated areas of the country, where strong job growth has enabled people to work at ever greater distances from traditional employment centers.

Between 1990 and 1998, average job growth exceeded 15% in the nations low and moderate density counties. In contrast, job gains in the highest density counties averaged less than 6%.

The study points out that “the vigorous pace of home building has stirred political activism at both state and local levels to curb growth in outlying areas and closer in low density suburbs. These efforts are primarily intended to preserve open space and to slow or halt further development”.

They say “as additional growth limitations measures are approved, land costs will rise even more sharply and housing affordability in less developed areas will continue to erode. These pressures underscore the importance of finding ways to strike a balance between the desire to preserve open space and the need to expand affordable housing”.
$G(c) \cdot 4$
Survey Suggests Market-Based Vision of Smart Growth

April 22, 2002 - More is better when it comes to buying a home, according to a new survey of home buyers co-sponsored by the National Association of Home Builders (NAHB) and the National Association of Realtors® (NAR).

The home buyers indicated that price and home size were far more important considerations than proximity to work, the city or schools. Given three statements to choose from, for example, 62 percent indicated that "the top concern was price," while 31 percent indicated that "finding a home in the right neighborhood was the top priority." Just 7 percent of respondents said that "being close to work and minimizing the commute was really important."

When asked to agree with various statements about their homes, 64 percent agreed with the statement, "I wish my home were larger." This was followed by "I wish I could walk to more places from my home," 27 percent; "I wish my home were closer to where I work," 23 percent; "I wish my home were closer to shopping and restaurants," 17 percent; "I wish my home were closer to public transportation," 9 percent; and "I wish I were closer to the city," 5 percent.

"This survey demonstrates that home buyers are quite conscious of the tradeoffs they make when buying a home," said Gary Garczynski, president of the National Association of Home Builders (NAHB) and a builder/developer from Woodbridge, Va. "They are willing to live further from the city in order to have a larger home, and the quality of the community is more important than the length of the commute. A better understanding of these tradeoffs enables us to develop planning and growth policies that take into account home buyers' preferences."

"Price, home size, and neighborhood quality are the most important factors affecting buyers' decision making. The marketplace will continue to determine the shape of America's communities. As the 2002 home buying season opens, this study provides valuable findings that can guide policymakers to arrive at solutions to the challenges of growth - solutions that reflect consumer choices," said NAR Treasurer Pat Kaplan, a Realtor® from Portland, Ore.

The survey was done to provide a better understanding of the factors that drive home buyers' decisions in the marketplace. The national sample of 2,000 households was derived from a panel maintained by the polling firm National Family Opinion (NFO) of households that have purchased a primary residence within the past four years. NFO conducted the survey in January 2002.
Other findings of the survey were:

- When asked to rate the importance of 16 aspects of a home and its location, "houses spread out" received the highest rating, with 62 percent of respondents checking important or very important. This was followed by less traffic in neighborhood, 60 percent; lower property taxes, 55 percent; bigger home, 47 percent; bigger lot, 45 percent; less developed area, 40 percent; away from the city, 39 percent; closer to work, 28 percent; closer to public transportation, 13 percent; smaller house, 10 percent; and smaller lot, 9 percent.

- When asked about the importance of 18 community amenities, the highest ranking features were (with percent ranking as important or very important): highway access, 44 percent; jogging/bike trails, 36 percent; sidewalks, 28 percent; parks, 26 percent; playgrounds, 21 percent, and shops within walking area, 19 percent.

- Asked to rank three alternatives for where new growth should occur, 37 percent selected "build new homes in existing, partially developed suburban areas" as their first choice and 51 percent as their second choice. "Build new homes on vacant land in the central city or inner suburbs" was the preferred choice of 35 percent and the second choice of 23 percent. "Build homes in outlying areas," was the first choice of 29 percent and second choice of 26 percent.

- Asked which single factor they would change in their home or community, "taxes would be lower" led with 35 percent, followed by "I'd live in a bigger home," 26 percent; "I'd own a larger lot," 17 percent; "my home would be closer to where I work," 8 percent; "schools would be better," 5 percent; and "other," 9 percent.

"The survey responses suggest a vision of smart growth that home buyers are prepared to embrace," Garczynski said. "A majority of consumers want single-family detached homes in a pedestrian-friendly community that has shopping within walking distance. They want a mix of open space, including parks, recreational facilities, playgrounds, farms, nature preserves and undeveloped areas. They want traffic minimized on neighborhood streets. To the extent that we, builders, developers, planners, elected officials - can create high quality, walkable, mixed-use communities, we will deliver a version of smart growth that is more likely to be accepted in the marketplace."

Powerpoint presentation of survey results.
Growth in the Golden Triangle in Kentucky

Northern Kentucky – 366,480
Kenton County – 151,464 (+6.7)
Boone County – 85,991 (+49.3)
Campbell County – 88,616 (+5.7)
Grant County – 22,384 (+42.2)
Gallatin County – 7,870 (+45.9)
Carroll County – 10,155 (+9.3)

Population: 1,725,702

Louisville – 846,121
Jefferson – 693,604 (+4.3)
Shelby - 33,337 (+34)
Bullitt – 61,236 (+28.7)
Oldham - 46,178 (+38.8)
Spencer - 11,766 (+27.7)

Lexington – 513,101
Fayette – 260,512 (+16)
Scott - 33,061 (+39)
Woodford – 23,208 (+16)
Jessamine – 39,041 (+28)
Clark – 33,144 (+12)
Anderson – 19,111 (+31)
Madison – 70,872 (+23)
Bourbon – 19,360 (+1)
Garrard – 14,792 (+27.7)
Source: U.S. Census Bureau; research by LINDA J. JOHNSON/STAFF

CRAIG JOHNSON/STAFF
# 100 Fastest Growing Counties by Percent Change: April 1, 2000 to July 1, 2001

<table>
<thead>
<tr>
<th>Rank</th>
<th>County</th>
<th>State</th>
<th>July 1, 2001 Estimate</th>
<th>April 1, 2000 Population Estimates Base</th>
<th>April 1, 2000 to July 1, 2001 Numeric Population Change</th>
<th>April 1, 2000 to July 1, 2001 Percent Population Change</th>
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Suggested Citation:
Table CO-EST2001-11 - 100 Fastest Growing Counties by Percent Change: April 1, 2000 to July 1, 2001
Source: Population Division, U.S. Census Bureau
Release Date: April 29, 2002
# Kentucky QuickFacts from the US Census Bureau

## State and County QuickFacts

### Kentucky

**Select a county**

Follow the ? link for definition and source information.

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<td>Private nonfarm employment, percent change 1990-1999</td>
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<td>Retail sales per capita, 1997</td>
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<td>Women-owned firms, percent of total, 1997</td>
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<td>Local government employment - full-time equivalent, 1997</td>
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<td>Persons per square mile, 2000</td>
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(a) Includes persons reporting only one race.
(b) Hispanics may be of any race, so also are included in applicable race categories.

FN: Footnote on this item for this area in place of data
D: Not available
NA: Not applicable
X: Suppressed to avoid disclosure of confidential information
S: Suppressed; does not meet publication standards
Z: Value greater than zero but less than half unit of measure shown
F: Fewer than 100 firms

Data Quality Statement

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Last Revised: Thursday, 07-Feb-2002 14:17:36 EST

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Comments by the Home Builders Association
On the
Purchase of Development Rights
And
Transfer of Development Rights

Transfer of Development Rights

In 1990 the Kentucky Legislature passed Senate Bill 405, which enabled local governments with planning units to institute a Transfer of Development Rights Program within their jurisdiction.

Although the law has been on the books for eleven years, it has not been successfully used within the Commonwealth of Kentucky.

The premise behind the Transfer of Development Rights is that agricultural land may be preserved, through the transfer of development rights to other areas in a county, which would be re-zoned to include a higher density of development than was previously permitted.

The Transfer of Development Rights has been used in Montgomery County, Maryland, and in New Jersey and have been somewhat successful due to the fact that there was a huge demand for high density housing in the “receiving areas”, as they were located in large urban areas.

The Transfer of Development Rights program has not been successfully used in Kentucky due to the lack of demand for high density housing.
Purchase of Development Rights

Fayette County, Kentucky

Enabling Legislation for Urban County Governments
In 1998 the Kentucky Legislature passed House Bill 644, which enabled only Urban County Governments in Kentucky to institute a Purchase of Development Rights Program. The bill stated that if new tax dollars were committed to purchase these development rights that a referendum of a percentage of voters voting in the last mayoral election needed to approve before these taxes could be instituted.

The taxes referred to in the HB 644 included 1) an ad valorem tax not to exceed $.05 per $100 of assessed value of all taxable property in the Urban County; 2) a 1/8 of one percent license fee on occupations and professions of residents of the Urban County, and 3) a transient tax on motels and hotels consisting of one percent of total rents.

This bill only applies to Urban County Governments which translates into only applying in Fayette County.

Funding of the Program
During the 2000 Legislative Session the Governor of Kentucky appropriated $15 million in grant money to Fayette County to help fund the Purchase of Development Rights Program.

Also the Lexington/Fayette Urban County Government appropriated a $2 million annual commitment to make payments on government bond revenue of $25 million.

Since no new tax dollars were proposed the Urban County Government has $40 million to run such a program.

It was speculated that no new tax dollars were proposed by the Urban County Government due to the fact that a silent poll indicated that the taxes proposed would not pass in a referendum.

It has also been speculated that $40 million is not enough to fund the 50,000 acres and that a tax increase is inevitable should the program continue toward the goal set by the Lexington/Fayette Urban County Government.

Status of the Program
Currently the program is proceeding at a slower pace than expected. Some 37 landowners have applied to have their property evaluated for purchase of development rights. These evaluations are expected to provide the rural land owner with a price for development rights somewhere between the price for agricultural land and the price for which it could be sold for development.
The major question at this time is whether or not the landholders will be satisfied with the price offered by the Board created to come up with the evaluations. Only time will tell.

**Purchase of Development Rights – General Terms**

In general the major problem with the implementation of Purchase of Development Rights Programs is coming up with the funds necessary to purchase the rural land.

As cited in the Boone County Report, the most successful program in the country is the Pennsylvania Purchase of Development Rights Program. It has been reported that the program has been funded with $143 million in a one time appropriation, and a $20 million annual tax income from a tax on cigarettes.

It was also cited that Pennsylvania has permanently protected 186,000 acres of land.

The $143 million dollars doesn’t seem to be a lot of money for a state that is 114,817 square miles in land mass. And the 186,000 acres preserved is miniscule in comparison to the total land mass.

Compare this with the $40 million currently in place in Fayette County with a goal to purchase 50,000 acres out of a total land mass of 285 square miles.

**Summary**

Although the Purchase of Development Rights may be an admirable goal by local governments the truth of the matter is that the program needs funding, which seems to be lacking.

The question arises, Will the taxpayers be burdened with the cost of preserving farmland that they cannot use for recreational or other purposes? If so will there have to be a referendum to get approval.

What is the true cost to the farmer to take his land from the sale for development for at least 25 years if not eternity?

What happens to the farmers’ descendants when and if they decide not to farm and cannot sell the land for any other purpose?
CURRENT REGULATORY ISSUES UNDER
THE CLEAN WATER ACT RELATING TO THE
CORPS OF ENGINEERS, THE U.S. ENVIRONMENTAL
PROTECTION AGENCY AND OTHER AGENCIES AS
THEY RELATE TO THE MINING INDUSTRY

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Greenebaum Doll & McDonald PLLC
Lexington, Kentucky

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SECTION H
CURRENT REGULATORY ISSUES UNDER THE CLEAN WATER ACT RELATING TO THE CORPS OF ENGINEERS, THE U.S. ENVIRONMENTAL PROTECTION AGENCY AND OTHER AGENCIES AS THEY RELATE TO THE MINING INDUSTRY

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SECTION H
CURRENT REGULATORY ISSUES UNDER THE CLEAN WATER ACT RELATING TO THE CORPS OF ENGINEERS, THE U.S. ENVIRONMENTAL PROTECTION AGENCY AND OTHER AGENCIES AS THEY RELATE TO THE MINING INDUSTRY

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I. INTRODUCTION

Frequent regulatory change relating to the coal mining industry is a way of life, given the industry’s status as one of the most heavily-regulated industries in the country. In the spirit of that tradition, the agencies with regulatory authority over administering Sections 401, 402 and 404 of the Clean Water Act (“CWA”) and other agencies with jurisdiction over mining are currently involved in the process of determining how mountaintop mining and valley fill construction should be regulated under the CWA and under other statutes. Under pressure from environmental groups and such agencies as the Environmental Protection Agency (“EPA”), the U.S. Fish and Wildlife Service (“FWS”) and others, both in the courts and in other arenas, the Corps of Engineers (“Corps”) is feeling the pressure to come up with a cohesive program on permitting fills and slurry impoundments insofar as such activity involves the placement of material in streams or stream channels. A number of side shows are unfolding simultaneously so that the ultimate outcome for the mining industry as this point is far from clear.
II. SOME RECENT HISTORICAL BACKGROUND

a. The Bragg v. West Virginia Coal Association Case

In 1998 a group of individuals and the West Virginia Highlands Conservancy sued the West Virginia Division of Environmental Protection ("DEP") and the Corps claiming that the Corps and DEP lacked authority to approve placement of excess spoil into waters of the United States in connection with mountaintop removal operations and the construction of excess spoil or valley fills. Plaintiffs claimed that the Corps’ authority under § 404 of the CWA was limited to discharges of “fill material” and that excess spoil was not fill material, but rather was “waste” which, under the Corps’ own definitions, was excluded from the definition of “fill.” Alternatively, the plaintiffs in Bragg claimed that even if the Corps had authority to allow placement of excess spoil into streams in connection with fill construction, the practice should never be allowed under the Corps’ nationwide permit program, but rather should only be considered by the Corps in the context of an individual § 404 permit application process inasmuch as, by its very nature, placing fill material in streams as part of fill construction at mountaintop removal operations involved “more than minimal impacts” to the environment, necessitating an individual § 404 permit.

In 1998, the Corps settled the claims asserted against it in Bragg by agreeing to conduct with OSM, EPA and FWS a programmatic environmental impact statement ("EIS") on the effects of mountaintop removal and valley fills. West Virginia DEP and Kentucky Department for Surface Mining, Reclamation and Enforcement ("DSMRE") were to contribute to the EIS effort as consulting agencies. For their part, the plaintiffs agreed that they would no longer press the issue that excess spoil is “waste,” thereby giving up the jurisdictional argument. The Corps
also agreed that while the programmatic EIS was being developed, the Corps would limit the use of nationwide permits for excess spoil fills to those fills with drainage areas of 250 acres or less (fills with drainage areas of greater than 250 acres would require individual permits from the Corps).

With the Corps removed from the case, the court agreed with plaintiffs in their assertion that DEP’s so-called “stream buffer zone” regulation\(^1\) did not authorize DEP to allow coal operators to place excess spoil, e.g. valley fills, in perennial or intermittent streams. *Bragg v. West Virginia Coal Association*, 72 F. Supp. 2d 642 (S.D.W.V.,1999). The court also expressed concern about DEP granting a stream buffer zone variance without making the required findings.\(^2\) The court ultimately found that mountaintop removal violates the Clean Water Act.

The court noted that excess spoil was neither “dredged” material (excavated from a water body) nor “fill” material (since it was not being placed in streams for the “primary purpose of replacing aquatic areas with dry materials” as that term was defined by the Corps. Thus, the court concluded that the Corps’ § 404 permitting authority did not include allowing valley fills to be

\(^1\) The “buffer-zone regulation in West Virginia prohibited disturbance within 100 feet of a perennial or intermittent stream unless approved by DEP which must find, to give such approval, that the disturbance will not violate applicable water quality standards and will not adversely affect water quality or quantity or other environmental resources of the stream.

\(^2\) The federal stream buffer zone rule (30 CFR 816.57(a)(1)) states, in part, as follows:

No land within 100 feet of a perennial stream or an intermittent stream shall be disturbed by surface mining activities, unless the regulatory authority authorizes surface mining activities closer to, or through, such a stream . . . upon a finding that –

(1) Surface mining activities will not . . . violate . . . applicable water quality standards, and will not adversely affect the water quantity or quality or other environmental resources of the stream.
constructed into and over streams. This ruling sent shock waves around the industry in the Appalachian region of the country because it would have effectively eliminated mountaintop removal as a mining method since there is no practical way to avoid placing excess spoil in stream beds when performing mountaintop removal operations. The court in Bragg rejected the arguments that since EPA guidelines under § 404 of the CWA defines “fill” to include any pollutant that enters and changes the bottom elevation of waters of the United States for any reason, such guidelines legitimized Corps jurisdiction over construction of valley fills in connection with mountaintop removal.

In 2001, the Fourth Circuit Court of Appeals reversed the lower court on other grounds, namely that the 11th Amendment to the U.S. Constitution bars actions in federal court against state governments to enforce state law. Bragg v. West Virginia Coal Assn, 248 F. 3d 275 (4th Cir. 2001). The Fourth Circuit rejected plaintiffs’ assertion that the state had not waived its 11th Amendment immunity by obtaining OSM approval of its state program and that West Virginia’s program was state law, not federal.

b. Kentucky Resources Council’s Notice of Intent To Sue

On June 28, 2000, Tom Fitzgerald of the Kentucky Resources Council filed with OSM and Kentucky a notice of intent to sue under Section 520 of the Surface Mining Control and Reclamation Act of 1977 (“SMCRA”) asserting, among other grounds, that Kentucky’s state program regulation on stream buffer zones, 405 KAR 16:060 Section 11, impermissibly limits the application of the prohibition against impairment of water quality or quantity to the stream reach below any impounding structure, including a valley fill and any sediment ponds. Fitzgerald asserted in his notice of intent that Kentucky’s regulation was inconsistent with and less stringent
than OSM’s standard and the terms of SMCRA. Fitzgerald also asserted that such regulation and practice by Kentucky’s DSMRE was inconsistent with the lower court’s ruling in Bragg v. Robertson, supra. The notice of intent further asserted that OSM had failed to perform its duty to require Kentucky DSMRE to revise its buffer zone regulation to make it consistent with the federal standard and SMCRA. While a number of other issues raised in the notice of intent were seemingly resolved to the satisfaction of Mr. Fitzgerald and the Kentucky Resources Council, the central issue regarding Kentucky stream buffer zone regulation has not been resolved. No suit has been filed against OSM and Kentucky to date in connection with this issue.

c. Kentuckians For the Commonwealth, Inc. v. Rivenburgh

On August 21, 2001, a citizens group, Kentuckians for the Commonwealth, Inc., ("KFTC") brought suit against the Corps in federal court in the Southern District of West Virginia challenging the Corps’ authorization of a nationwide permit issued to Martin County Coal Company in connection with a large mountaintop removal operation in Kentucky which entailed 27 valley fills and allegedly over six miles of streams. The suit was filed in federal court in West Virginia on the theory that court had jurisdiction since the Huntington, West Virginia District of the Corps has jurisdiction over the Martin County operation.\(^3\) The issues raised in the KFTC case are essentially the same as were raised in the Bragg case.

\(^3\) Despite an attempt by defendants and intervenors to transfer the case to federal court in Kentucky, the case remains in the Southern District of West Virginia. Plaintiffs obviously favor keeping the case in front of Judge Hayden in view of his rulings in the Bragg litigation. On the other hand, as long as the case remains in West Virginia, any appeal would be before the Fourth Circuit Court of Appeals which reversed Judge Hayden in the Bragg litigation on the basis of the Eleventh Amendment issue as discussed above.
On February 7, 2002, plaintiffs in the KFTC case filed a motion for summary judgment and for permanent injunction on Count 1 of the complaint - Count 1 being that the Corps has no authority under the CWA to issue permits to dispose of excess spoil from surface coal mining operations in streams. KFTC seeks a declaratory judgment and permanent injunction (1) prohibiting the Corps from authorizing any activity at any site that would involve the placement of excess spoil into “waters of the United States” and (2) requiring the Corps to revoke Martin County Coal’s authorization to do so pursuant to Nationwide Permit # 21 (“NWP 21”).

The gist of plaintiff’s argument is as follows: (1) excess spoil material is “waste” and not “fill” based on the Corps’ own definition of “fill material.” Thus, under the plain language of the Corps’ definition, § 404 permits cannot be issued for disposal of waste. Disposal of waste is regulated instead under § 402 of the CWA, 33 U.S.C. § 1342. Also, plaintiffs are arguing that under the Corps’ contemporaneous construction of its regulation, such material is waste. The

4 In 33 CFR § 323.2(e) the Corps defined “fill material” as “any material used for the primary purpose of replacing an aquatic area with dry land or of changing the bottom elevation of a water body. The term does not include any pollutant discharged into the water primarily to dispose of waste, as that activity is regulated under section 402 of the Clean Water Act.” Plaintiffs also rely on preamble language contained in the Federal Register accompanying this definition which, according to plaintiffs, demonstrates the Corps’ intent that disposal of such things as solid waste, sludge, garbage, trash and “debris” in water is not allowed under § 404 of the CWA, but rather must be regulated under § 402 (the NPDES program).

5 In its preamble to its current rule defining “fill material” (42 Fed. Reg. at 37130) (July 19, 1977), the Corps stated that during two years of experience with the 404 program, discharges of industrial and municipal solid waste materials should be regulated through the NPDES program and not under the 404 program of the CWA. Thus they modified their definition of fill material to exclude those pollutants that are discharged into water primarily to dispose of waste. As will be discussed below, EPA and the Corps are in the process of re-defining “fill material” so as to address specifically the issue, among others, of whether the construction of valley fills in areas that include streams is allowable under § 404 of the CWA as fill material. This rule change may be finalized prior to the date of the seminar.
plaintiffs in the KFTC litigation are also pointing to deposition statements by three key Corps officials that the purpose of placing mining spoil in valley fills is to dispose of waste, and that such discharges should be regulated by EPA under the NPDES program pursuant to § 402 of the CWA. The plaintiffs further rely upon informal policy issued by the Corps’ Division Office in Cincinnati to that effect. They further remind Judge Hayden that in the Bragg case he had concluded that overburden or excess spoil, “being a pollutant and waste material, is not ‘fill material’ subject to authority under 404 of the CWA, but rather subject to EPA jurisdiction under 402.

The 404-402 argument being presented in the plaintiffs’ motion for summary judgment may be, in the end, a negotiating point for the plaintiff if it was able to persuade the Corps to focus on the other issue in the case, namely that, as EPA has stated many times6, the construction of large valley fills or a series of valley fills covering large portions of stream beds in connection with mountaintop removal operations involves more than “minimal impacts” on the aquatic environment, thus necessitating an individual § 404 Corps permit as opposed to one or more nationwide permits.

d. Corps of Engineers/Environmental Protection Agency Rulemaking To Revise CWA Definition of “Fill Material.”

6 For example, on July 18, 2000, the Regional Administrator of Region 4, EPA wrote to the District Engineer of the Huntington, West Virginia District of the Corps to express his strong opposition to the Corps’ approval, via a single nationwide #21 permit, the Martin County Coal Company project in Kentucky which EPA characterized as involving 27 valley fills that would “destroy” over “33,000 linear feet of streams.” EPA demanded that the Corps proceed via an individual permit. Since this letter, EPA gave notification that it intended to elevate the issue with the possibility of an EPA veto of the Corps’ action.
On April 20, 2000, EPA and the Corps jointly issued a proposed rule 7 in which they propose to revise their CWA regulations defining the term “fill material.” As noted above, the Corps’ and EPA’s definitions of that term differ from each other which, as they noted, has led to uncertainty and confusion. While the Corps had amended its definition in 1977 to add its “primary purpose” test and excluded from the definition material that was discharged primarily to dispose of waste 8, EPA did not add this test. To resolve this inconsistency and to reduce or eliminate extensive litigation engendered by the inconsistent definitions (including the cases discussed above involving mountaintop removal/valley fills), EPA and the Corps propose to re-define “fill material” to mean “material that has the effect of replacing any portion of a water of the U.S. with dry land, or changing the bottom elevation of any portion of a water of the U.S.” At the same time, it would exclude from the definition fill material discharges subject to EPA proposed or promulgated effluent limitation guidelines and standards under the CWA sections 301, 304 and 306 and discharges under an NPDES permit under § 402 of the CWA. With regard to coal mining overburden, the proposed rule states that EPA and the Corps believe that such material has the effect of “fill” and thus should be regulated under Corps jurisdiction under § 404. The preamble to the rule goes on to state that the placement of “rock and other material in the heads of valleys, with a sedimentation pond located downstream” has historically been regulated by the Corps under § 404 and that they believe that it should continue to be so regulated.

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8 42 Fed. Reg. 41291 (7-19-77)
This proposed rule has produced both a veritable avalanche of written comments as well as some political fall-out. The former is best reflected in the preamble to the Corps’ January 15, 2002 final rule re-issuing its nationwide permits\textsuperscript{9} where the Corps acknowledges the substantial number of comments it had received on the “fill material” rulemaking and the difficulty it was having in that rulemaking. On the political front, both Democrats and Republicans alike have openly criticized the Corps/EPA proposed re-definition of fill material. Several GOP House members have called on the agencies to withdraw the proposed rule. For example, Representative Christopher Shays (R-Conn.) indicated that the rule would have a “devastating effect on the nation’s waters.” Rep. Nancy Johnson (R.Conn.), Rep. Rick Lazio (R-N.Y.), Rep. Brian Bilbray (R-Cal.) and Rep. Benjamin Gilman (R-N.Y.) joined Rep. Shays in filing comments on the proposed rule opposing the revised definition. The stakes grow higher with the virtual certainty that numerous environmental groups have promised to challenge the rule if it becomes final. The aforementioned GOP lawmakers are urging President Bush to have the Corps and EPA to change course away from the proposed rule so as not to allow disposal of coal mining spoil into valley fills. In a March 25, 2002 letter to the President, a dozen Republican House members expressed strong opposition to the proposed rule change, arguing that the rule “is designed to legitimize mountaintop removal mining.” They also argue that the rule change would enable other undesirable non-mining wastes to be dumped in streams, rivers, lakes and wetlands, contrary to the CWA.

One side issue is reflected in the preamble to the proposed regulation where the Corps/EPA discuss creating a definition of “unsuitable fill material.”

\textsuperscript{9} 67 Fed. Reg. 2020 (1-15-02) at page 2038
Association has urged EPA’s Office of Water to drop this concept from the final rule, urging instead that the Corps make such determinations on a case-by-case basis. NMA has argued that “a refusal to process a permit application [under § 404 of the CWA] on the basis of ‘unsuitable fill’ raises procedural and due process issues.”

The national media, including major stories on National Public Radio, the television networks and major national newspapers, have highlighted the importance of the impending Corps/EPA rule, raising the specter that the revised rule could even become an important election issue in somewhat the same vein as opening up the Arctic National Wildlife Reservation to oil and gas exploration.

e. Programmatic Environmental Impact Statement on Mountaintop Mining and Valley Fills

As part of the price of getting out of the Bragg litigation in West Virginia discussed above, the Corps, EPA, OSM and the U.S. Fish and Wildlife Service (“FWS”) agreed to prepare a programmatic environmental impact statement (“EIS”) under NEPA on mountaintop mining and valley fills. As discussed, plaintiffs in the Bragg litigation in West Virginia, in agreeing to dismiss their case against the Corps and the other federal defendants, received an agreement from the federal defendants (the Corps, OSM, and FWS) to perform this programmatic EIS on mountaintop removal and valley fills. The Corps indicated in its preamble to its January 15, 2002 rulemaking (re-authorizing its nationwide permit program) that the Corps will use this EIS to “better understand the environmental effects of mountaintop mining and valley fills, as well as programmatic changes that may be necessary to address those impacts.” The Corps further stated
that it would reevaluate NWP 21 when the mountaintop EIS is completed.\footnote{67 \textit{Fed. Reg.} 2039 (1-15-02); The Corps added that it will use the results of the EIS and ``all other information that may be available at that time, including information resulting from individual verification of all NWP 21 projects to make sure that NWP 21 results in no more than minimal impacts (site-specific or cumulatively) on the aquatic environment.} Presumably, based on the Corps' own preamble comments in its nationwide regulations, the use of NWP 21 for valley fills and mountaintop removal operations will be guided and utilized only to the extent deemed appropriate based on the findings in the joint agency programmatic EIS. If the EIS concludes that valley fills involve more than ``minimal impact'' (either individually or cumulatively) at a site, then it would seem that the Corps will be locked into requiring individual permits.

The latest estimate by the agencies working on the EIS is that an official draft is expected to be available in August, 2002.

f. OSM's Rulemaking To Revise Its Stream Buffer Zone Regulation

As if there weren't already enough regulatory activity surrounding the issue of the placement of spoil material and coal refuse into streams as part of coal mining operations, OSM is working on a revision to its stream buffer rule, 30 CFR 816.57(a)(1), which is quoted, in part, above. As in the case of the Corps/EPA joint rulemaking on the definition of ``fill material'' and the Corps' implementation of its nationwide permit program as to mountaintop mining, OSM's rulemaking to amend or clarify its stream buffer zone rule would appear to be tied to the result of the joint agency programmatic EIS on mountaintop removal/valley fills. These actions are all seemingly tied together in the scheme of things. Discussions with OSM regarding the
status of its rulemaking confirm that OSM will be guided by the findings of the EIS as much as anything.

According to an April 11, 2002 Department of Interior memorandum, OSM intends to propose a rule to modify the stream buffer zone rule to clarify that the buffer zone rule should not be interpreted “as a prohibition on placement of excess spoil fills in streams.” The memo was released by environmental groups, following which it was released by Interior. Environmentalists cite this memo, together with the Corps/EPA proposed revision of the definition of “fill material” as evidence of a “one-two punch that will knock out all federal protection for streams in Appalachia.”

**g. Refuse Impoundments, the Corps of Engineers and the Kentucky Division of Water**

A somewhat related issue to the placement of spoil or overburden in streams in connection with the construction of valley fills is the construction of new refuse impoundments that would cover or affect streams. The Corps has considered coal refuse to be “fill material” and thus appropriate for regulation under the Corps’ § 404 CWA jurisdiction. However, the Kentucky Resources Council (“KRC”) wrote to the Corps’ Louisville District on July 4, 2001 serving notice of its opposition to the construction of a coal slurry pond at the confluence of Jake Campbell Branch and the North Fork of the Kentucky River. The basis for the opposition is KRC’s reading of the Corps’ definition of “fill material” which, in KRC’s view, would preclude coal refuse and fine slurry/water material which KRC concludes is coal preparation “waste”

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material. As such, KRC assets that it must be regulated under Section 402 of the CWA and not Section 404.

Alternatively, KRC argues that assuming for the sake of argument that filling the stream with coal slurry can be approved under § 404 of the CWA, the proposal to do so still cannot be approved because: (1) an environmental impact statement ("EIS") is needed in order to comply with NEPA; (2) the proposal must be accompanied with a discussion and assessment of the "practicable alternatives" to locating the impoundment at this location; (3) the proposal is contrary to the public interest because there are available alternative, cost-competitive and safer technologies for disposal of coal preparation wastes. KRC pins its EIS/NEPA argument on its assertion that the scale, location and potential environmental and public safety considerations of such a project (invoking the two recent coal slurry spills as evidence) make the permitting of such a facility a "major federal action" that may significantly affect the human environment, mandating an EIS under CEQ regulations at 40 CFR 1508.8(b). KRC goes on to point out inadequacies in the application for a permit/authorization, arguing that it fails to satisfy the § 404(b)(1) guidelines which are the roadmap for the Corps' approval of a project. Specifically, KRC asserts that in addition to no discussion of "practicable alternatives" as to site location, configurations and technologies, there is also no discussion of what is the "project purpose" for purposes of evaluating impacts and complying with NEPA. Finally, the KRC asserts that there is no evaluation of a public interest review apart from the requirements of NEPA and the performance of an EIS.

Whether or not the Corps and EPA will address the issue of placing coal slurry into streams as part of their soon-to-be released redefinition of "fill material" remains to be seen.
Many in industry fear that the joint Corps/EPA definition and accompanying preamble may “split the baby” by defining overburden/spoil material as “fill material” while defining coal slurry as “waste” which, as mentioned, may not be regulated under § 404 of the CWA, but rather under § 402 which would effectively eliminate coal slurry impoundments.

By letter dated October 11, 2001, Jack Wilson, then Director of Kentucky’s Division of Water, informed Czar Coal Company that its application for a water quality certification under Section 401 of the CWA was denied in connection with Czar Coal’s proposed coal slurry impoundment on Middle Fork Rockcastle Creek. The letter (which was later withdrawn by then Director Wilson) references the pending Corps/EPA rulemaking on the definition of “fill material” which may be determinative on the issue of disposal of coal slurry in connection with a § 404 permit application. Regardless of how the rulemaking comes out, Wilson’s letter states that he recommends that this project, as well as other projects of “similar magnitude,” should be processed by the Corps as an individual 404 permit because of the potential for significant impact to aquatic resources and because of the increased opportunity for public input and scrutiny via the individual permit process. As of the date this paper is being prepared, no action has been taken either by the Corps or by the DOW to act on Czar Coal’s request to construct a slurry impoundment. The problem may or may not be solved by the Corps/EPA rulemaking on redefining “fill material.”

III. STATE WATER QUALITY CERTIFICATIONS UNDER § 401 OF THE CWA

Coal operators have many hurdles to clear in order to obtain the requisite approvals to construct valley fills in connection with mountaintop removal operations. In
addition to approvals/authorizations by the Corps under its permitting system under § 404, and
the requisite permit by the state surface mining authority, approvals must be obtained from state
water quality agencies pursuant to § 401 of the CWA. The CWA requires that states adopt water
quality standards to protect uses of waters within the state12, and further requires as a prerequisite
for a federal permit involving a discharge into waters that there be a certification from the state
that the discharge will comply with state water quality standards.13 In establishing water quality
standards, the state must designate what use is to be protected for the various waters of the state
and then adopt criteria sufficient to protect those designated uses.

In connection with the Corps regulatory process, the water quality certification process
generally begins when the Corps issues its public notice of a permit application and sends a copy
to the state water quality agency. Section 401 of the CWA provides that the state certification
requirement is waived if the state fails to act within a “reasonable time” which shall not exceed
one year. It is important to note, however, that frequently the water quality certification becomes
a bone of contention before the Corps even gets involved since the state mining agency may
decline to issue a mining permit until the water quality certification is issued. EPA can also play
a role since it may raise independently of the state its own water quality concerns.

In the context of water quality certifications applicable to nationwide permits, such as
NWP 21 applicable to mining, each state must certify a particular NWP for it to be applicable in
that state. In Kentucky, there are several factors to be aware of. First, in 1994 the legislature

12 33 U.S.C. 1313(a)

13 33 U.S.C. 1341. The water quality certification requirement is noted in the Corps
regulations at 33 CFR 320.4(d).
enacted House Bill 633 \textsuperscript{14} which clarified that for valley fills greater than 480 acres, a 401 water quality certification may only be issued if it requires as a condition stream mitigation on a one-to-one ratio as discussed below. HB 633 also provided that no water quality certification would be required for a road crossing on the permitted area impacting less than 200 linear feet of water. This legislation was a compromise reached between environmentalists and the coal industry. It does not specifically authorize the purchase of mitigation as exists under West Virginia law.

KRS 224.16-070 also provides that it only applies if the applicant for the water quality certification is eligible for a NWP #21 and if the surface coal mining operation will not impact waters designated by the cabinet in its water quality standards as outstanding state or national resource waters or as cold water aquatic habitat. It further provides that if the watershed above the toe of the farthest downstream permanent structure authorized by NWP #21 is less than 480 acres, the Cabinet “shall” issue a water quality certification containing only the standard conditions set out in other parts of the statute. If the watershed is to be greater than 480 acres, the Cabinet may require a water quality certification containing additional conditions. Further, a water quality certification may require mitigation at a maximum ratio of one acre of mitigation area for every one acre of permanent loss of waters of the Commonwealth. Such mitigation may be on or off the permitted area, and mitigation banking may be utilized.

During the 2002 Kentucky legislative session, there was an unsuccessful attempt to amend KRS 224.16-070 to allow certain additional types of activities to serve as acceptable mitigation for compensation for the loss of stream in connection with water quality certifications from Kentucky in connection with NWP #21. House Bill 798 would have authorized such

\textsuperscript{14} This legislation is codified at KRS 224.16-070
activities as expending costs to extend public sewer lines to areas where homes were discharging raw sewage into streams, and other similar “public works” type projects that would have a direct effect on the water quality of the Commonwealth. Specifically this bill would have allowed as compensatory mitigation such things as (1) removing sediment control structures at abandoned sites and restoring the stream where the applicant had no legal responsibility to do so; (2) improving impaired streams; (3) constructing new or upgraded existing wastewater treatment facilities of local communities or homeowners; (4) extending sanitary sewer lines to areas not presently served; (5) funding the preparation of wastewater facility plans; (6) relocating local road segments directly impacting water quality and aquatic habitat (other than roads already permitted and bonded under KRS Chapter 350); (5) purchasing conservation easements to protect riparian zones. This legislation was not enacted primarily because there was insufficient time in the session to enable it to be properly considered.

In addition to publishing general conditions for water quality certifications, the Kentucky Division of Water has also established “Section 401 Water Quality Certification Conditions for Nationwide Permit #21 Within the Commonwealth of Kentucky.” These may be accessed on the Division of Water’s website at www.water.nr.state.ky.us/wq/wqcertification/NW21.htm.

Water quality certifications can be a powerful tool in the hands of a state to prevent or to place significant conditions on a proposal to conduct mountaintop removal and its attendant use of valley fills. Care must be taken to insure that all of the requisite steps are taken to satisfy Division of Water requirements/concerns as part of the overall regulatory strategy and approval process. Without Division of Water approval, a coal operator will go nowhere on its proposal to
construct a valley fill. It should be noted, however, that a denial of a water quality certification or unreasonable conditions may be challenged administratively and then judicially.

IV. CURRENT STATUS OF PERMIT APPLICATIONS WITH THE CORPS

The starting point with the Corps during this interim period prior to the preparation of the joint CORPS/OSM/EPA/FWS programmatic EIS on mountaintop mining/valley fills and prior to the promulgation of a final EPA/Corps rule on redefining “fill material” are the terms of the settlement agreement that grew out of the Bragg litigation in West Virginia. As mentioned, this agreement provided that the Corps would limit the application of NWP #21 to fills that, measured from the toe of the fill, drained an area 250 acres or less. Fills that drained larger areas would require an individual § 404 permit. A question still remains as to whether the 250 acre cutoff is limited to single fills or could be interpreted to mean multiple fills on the same permit which, when considered cumulatively, drain more than 250 acres. An additional question exists as to whether the Corps can authorize or deny fill construction under a nationwide permit, regardless of the drainage area, without a site-specific evaluation of the cumulative impacts on the aquatic environment as mandated by the CWA and the §404 (b)(1) guidelines. In general, it appears that coal operators in West Virginia are intentionally designing proposed fills so that they do not individually receive drainage from more than 250 acres to avoid triggering the individual permit process. However, a number of operators in West Virginia have also applied for individual §404 permits from the Huntington District of the Corps. To date, only two individual permits have been issued by the Huntington District since the Bragg case settlement agreement. Hobet Mining (which was the subject of the original Bragg lawsuit) and which is a very large
operation, has applied for an individual permit and a site-specific EIS is being performed under NEPA. A public hearing will be held as part of this individual permitting process, and the fate of the permit application is far from certain.

**Mitigation Requirements**

The Corps offices with jurisdiction over mountaintop mining/valley fill-related applications (which are confined to the Appalachian region of the country) are located primarily in Huntington, West Virginia and Louisville, Kentucky. One of the “quirks” of the Corps organization is that the Corps District offices operate somewhat independently of each other and differ occasionally on regulatory issues. The Corps headquarters has published a “Regulatory Guidance Letter (“RGL”)” on October 31, 2001 on mitigation (RGL 01-1) which applies generally to all Corps-issued permits and which emphasizes that mitigation is a “critical element in the Corps’ decisions to issue permits under Section 404 of the CWA and that it is intended to encourage consistency among Corps district offices. However, each Corps District office still operates somewhat independently. The “sense” of the RGL is that the Corps would be imposing tougher standards for mitigation plans. The Huntington and Louisville District offices of the

15 The other Corps District offices with jurisdiction in Appalachia are Memphis and Nashville which have jurisdiction over watersheds in portions of the Mississippi and its tributaries, the Cumberland River, Red River, Rockcastle River, Clarks River, Laurel River, Poor Fork of the Cumberland River, Big South Fork of the Cumberland River and Little South Fork-Tennessee River.

16 The Corps RGL 01-1 was created in response to a June, 2001 report by the National Research Council, an arm of the National Academy of Science, which found that permits were inadequate to protect the aquatic ecosystems. The Corps guidance letter adopts a system of credits and debits regarding disturbed acreage to better account for the comparability of the mitigation project. The Corps would consider the use of off-site mitigation projects when on-site mitigation was not practical.
Corps have been evolving or developing their policy on mitigation during the past few years. The Huntington District office had traditionally been looking to the respective state water regulatory agencies to approve an operator's mitigation plan, while the Louisville District established an eastern Kentucky field office which conducts site visits and take a more proactive approach to mitigation. An unpublished "grid" system was implemented by the Louisville District which calculated the number of feet of stream to be disturbed, the quality of the streams (ephemeral, intermittent or perennial), applied certain multipliers and came up with the "cumulative impact" of the proposed fill.

**In-lieu Fee-Based Mitigation**

Another concept that has evolved is the use by both Districts of so-called "in-lieu fee-based" mitigation which means the payment of money to offset adverse impacts to streams to be used in lieu of on-site or off-site stream mitigation. This fee-based mitigation is discussed in a "draft" memorandum from the Corps which states that the applicant may elect to pay a fee to compensate for the loss of aquatic habitat, and that the fee will be calculated based on the length of the stream(s) times the mitigation ratio times $100 times 1.2. In a letter to the Corps dated October 30, 2001, the Kentucky Coal Association ("KCA") complained about the uncertainty in the in-lieu fee-based mitigation, indicating that while the Louisville District used the above-described formula for calculating the amount of fee, the Huntington District used $200,000 an acre. While this may change in the weeks or months ahead, the Louisville District is currently

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17 The memo notes that for purposes of determining the length of stream affected, the stream is defined as a channel having "a recognizable bed and bank. For disturbances in ephemeral streams we will need to determine the upper limit of the stream so as to minimize the length of stream to be affected. The factor of 1.2 in the above formula was explained as being a regional adjustment of cumulative impacts."
using a somewhat more refined version of the above-described grid, incorporating additional ecological information based upon a site-specific evaluation by the Eastern Kentucky office of the Louisville District. The Huntington District is currently still calculating the fee on the basis of the acreage of stream affected at the rate of $200,000 per acre. A number of operators are opting to use in-lieu fee-based mitigation because of the lack of suitable on-site or off-site streams on which to perform mitigation activities. Potential offsite streams are frequently off-limits because of problems with landowner approval, access and the like.

V. CONCLUSION.

As described above, there are a myriad of agencies that are engaged in either (or all) of the following: litigation, rulemaking, environmental impact statement preparation, internal policy development and permitting decisions, all of which pertain, directly or indirectly, to mountaintop mining/valley fill activity. Superimposed on all of this activity are the political ramifications of agency decisions relating to these issues. In such an environment, it is difficult to predict how all of this will work out in the end. It appears that ultimately each federal agency that is involved in the process (the Corps, EPA, OSM, and FWS) must get guidance from the White House on how the Bush Administration wants to play this in view of the high profile these issues are achieving. In the interim, coal companies and regulators are muddling through this maze with regard to pending and new applications for permits and authorizations to conduct mountaintop removal mining and valley fill construction.
DEPARTMENT OF DEFENSE

Department of the Army, Corps of Engineers

33 CFR Part 323

ENVIRONMENTAL PROTECTION AGENCY

40 CFR Part 232

Final Revisions to the Clean Water Act Regulatory Definitions of "Fill Material" and "Discharge of Fill Material"

AGENCIES: U.S. Army Corps of Engineers, Department of the Army, DoD; and Environmental Protection Agency.

ACTION: Final rule.

SUMMARY: The U.S. Army Corps of Engineers (Corps) and the Environmental Protection Agency (EPA) are promulgating a final rule to reconcile our Clean Water Act (CWA) section 404 regulations defining the term "fill material" and to amend our definitions of "discharge of fill material." Today's final rule completes the rulemaking process initiated by the April 20, 2000, proposal in which we jointly proposed to amend our respective regulations so that both agencies would have identical definitions of these key terms. The proposal was intended to clarify the Section 404 regulatory framework and generally to be consistent with existing regulatory practice. Today's final rule satisfies those goals.

Today's final rule defines "fill material" in both the Corps' and EPA's regulations as material placed in waters of the U.S. where the material has the effect of either replacing any portion of a water of the United States with dry land or changing the bottom elevation of any portion of a water. The examples of "fill material" identified in today's rule include rock, sand, soil, clay, plastics, construction debris, wood chips, overburden from mining or other excavation activities, and materials used to create any structure or infrastructure in waters of the U.S. This rule retains the effects-based approach of the April 2000 proposal and reflects the approach in EPA's longstanding regulations. Today's final rule, however, includes an explicit exclusion from the definition of "fill material" for trash or garbage.

Today's final rule also includes several clarifying changes to the term "discharge of fill material." Specifically, the term "infrastructure" has been added in several places following the term "structure" to further define the situations where the placement of fill material is considered a "discharge of fill material." In addition, the phrases "placement of fill material for construction or
maintenance of any liner, berm, or other infrastructure associated with solid waste landfills' and 'placement of overburden, slurry, or tailings or similar mining-related materials' have been added to the definition of 'discharge of fill material' to provide further clarification of the types of activities regulated under section 404.

As indicated in the proposal, as a general matter, this final rule will not modify existing regulatory practice. Today's final rule, which establishes uniform language for the Corps' and EPA's definitions of 'fill material' and 'discharge of fill material,' will enhance the agencies' ability to protect aquatic resources by ensuring more consistent and effective implementation of CWA requirements.

EFFECTIVE DATE: June 10, 2002.

FOR FURTHER INFORMATION CONTACT: For information on today's rule, contact either Mr. Thaddeus J. Rugiel, U.S. Army Corps of Engineers, ATTN CECW- OR, 441 "G" Street, NW., Washington, DC 20314-1000, phone: (202) 761-4595, e-mail address: thaddeus.j.rugiel@hq02.usace.army.mil, or Ms. Brenda Mallory, U.S. Environmental Protection Agency, EPA West, Office of Wetlands, Oceans and Watersheds (4502T), 1200 Pennsylvania Avenue, NW., Washington, DC 20460, phone: (202) 566-1368, e-mail address: mallory.brenda@epa.gov.

SUPPLEMENTARY INFORMATION:

I. Background

A. Potentially Regulated Entities

Persons or entities that discharge material to waters of the U.S. that has the effect of replacing any portion of a water of the U.S. with dry land or changing the bottom elevation of any portion of a water of the U.S. could be regulated by today's rule. The CWA generally prohibits the discharge of pollutants into waters of the U.S. without a permit issued by EPA, or a State or Tribe approved by EPA under section 402 of the Act, or, in the case of dredged or fill material, by the Corps or an approved State or Tribe under section 404 of the Act. Today's final rule addresses the CWA section 404 program's definitions of "fill material" and "discharge of fill material," which are important for determining whether a particular discharge is subject to regulation under CWA section 404. Today's final rule reconciles EPA's and the Corps' differing definitions of "fill material" and provides further clarification for the regulated public on what constitutes a "discharge of fill material." Examples of entities potentially regulated include:

<table>
<thead>
<tr>
<th>Category</th>
<th>Examples of potentially regulated entities</th>
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<tbody>
<tr>
<td>State/Tribal governments or</td>
<td>State/Tribal agencies or instrumentalities that discharge material that has the effect of replacing any portion of a water of the U.S. with dry land or changing the bottom elevation of a water of the U.S.</td>
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<td>instrumentalities.</td>
<td></td>
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<tr>
<td>Local governments or instrumentalities</td>
<td>Local governments or instrumentalities that discharge material that has the effect of replacing any portion of a water of the U.S. with dry land or changing the bottom elevation of a water of the U.S.</td>
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</tbody>
</table>

2 of 27
Federal government agencies or instrumentalities.

Industrial, commercial, or agricultural entities.

Land developers and landowners.......

This table is not intended to be exhaustive, but rather provides a guide for readers regarding entities that are likely to be regulated by this action. This table lists the types of entities that we are now aware of that could potentially be regulated by this action. Other types of entities not listed in the table also could be regulated. To determine whether your organization or its activities are regulated by this action, you should carefully examine the applicability criteria in sections 230.2 of Title 40 and 323.2 of Title 33 of the Code of Federal Regulations, as well as the preamble discussion in Section II of today's final rule. If you have questions regarding the applicability of this action to a particular entity, consult the persons listed in the preceding section entitled FOR FURTHER INFORMATION CONTACT.

B. Summary of Regulatory History Leading to Final Rule and Related Litigation

The CWA governs the "discharge" of "pollutants" into "navigable waters," which are defined as "waters of the United States." Specifically, Section 301 of the CWA generally prohibits the discharge of pollutants into waters of the U.S., except in accordance with the requirements of one of the two permitting programs established under the CWA: Section 404, which regulates the discharge of dredged or fill material, or section 402, which regulates all other pollutants under the National Pollutant Discharge Elimination System (NPDES) program. Section 404 is primarily administered by the Corps, or States/Tribes that have assumed the program pursuant to section 404(g), with input and oversight by EPA. In contrast, Section 402 and the remainder of the CWA are administered by EPA or approved States or Tribes. The CWA defines the term "pollutant" to include materials such as rock, sand, and cellar dirt that often serve as "fill material." The CWA, however, does not define the terms "fill material" and "discharge of fill material," leaving it to the agencies to adopt definitions consistent with the statutory framework of the CWA.

Prior to 1977, both the Corps and EPA had defined "fill material" as "any pollutant used to create fill in the traditional sense of replacing an aquatic area with dry land or of changing the bottom elevation of a water body for any purpose." * * *' 40 FR 31325 (July
In 1977, the Corps amended its definition of "fill material" to add a "primary purpose test," and specifically excluded from that definition material that was discharged primarily to dispose of waste. 42 FR 37130 (July 19, 1977). This change was adopted by the Corps because it recognized that some discharges of solid waste materials technically fit the definition of fill material; however, the Corps believed that such waste materials should not be subject to regulation under the CWA section 404 program. Specifically, the Corps' definition of "fill material" adopted in 1977 reads as follows:

(e) The term "fill material" means any material used for the primary purpose of replacing an aquatic area with dry land or of changing the bottom elevation of an [sic] water body. The term does not include any pollutant discharged into the water primarily to dispose of waste, as that activity is regulated under section 402 of the Clean Water Act." 33 CFR 323.2(e) (2001) (emphasis added).

EPA did not amend its regulations to adopt a "primary purpose test" similar to that used by the Corps. Instead, the EPA regulations at 40 CFR 232.2 defined "fill material" as "any pollutant which replaces portions of the 'waters of the United States' with dry land or which changes the bottom elevation of a water body for any purpose" (emphasis added). EPA's definition focused on the effect of the material (an effects-based test), rather than the purpose of the discharge in determining whether it would be regulated by section 404 or section 402.

C. April 2000 Proposal

These differing definitions of "fill material" have resulted in some confusion for some members of the regulated community which has not promoted effective implementation of the CWA. See 65 FR at 21294. As a result, in April 2000, the agencies proposed revisions to their respective definitions of "fill material" and "discharge of fill material," adopting a single effects-based definition similar to that in EPA's regulations. The April 2000 proposed rule defined "fill material" as material that has the effect of replacing any portion of a water of the U.S. with dry land, or changing the bottom elevation of any portion of a water of the U.S. The agencies believe that an effects-based definition is, as a general matter, the most effective approach for identifying discharges that are regulated as "fill material" under section 404. Thus, the proposal removed from the Corps' definition the "primary purpose" test and the provision excluding pollutants discharged into water primarily to dispose of waste.

The April 2000 proposal also would have excluded from the definition discharges subject to an EPA proposed or promulgated effluent limitation guideline or standard under CWA sections 301, 304, 306, or discharges covered under a NPDES permit under CWA section 402. Finally, the April 2000 proposal solicited comments on the idea of the agencies creating an "unsuitable fill" category in the regulations that would identify materials that the Corps District Engineer could determine were not appropriate as fill material and, consequently, refuse to process an application seeking authorization to discharge such material.

In the preamble for the April 2000 proposal, the agencies discussed the need to address the confusion created by the agencies' differing definitions. While in practice some Corps Districts and EPA Regions have developed consistent approaches for determining whether proposed activities would result in a discharge of fill material, national uniformity will ensure better environmental results. Moreover, two judicial decisions discussed in the April 2000 proposal, Resource Investments Incorporated v. U.S. Army Corps of Engineers, 151 F. 3d 1162 (9th Cir. 1998) ("RII") and Bragg v. Robertson, (Civil Action No. 2:98-636, S.D. W. Va.), vacated on other grounds, 248 F. 3d 275
(4th Cir. 2001) (''Bragg''), indicate that the differing EPA and Corps definitions can result in judicial decisions that further confuse the regulatory context. See 65 FR at 21294-95. The clarification in the April 2000 proposal was intended to promote clearer understanding and application of our regulatory programs.

With respect to the term "discharge of fill material,' the April 2000 proposal also included several clarifying changes. Unlike the definition of "fill material,' EPA's and the Corps' then-existing regulations defining the term "discharge of fill material" were substantively identical. The proposed changes to the term were intended to provide further clarification of the issue. Specifically, the proposal provided for adding two phrases to the definition: (1) "Placement of fill material for construction or maintenance of liners, berms, and other infrastructure associated with solid waste landfills; and (2) "placement of coal mining overburden.'

As summarized in more detail in the U.S. Army Corps of Engineers' and Environmental Protection Agency's Response to Comments on the April 20, 2000, Proposed Rule Revising the Clean Water Act Regulatory Definitions of "Fill Material" and "Discharge of Fill Material," dated May 3, 2002 ("Response to Comments''), we received a number of comments addressing these proposed changes. The comments and the above-referenced document are part of the administrative record for this rule and are available from either agency. See the section entitled FOR FURTHER INFORMATION CONTACT.

II. Discussion of Final Rule

A. Overall Summary of Comments

We received over 17,200 comments on the proposed rule, including several hundred late comments, most of which consisted of identical or substantially identical e-mails, letters, and postcards opposing the rule. (In April 2002, an additional several thousand letters and e-mails were sent opposing the adoption of a rule similar to the proposal.) Approximately 500 of the original comments consisted of more individualized letters, with a mixture of those comments supporting and opposing the rule. The comments of environmental groups and the various form letters were strongly opposed to the proposal, in particular, the elimination of the waste exclusion and the discussion in the preamble regarding treatment of unsuitable fill material. Except for several landfill representatives, comments from the regulated community generally supported the proposal, in particular, the fact that the rule would create uniform definitions of "fill material" for the Corps' and EPA's rules and maintain regulation of certain discharges under section 404 as opposed to section 402 of the CWA. A detailed discussion of the issues raised in the comments and the agencies' responses can be found in the Response to Comments document.

The April 2000 proposal would have achieved four major outcomes and these were the focus of many of the comments. These outcomes were (1) Conforming the EPA and Corps definitions of "fill material" to one another; (2) adopting an effects-based

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test, as opposed to the Corps' primary purpose test, for defining "fill material;" (3) eliminating the waste exclusion from the Corps' regulation; and (4) soliciting comments on whether to develop a definition for "unsuitable fill material.' A summary of comments relating to these four issues and our responses are discussed in section II.B of this preamble, which describes today's final rule.

In addition, comments asserted the need for the agencies to prepare an environmental impact statement (EIS) in order to comply with the National Environmental Policy Act; and questioned the consistency of the April 2000 proposal with the CWA, existing judicial decisions, and agency guidance documents. These comments are addressed in this section
of the preamble.

With respect to the need for an EIS, many of the comments opposing the adoption of the rule argued that an EIS should have been prepared, particularly to address the impacts of eliminating the waste exclusion. Supporters of an EIS rejected the notion that the issues will be addressed in the individual permit situations. First, they pointed out that many of the mining activities have historically been permitted under the nationwide permit program where truncated environmental review occurs and no individual NEPA analysis is undertaken. Second, they argued that the cumulative impacts often are not appropriately addressed in this context. As described in section III. J of this final preamble and in the Response to Comments document, the agencies have concluded that preparation of an EIS is not required for this rule pursuant to NEPA. While supporters of an EIS suggest that finalizing this rule will result in significant new discharges that previously would not have occurred, that is not the case. Although the rule will clarify the appropriate regulatory framework, we do not expect there to be any significant change in the nature and scope of discharges that will occur.

Finally, a number of comments asserted that the proposal should not be finalized because it violated the then-existing law (e.g., CWA, Bragg, and RII). Other comments argued that the proposal was consistent with the CWA and current regulatory practice. We do not agree that the proposal or today's final rule violate the CWA or any other law. Moreover, we believe that agencies have an obligation to take whatever steps may be necessary, including making revisions to their regulations, to ensure that their programs are appropriately implementing statutory mandates. As indicated, the Corps and EPA believe that the current inconsistency between their respective definitions of "fill material" is impeding the effective implementation of the section 404 program. Under those circumstances, we believe that a change in the regulatory language is justified and that by adopting the substance of EPA's longstanding definition, we are minimizing potential confusion and disruption to the program, while remaining consistent with the CWA. We agree with those comments that recognize the consistency of our action with the CWA and current practice. As described in more detail in the Response to Comments document and sections II. B and D of this preamble, today's final rule clarifies the governing regulatory framework in a manner consistent with the CWA and existing practice.

B. Discussion of the Final Rule

1. Definition of "Fill Material"

Today's final rule modifies both the EPA's and Corps' existing definitions of "fill material" and has retained the effects-based approach set forth in the proposal. The final rule defines "fill material" as material placed in waters of the U.S. where the material has the effect of either replacing any portion of a water of the United States with dry land or changing the bottom elevation of any portion of a water. The examples of "fill material" identified in today's rule include rock, sand, soil, clay, plastics, construction debris, wood chips, overburden from mining or other excavation activities, and materials used to create any structure or infrastructure in waters of the U.S. The proposed rule only specifically identified rock, earth and sand as examples, but the preamble made it clear that these were merely illustrative. In addition, in the preamble to the proposal, we indicated that wood chips, coal mining overburden, and similar materials would also constitute "fill material" if they had the effect of fill. As a result of questions raised in the comments about the scope of the term "fill material," we have included additional examples in the final rule, several of which were discussed in the proposed preamble. We believe that these additional examples will further clarify the rule.

Although today's final rule adopts a general effects-based approach for defining "fill material," it specifically excludes trash or
garbage. Today's final rule does not modify any other Section 404 jurisdictional terms or alter any procedures governing the individual or general permit processes for Section 404 authorizations, requirements under Section 402, or the governing permit programs. Following is a summary of the actions that the agencies have taken in response to public comments.

a. Reconciling Agencies' Definitions

The majority of the comments from both the environmental and industry perspectives addressing the issue of whether the agencies should have identical definitions expressed the general view that the agencies should have the same definitions for the key jurisdictional terms "fill material" and "discharge of fill material." Many of the comments also noted that the differences between the Corps' and EPA's rules have historically caused confusion for the regulated community. Several asserted that despite differences in the regulatory language, some Corps Districts have been applying an effects-based test for some time. As described in the Response to Comments document, the agencies agree with those comments supporting the promulgation in both the Corps' and EPA's regulations of a uniform definition for the terms "fill material" and "discharge of fill material." Today's final rule achieves this result.

b. Effects-Based Test

Most of the comments supported the proposed rule's use of an effects-based test similar to EPA's longstanding definition for defining "fill material" and the elimination of the "primary purpose" test from the Corps regulations. Those disagreeing with such an approach gave a variety of reasons including, the lack of any demonstrated justification that eliminating the primary purpose test from the Corps' regulation was necessary; the existence of similar purpose tests in other statutes involving waste materials as well as in the Section 404(b)(1) Guidelines as demonstrating that such tests need not be unwieldy; the existence of alternative ways of addressing the issues of concern without resorting to this rule change; and concerns about the inappropriate expansion of section 404 jurisdiction. As will be explained, the agencies are not persuaded by these arguments.

First, we believe that the objective standard created by the effects-based test will yield more consistent results in determining what is "fill material" and will provide greater certainty in the implementation of the program. We believe that these benefits provide sufficient justification for today's rule change. In addition, although similar "purpose" tests may be used under other statutes and even under the section 404 program, this does not negate the difficulties we have faced in applying the primary purpose test, as well as some confusion that has resulted from the use of the subjective primary purpose test in the section 404 jurisdictional context. An objective, effects-based standard also helps ensure that discharges with similar environmental effects will be treated in a similar manner under the regulatory program. The subjective, purpose-based standard led in some cases to inconsistent treatment of similar discharges, a result which hampers effective implementation of the statute.

Moreover, we believe there is an important distinction between the use of a purpose test here, where it determines the basic jurisdiction of the section 404 versus the section 402 program, and its use in the other contexts, such as in the evaluation of whether alternatives to a discharge of dredged material are "practicable" within the meaning of the section 404(b)(1) Guidelines. See 40 CFR 230.10(a)(2). The use of project purpose in the latter case is appropriate because it would make no sense to consider an alternative "practicable" if it did not
satisfy the basic or overall purpose of the project proposed by the applicant. The definition of fill material, on the other hand, determines which legal requirements must be met for a discharge to be authorized under the statute. In that circumstance, we believe it is important to use an objective, effects-based test that ensures consistent treatment of like discharges, and prevents uncertainty for the regulated community as to what regulatory program applies to particular discharges. Moreover, we disagree that alternatives other than a rulemaking could have adequately addressed the agencies' concerns since the facial differences in our regulations could only be completely reconciled by revising the rules. In addition, the agencies previously had attempted to clarify their interpretation of the rules in a 1986 Memorandum of Agreement (MOA). Nevertheless, issues persisted.

Finally, we disagree that the rule causes an inappropriate expansion of section 404 jurisdiction. The CWA does not limit section 404 jurisdiction over fill material to materials meeting the primary purpose test. The "primary purpose test" is a regulatory definition and within the agencies province to modify as long as the modification is consistent with the CWA. In sum, as described in the Response to Comments document, the final rule, just as the proposal, adopts an effects-based approach to defining fill material. We believe the clarity and consistency created by the agencies relying on a more objective test for defining these key jurisdictional terms will result in more effective regulation under the CWA.

c. Elimination of Waste Exclusion

Many comments opposed the proposal to eliminate the waste exclusion from the Corps' regulation. Some of these comments recommended that, in addition to the effects-based test, the agencies should include a general exclusion from the definition of "fill material" for any discharge of "waste." These comments asserted that such an approach provides the advantages of EPA's effects-based approach while more effectively implementing the Corps' exclusion of waste material from regulation under section 404. Some of the comments argued that the proposed rule's deletion of the waste exclusion language from the Corps' regulations violates the CWA. According to these comments, while waste material can permissibly be covered by section 404 when it is placed in waters for a beneficial purpose, the CWA categorically prohibits authorizing such discharges under section 404 when their purpose is waste disposal. These comments pointed to the decisions in RII and Bragg to argue that all waste material is outside the scope of section 404.

These comments do not object to, nor claim that the CWA prohibits, issuance of a section 404 permit for waste material discharged into waters of the U.S. under all circumstances. Where waste is discharged for a purpose other than waste disposal (e.g., to create fast land for development), these comments acknowledged that the Corps' issuance of a section 404 permit in accordance with the section 404(b)(1) Guidelines adequately protects the environment and is consistent with the CWA. On this point, we agree. However, where the identical material—with identical environmental effects—is discharges into waters for purposes of waste disposal, the comments contend that issuance of a section 404 permit in accordance with the Guidelines would neither protect the environment nor be allowed by the CWA. Here, we disagree.

Simply because a material is disposed of for purposes of waste disposal does not, in our view, justify excluding it categorically from the definition of fill. Some waste (e.g., mine overburden) consists of material such as soil, rock and earth, that is similar to "traditional" fill material used for purposes of creating fast land for development. In addition, other kinds of waste having the effect of fill (e.g., certain other mining wastes) can, unlike trash or garbage, be indistinguishable either upon discharge or over time from structures created for purposes of creating fast land. Given the similarities of some discharges of waste to "traditional" fill, we believe that a
categorical exclusion for waste would be over-broad. Instead, where a waste has the effect of fill, we believe that regulation under the section 404 program is appropriate.

This does not mean, however, that today's rule opens up waters of the U.S. to be filled for any waste disposal purposes. As explained previously, today's rule is generally consistent with current agency practice and so it does not expand the types of discharges that will be covered under section 404. The section 404(b)(1) Guidelines provide for a demonstration that there are no less damaging alternatives to the discharge, and that all appropriate and practicable steps have been taken to avoid, minimize and compensate for any effects on the waters. We recognize that, some fill material may exhibit characteristics, such as chemical contamination, which may be of environmental concern in certain circumstances. This is true under either a primary purpose or effects based definition of fill material. The section 404 permitting process, however, is expressly designed to address the entire range of environmental concerns arising from discharges of dredged or fill material. See 40 CFR Part 230, subparts C-G (containing comprehensive provisions for addressing physical, chemical and biological impacts of discharges).

The 404(b)(1) guidelines provide a comprehensive means of evaluating whether any discharge of fill material, regardless of its purpose, is environmentally acceptable and therefore may be discharged in accordance with the CWA. Where the practicable alternatives test has been satisfied and all practicable steps have been taken both to minimize effects on the aquatic environment and to compensate for the loss of aquatic functions and values, we believe the section 404 permitting process is adequate to ensure protection of the aquatic ecosystem for any pollutant that fills waters. There is no environmental basis for contending that the sufficiency of the permitting process to protect waters of the U.S. depends on the purpose of the discharge.

The position reflected in some of the comments appears to be based on the contention that Congress did not intend for waste disposal to be a permissible purpose of discharging pollutants into waters of the U.S. While we agree that

Congress wanted to prevent utilization of waters as unlicensed dumping grounds for waste material, the Act as a whole is focused primarily on discharges of waste material, as shown by the Act's definition of pollutant, which includes solid waste, sewage, garbage, discarded equipment, industrial, municipal and agricultural waste. See CWA section 502(6). While the elimination of all discharges is an important goal of the Act (see CWA section 101(a)(1)), the Act seeks to meet that goal not by banning discharges of waste outright, but by imposing carefully tailored restrictions on discharges of pollutants based on factors such as the impact of the discharge on the receiving water, availability of treatment technologies, cost, and the availability of alternatives to the discharge. See, e.g., CWA sections 301(b), 304(b) (requiring discharges to meet technology-based effluent limitations guidelines and standards); section 306(a)(1) (defining new source performance standard to include no discharge of pollutants "where practicable"); section 301(b)(1)(C) (requiring dischargers to comply with any more stringent limitations necessary to meet water quality standards); sections 404(b)(1) and 403(c)(1)(F) (requiring that 404(b)(1) Guidelines be based on section 403(c) criteria, which include consideration of "other possible locations" of disposal).

Nor do we think that there is any indication that Congress intended to exclude discharges for purposes of waste disposal entirely from coverage under section 404. For example, section 404 applies to "dredged material" (referred to as dredged "spoil" in the definition of pollutant in section 502(6)), which is typically discharged not for any beneficial purpose, but as a waste product from a dredging operation. Moreover, section 404(a) authorizes the Corps to
issue permits for discharges of dredged or fill material at specified "disposal" sites. Congress' use of the word "disposal" supports the reasonableness of our view that regulating waste material having the effect of fill under section 404 is consistent with the Act.

We also disagree with the interpretation of some of the comments on the RII and Bragg decisions as mandating that the Corps retain the current exclusion of waste disposal in the definition of fill material. We note first that the decision of the district court in Bragg has been vacated by the Fourth Circuit on 11th amendment grounds. Bragg v. Robertson, 72 F. Supp. 2d 642 (S.D. W. Va. 1999), rev'd, 248 F. 3d 275 (4th Cir. 2001). In any event, both Bragg and RII applied the Corps' then-existing definition of fill material to conclude that certain discharges were not covered by section 404. Nothing in those decisions suggests that the Act itself precluded the regulation of waste materials with the effect of fill under section 404. Nothing in those decisions suggests that the Act itself precluded the regulation of waste materials with the effect of fill under section 404. See section II. D. of this preamble for further discussion of the RII decision. While we agree that trash or garbage generally should be excluded from the definition of fill material (for the reasons explained in section II.B.1d of this preamble), we do not agree that an exclusion for all waste is appropriate and have not included such a provision in today's rule. These issues are discussed in section II.B.1d of the preamble and are addressed more fully in the Response to Comments document.

d. Trash or Garbage

The agencies have added an exclusion for trash or garbage to the definition of "fill material" for several reasons. First, the preamble to the proposed rule and many of the comments recognized that trash or garbage, such as debris, junk cars, used tires, discarded kitchen appliances, and similar materials, are not appropriately used, as a general matter, for fill material in waters of the U.S. In particular, we agree that the discharge of trash or garbage often results in adverse environmental impacts to waters of the U.S. by creating physical obstructions that alter the natural hydrology of waters and may cause physical hazards as well as other environmental effects. We also agree that these impacts are generally avoidable because there are alternative clean and safe forms of fill material that can be used to accomplish project objectives and because there are widely available landfills and other approved facilities for disposal of trash or garbage.

Accordingly, a party may not obtain a section 404 permit to dispose of trash or garbage in regulated waters. Because the discharge of any pollutant into jurisdictional waters is prohibited under CWA section 301 except in accordance with a permit issued under sections 404 or 402, section 402 would govern such discharges. For many of the reasons identified in this preamble, such as the physical obstruction and hazards that such materials would create in waters of the U.S., we would emphasize that trash or garbage are unlikely to be eligible to receive a permit under the section 402 regulatory program. We also note that where such materials are placed in waters of the U.S. without a permit, EPA or an approved State/Tribal agency with permitting authority, remains the lead enforcement agency. Today's rule does not affect the application of section 402 of the CWA to discharges of pollutants other than fill material that may be associated with such things as solid waste landfill structures and mine impoundments. Where such structures release pollutants into waters of the U.S., a permit under section 402 of the CWA is required that will ensure protection of any downstream waters, including compliance with State water quality standards.

While the agencies have generally excluded materials characterized as trash or garbage from the definition of "fill material," we agree that there are very specific circumstances where certain types of material that might otherwise be considered trash or garbage may be appropriate for use in a particular project to create a structure or infrastructure in waters of the U.S. In such situations, this material
would be regulated as fill material. Such material would have to be suitably cleaned up and not include constituents that would cause significant environmental degradation. An example would be where recycled porcelain fixtures are cleaned and placed in waters of the U.S. to create environmentally beneficial artificial reefs. Such material would not be considered trash or garbage and thus would not be subject to the exclusion. The agencies believe that this is appropriate, and even environmentally beneficial, in situations where (1) the otherwise excluded materials are being placed in waters of the U.S. in a manner consistent with traditional uses of fill material to create a structure or infrastructure, (2) the material's characteristics are suitable to the project purpose, and (3) the review under section 404 can effectively ensure that the material will not cause or contribute to significant environmental degradation.

We also note that as stated in the preamble to the proposal, it is important to draw a clear distinction between solid waste discharged directly into waters of the U.S. and sanitary solid waste landfills. With respect to solid waste landfills, the liners, berms, and other infrastructure that are constructed of fill materials in waters of the U.S. are regulated under section 404 of the CWA. In the case of a landfill that has received a section 404 permit for the placement of berms, dikes, liners and similar activities needed to construct the facility, the subsequent disposal of solid waste into the landfill, while subject to regulation under the RCRA, would not be subject to regulation under the CWA because the constructed facility is not waters of the U.S. As with current practice, discharges of leachate from landfills into waters of the U.S. would remain subject to CWA section 402. Today's final rule does not change this general regulatory framework for landfills. See section II D of this preamble for further discussion.

e. Unsuitable Fill Material

With respect to developing a potential definition of "unsuitable fill material," there was almost unanimous opposition to the unsuitable fill concept as discussed in the preamble. Some comments viewed it as an inadequate substitute for the elimination of the waste exclusion. Others argued that having an unsuitable fill provision would be a good idea but that it would need to be much broader and to specifically include mining-related wastes. These commenters also objected to leaving the question of whether something was "unsuitable fill material" to the discretion of the District Engineer. Some comments expressed concern that the definition of unsuitable fill material focused on materials that have a potential to leach or that have toxic constituents in toxic amounts. They argued that the definition could result in prohibiting activities that with appropriate permit terms and conditions potentially are allowable under section 404. They also argued that such issues should be addressed in the context of the permitting process and should not result in the permit application being rejected. As described in the Response to Comments document, the agencies have not included an unsuitable fill category in the final rule but, as discussed, the final rule does narrow the scope of "fill material" by excluding trash or garbage.

f. Effluent Guideline Limitations and 402 Permits

In addition to the changes already discussed in this preamble, today's final rule also deletes the exclusion contained in the proposal for discharges covered by effluent limitation guidelines or standards or NPDES permits. Several of the comments raised concerns that the exclusion included in the proposed definition for discharges covered by proposed or existing effluent limitation guidelines or standards or NPDES permits was vague and would result in uncertainty with respect to
the regulation of certain discharges. Other comments stated that it was inappropriate for rule language to allow reliance on proposed effluent limitation guidelines or standards before they are promulgated as a final rule. In addition, including the language in the actual rule could raise questions as to whether the reference to effluent guidelines was meant to refer only to those in existence at the time today's rule was promulgated or whether the reference was prospective.

In light of the concerns and confusion associated with the proposed provision, we have decided to delete it from the rule. However, although we have removed the language in question from the rule itself, we emphasize that today's rule generally is intended to maintain our existing approach to regulating pollutants under either section 402 or 404 of the CWA. Effluent limitation guidelines and new source performance standards ("effluent guidelines") promulgated under section 304 and 306 of the CWA establish limitations and standards for specified wastestreams from industrial categories, and those limitations and standards are incorporated into permits issued under section 402 of the Act. EPA has never sought to regulate fill material under effluent guidelines. Rather, effluent guidelines restrict discharges of pollutants from identified wastestreams based upon the pollutant reduction capabilities of available treatment technologies. Recognizing that some discharges (such as suspended or settleable solids) can have the associated effect, over time, of raising the bottom elevation of a water due to settling of waterborne pollutants, we do not consider such pollutants to be "fill material," and nothing in today's rule changes that view. Nor does today's rule change any determination we have made regarding discharges that are subject to an effluent limitation guideline and standards, which will continue to be regulated under section 402 of the CWA. Similarly, this rule does not alter the manner in which water quality standards currently apply under the section 402 or the section 404 programs.

2. Definition of "Discharge of Fill Material"

Most of the comments addressing "discharge of fill material" supported the inclusion of items related to solid waste landfills, although several asserted that the regulation of discharges associated with solid waste landfills was inconsistent with the court's decision in Resource Investments Inc. v. U.S. Army Corps of Engineers, 151 F.3d 1162 (9th Cir. 1998). See detailed discussion in section II. D of this final preamble. With respect to the placement of coal mining overburden, two diametrically opposed views were reflected in the comments. Many of the comments argued that coal overburden was "waste" material and that allowing such discharges was a violation of the CWA. In contrast, other comments argued that focusing on "coal mining overburden" was confusing, because it created the impression that the overburden or similar materials from other mining processes may not be regulated as "discharges of fill material."

Today's final rule responds to the comments in the following ways. First, the agencies continue to agree with those comments that supported including the placement of material associated with construction and maintenance of solid waste landfills and related facilities in the discharge of fill material. For the reasons discussed in section II. D of this final preamble and in the Response to Comments document, we do not agree that we are precluded by the RII decision from issuing a rule that defines "fill material" or the "discharge of fill material" as encompassing discharges associated with the construction of solid waste landfill infrastructures. Second, the agencies have modified the "placement of coal mining overburden" to read "placement of overburden, slurry, or tailings or similar mining-related materials." The language in today's final rule will clarify that any mining-related material that has the effect of fill when discharged will be regulated as "fill material." We made this clarification because it was clear from the comments that some were reading the examples we identified as an exclusive list. The general intent of this rule is to cover materials that have the effect of fill, not simply to focus on any one industrial activity. We believe that the additional mining related examples will address the confusion reflected
in the comments. Finally, as discussed in section II.B.1.c of this preamble, we do not agree that the CWA contains a blanket prohibition precluding discharges of "waste" materials in to waters of the U.S. Instead, the Act establishes the framework for regulating discharges into waters and we believe the section 404 program is the most appropriate vehicle for regulating overburden and other mining-related materials. Several other minor changes, editorial in nature, have also been made in today's final rule.

C. Appropriate Reliance on the Environmental Reviews Conducted by Other Federal or State Programs

As indicated, today's rule is designed to improve the effective implementation of the section 404 program by having the Corps and EPA adopt a single, uniform definition for these key jurisdictional terms. We also believe

that we can improve the effective implementation of the program by placing greater emphasis on coordination among the Federal agencies and with relevant State and Tribal programs. There are numerous examples of where the agencies can effectively work together and with other State, Tribal and Federal programs in the review of proposed projects that involve a section 404 discharge to jointly develop information that is relevant and reliable. Projects involving discharges to waters of the U.S. are often subject to review under other Federal and State permit programs, including the RCRA, the Surface Mining Control and Reclamation Act (SMCRA), the Coastal Zone Management Act (CZMA), CWA Section 402 NPDES, and others. Examples where closer coordination may be beneficial include the review of proposed solid waste landfills under the CWA and RCRA, proposed highway projects under the CWA and NEPA, proposed mining projects under the CWA and SMCRA, and proposed coastal restoration projects under the CWA and CZMA.

As EPA and the Corps implement today's rule, we will be placing even greater emphasis on effective coordination with other relevant State, Tribal and Federal programs and, consistent with our legal responsibilities, on reliance, as appropriate, on the information developed and conclusions reached by other agencies to support the decisions required under these programs and ours. We are confident that this coordination will serve to make the implementation of today's rule and, more broadly, the CWA section 404 program, more effective, consistent and environmentally protective.

Some comments expressed concern that an effects-based approach to the definition of "fill material" would result in a duplication of effort among Federal programs and an increased workload for the Corps. We believe that more effective coordination among the State, Tribal and Federal agencies and appropriate reliance on the analyses of other agencies will help significantly to address these concerns.

First, it is important to note that EPA and Corps regulations encourage coordination and allow for appropriate reliance on relevant information and analyses developed under other programs to help satisfy section 404 program requirements. In the most effective circumstances, the Corps is able to coordinate with other relevant State, Tribal and Federal agencies before and during project review to identify the most efficient and effective role for each agency and ensure mutual reliance on information and analyses, particularly where that reliance is consistent with individual agency expertise and experience. For example, for many years, subject to advice from EPA, the Corps has relied on State determinations regarding water quality matters, as those State determinations are reflected in State CWA section 401 water quality certifications (see 33 CFR 320.4(d)). Such Corps reliance on State water quality determinations will continue for discharges associated with activities such as mining and solid waste landfills. In regulating discharges associated with mining, close coordination with the State, Tribal and Federal entities responsible for implementation
of SMCRA, CWA section 401 and section 402 will enable the Corps to take advantage of the specialized expertise of the agencies as the Corps completes the section 404 review. Such coordination also helps to reduce the costs associated with project reviews, promotes consistent and predictable decision-making, and ultimately ensures the most effective protection for human health and the environment. EPA and the Corps anticipate that Corps District offices will rely on State/Federal site selection under SMCRA regarding the siting of coal mining related discharges to the extent allowed under current law and regulations. Similarly, the Corps will make full use of State RCRA information regarding the siting, design and construction of solid waste landfills, and will defer to those State decisions to the extent allowed by current law and regulation.

Both agencies recognize, however, that the Corps is ultimately responsible under the CWA for making the required determinations that support each permit decision based on the Corps' independent evaluation of the record. The Corps itself determines the extent of deference to information generated from other programs including, for example, site selection under SMCRA and RCRA, that is appropriate on a case-by-case basis. Ultimately the Corps is relying on, rather than relinquishing to, these other sources of information as a record is developed and the Corps makes the determinations required by the Section 404 regulatory program. For example, the Corps will make full use of State site selection decisions under SMCRA (e.g., coal slurry impoundments) and RCRA (e.g., solid waste landfills), but the Corps will independently review those decisions and the State processes that generated them, to ensure that any Corps permit decision for a discharge site will fully comply with NEPA, the section 404(b)(1) Guidelines, and other relevant legal requirements. The Corps and EPA believe that effective coordination with other State and Federal agencies and the information they develop will help the Corps continue to make more timely, consistent and environmentally protective permit decisions.

D. The Final Rule and the Resource Investments Decision

In Resource Investments Inc v. Corps, 151 F.3d 1162 (9th Cir. 1998), the Ninth Circuit held that the Corps lacked the authority to regulate a solid waste landfill in waters of the U.S. The court found that: (1) Neither the solid waste itself nor the liner consisting of layers of gravel and low-permeability soil constituted "fill material" under Corps regulations; and (2) because of the potential for inconsistent results if landfills were regulated under both section 404 of the CWA and Subtitle D of RCRA, requiring these facilities to be subject solely to RCRA would "harmonize" the statutes.

We discussed this decision in the preamble to the proposed rule as an example of some of the confusion engendered by the "primary purpose" test. The court found in RII that the liner was not fill material because its primary purpose was not to replace an aquatic area with dry land or change the bottom elevation of a waterbody, "but rather to serve as a leak detection and collection system." 151 F.3d at 1168. We explained in the proposal that fills typically serve some other purpose than just creating dry land or raising a water's bottom elevation and that, if the court's reasoning were taken to its logical conclusion, many traditional fills in waters of the U.S. would not be subject to section 404.

Some commenters objected to our proposal not to follow the decision in RII in this rulemaking. They criticized the proposal as an improper attempt to "override" or "overrule" the Ninth Circuit's decision, particularly within the Ninth Circuit where the decision is binding. They also argued that the proposed rule failed to address the potential for duplication and inconsistency in decision-making by State and Federal agencies identified in RII.

In our view, these comments raise two distinct issues. The first is whether we should follow the RII decision outside the Ninth Circuit and cease regulating discharges associated with the construction of solid waste landfills under section 404. The second issue is whether RII
Regarding the first question, we note first that, after RII was decided, we chose not to acquiesce in the decision outside the Ninth Circuit. While we agreed that the solid waste disposal placed in a landfill is not fill material (and such waste continues to be excluded under today's rule), we believed that the court misapplied the primary purpose test in the Corps' regulations, and that the court's conclusion that RCRA supplanted CWA regulation was contrary to Congressional intent. See Resource Investments Inc. et al. v. Corps, No. 97-35934 (Government's Petition for Rehearing and Suggestion for Rehearing En Banc, September 30, 1998). Thus, after the court decided RII, the Corps has continued to issue section 404 permits for the construction of solid waste landfill infrastructures outside the Ninth Circuit.

After considering public comments, we continue to decline to follow RII outside the Ninth Circuit and have, therefore, maintained the approach in the proposed rule to the regulation of solid waste landfills. The revisions to the Corps' definition of fill material in today's rule address the basis for the court's holding that the landfill did not involve the discharge of fill material under section 404. For the reasons explained elsewhere in today's notice, we believe that an effects-based test is the appropriate means of evaluating whether a pollutant is "fill material" and should be regulated under section 402 as opposed to section 404 of the CWA. The placement of berms, liners and other infrastructure (such as roads) associated with construction of a solid waste landfill in waters of the U.S. has the effect of replacing water with dry land or raising the bottom elevation of a water. Therefore, under today's rule, they constitute fill material. Such discharges are indistinguishable from similar discharges associated with other construction activity, which the Corps has always regulated as fill under section 404. See 40 CFR 232.2; 33 CFR 323.2 (defining "discharge of fill material," to include "fill that is necessary for the construction of any structure in a water of the U.S.; the building of any structure or impoundment requiring rock, sand, dirt or other material for its construction; site-development fills for recreational, industrial, commercial, residential and other uses; causeways or road fills; * * *")]. We have amended our definition of this term to include the "placement of fill material for construction or maintenance of any liner, berm, or other infrastructure associated with solid waste landfills." That amendment does not change substantively the prior definition, but merely adds solid waste landfills as an example to make clear that it constitutes a "discharge of fill material." Thus, under our new regulations, discharges associated with the creation of solid waste landfill structures clearly constitute "fill material."

To the extent some commenters asserted that revising our regulation was an improper attempt to "overrule" or "override" this holding in RII, we disagree. The court's analysis of the "fill material" in RII was based entirely on the Corps regulations as they existed at that time, and not upon the interpretation of the CWA itself. Moreover, the CWA does not define "fill material." Therefore, both the statute and the Ninth Circuit's decision leave us the discretion to adopt a reasonable definition consistent with the statutory scheme. We have explained elsewhere why we believe today's definition of fill is reasonable and appropriate under the CWA. To the extent today's rule has the practical effect of "overriding" this aspect of the court's decision in RII, that is neither remarkable nor inappropriate, since it is entirely proper for agencies to consider and, if appropriate, revise their regulations in light of judicial interpretation of them.

For purposes of deciding whether to apply the RII decision outside the Ninth Circuit, we have also evaluated the second basis for the
court's decision—that regulation solely under Subtitle D of RCRA instead of section 404 would 'harmonize' the statutes and avoid necessary duplication. We decline to follow that holding both on legal and policy grounds. First, we believe, notwithstanding RII, that eliminating the CWA permitting requirement on the grounds that an activity is regulated under RCRA is contrary to Congressional intent in both statutes. Second, we do not agree with the court that regulation under Subtitle D and section 404 would constitute unnecessary duplication, in light of the distinct purposes served by these authorities, the differing Federal roles under the two statutes, and our clarification in today's rulemaking of our intent to give all appropriate deference to State RCRA decision-making in the section 404 permitting process.

We first do not agree with the court's legal reasons for concluding that regulation under Subtitle D of RCRA supplants CWA regulation. The CWA prohibits the discharge of any pollutant into waters of the U.S. without a permit under the Act. See CWA section 301(a). Even though an activity associated with a discharge may be regulated under other Federal or State authorities, we believe there is not any basis to conclude that such regulation by itself makes section 301(a) of the Act inapplicable to a discharge of a pollutant into waters of the U.S. In effect, the court concluded that enactment of a regulatory scheme under Subtitle D of RCRA impliedly repealed the statutory permit requirement under the CWA. But "the intention of the legislature to repeal must be clear and manifest." Radzanower v. Touche Ross & Co., 426 U.S. 148, 154 (1976), and the court must conclude that the two acts are in irreconcilable conflict or that the later act covers the whole subject of the earlier one and is clearly intended as a substitute. Id. The court in RII did not, and could not, make these findings.

In fact, Congress itself made precisely the opposite findings when it enacted RCRA. Section 1006(a) states:

Nothing in this chapter shall be construed to apply to (or to authorize any State, interstate, or local authority to regulate) any activity or substance which is subject to the [CWA] except to the extent such application (or regulation) is not inconsistent with the requirements of (the CWA).

This provision precludes regulation of solid waste landfills under Subtitle D in a manner inconsistent with the requirements of the CWA. In our view, it is plainly "inconsistent" with the requirements of the CWA to hold that regulation under RCRA eliminates CWA permitting requirement altogether.

Instead, the court relied upon certain Corps regulations, statements by Corps officials and a 1986 interagency MOA. The court first stated that applying section 404 to solid waste landfills was "unreasonable" because there would be "potentially inconsistent results" where both the State and the Corps were applying the same criteria in regulating solid waste landfills. 151 F.3d at 1169. The court held that this "regulatory overlap is inconsistent with Corps regulations stating that "the Corps believes that State and Federal regulatory programs should complement rather than duplicate one another." 33 CFR 320.1(a)(5). In addition, the court cited statements by the Corps in a 1984 letter to EPA stating that EPA was in a better position than the Corps to regulate solid waste landfills. Finally, the court cited the 1986 MOA between the Corps and EPA. However, none of these "authorities" purport to modify the statutory

permitting requirements of the CWA, nor could they. The Corps' regulation cited by the court is simply a statement of the Corps' policy objective of working in concert with State regulatory programs, an important and continuing Corps objective that was discussed previously. The Corps' letter and the MOA reflected our efforts to
manage our programs in light of our differing definitions of fill material, but did not speak to the CWA statutory permitting requirement. The court also misconstrued the 1986 MOA entered into by EPA and the Corps as indicating we intended to make the regulation of solid waste facilities within "the sole purview of the EPA and affected states" after EPA promulgated certain Subtitle D regulations. 151 F.3d at 1169. In fact, we stated,

EPA and Army agree that consideration given to the control of discharges of solid waste both in waters of the United States and upland shall take into account the results of studies being implemented under the 1984 Hazardous and Solid Waste Amendments (HSWA) to the Resource Conservation and Recovery Act (RCRA), signed into law on November 8, 1984. . . .

Unless extended by mutual agreement, the agreement will expire at such time as EPA has accomplished specified steps in its implementation of RCRA, at which time the results of the study of the adequacy of the existing Subtitle D criteria and proposed revisions to the Subtitle D criteria for solid waste disposal facilities, including those that may receive hazardous household wastes and small quantity generator waste, will be known. In addition, data resulting from actions under the interim agreement can be considered at that time.

It should be noted that this MOA is about the regulation of solid waste disposal, not about the construction of infrastructure, including solid waste landfill infrastructure, that involves discharges of fill material to waters of the U.S. We did not address in the MOA how solid waste landfills would be regulated after EPA completed its study and certain RCRA regulations, but said only that these developments would "be taken into account" as we decided how to address these discharges in the future. Thus, in addition to the inability of the agencies as a legal matter to modify the CWA statutory permitting requirement through an MOA, we expressly reserved any judgment about the appropriate regulatory approach to be taken after certain actions were taken under RCRA. The court appears to have assumed that the MOA expired after we completed the specified steps under RCRA, and that regulatory authority over solid waste landfills thereafter became the sole purview of RCRA. In fact, the MOA did not expire, and it has continued to provide the framework for regulation of solid waste landfills under section 404 of the CWA. See Memorandum of John F. Studt, U.S. Army Corps of Engineers, May 17, 1993 (stating "the subject MOA remains effective in its entirety until further notice" and noting that this position was coordinated with EPA).

We conclude, therefore, that it would be contrary to the language and intent of both the CWA and RCRA to conclude that RCRA subtitle D supplants the CWA permitting requirement for discharges into waters of the U.S. associated with the construction of solid waste landfills. The different Federal roles in the permitting schemes in these statutes supports this conclusion. Subtitle D provides that each State will "adopt and implement a permit program or other system of prior approval and conditions" to assure that each solid waste management facility within the State "will comply" with criteria established by EPA for the siting, design, construction, operation and closure of solid waste landfills. RCRA section 4005(c)(1)(B). States are required to submit permit programs for EPA to review and EPA is required to "determine whether each State has developed an adequate program" to ensure compliance with EPA's Subtitle D regulations. RCRA section 4005(c)(1)(B) and (C). However, RCRA does not grant to EPA authority to issue permits for solid waste landfills, review State permitting decisions or enforce Subtitle D requirements in States with approved programs. The court in RII appeared to misunderstand EPA's authorities under Subtitle D of RCRA when it stated that EPA would be the permitting authority in the absence of an approved State program. See 151 F.3d 1169 ("we hold that when a proposed project affecting a wetlands area is a solid waste landfill, the EPA (or the approved State
program) . . . will have the permit authority under RCRA.'') (Emphasis added); 151 F.3d at 1167 (``RCRA gives the EPA authority to issue permits for the disposal of solid waste, but allows states to substitute their own permit programs for the Federal program if the State program is approved by EPA.''). While this authority exists with regard to disposal of hazardous waste under Subtitle C of RCRA, EPA does not have this authority with regard to disposal of non-hazardous solid waste under Subtitle D.

In contrast, the CWA requires either a Federal permit for discharges of pollutants into waters of the U.S., or issuance of a permit by a State/Tribe with an approved program, subject to EPA's authority to object to a permit where EPA finds it fails to meet the guidelines and requirements of the CWA. CWA sections 402(d); 404(j). EPA also has authority under the CWA to enforce conditions in Federal or State permits under the Act. CWA section 309.

These contrasting statutory schemes support the conclusion that eliminating CWA authority over discharges of fill material associated with construction of solid waste landfills would mean a significant departure from the statutory structure created by Congress in the CWA, a scheme which Congress expressly sought to preserve when it adopted RCRA. See RCRA section 1006(a). This does not mean that we view the Federal role as one of second-guessing every decision made by State regulatory authorities under RCRA. To the contrary, both RCRA and the CWA reflect a strong presumption in favor of State-administered regulatory programs. As discussed elsewhere, we intend to rely on State decision-making under RCRA to the extent allowed under current law and regulations. However, we believe that eliminating a Federal role entirely on these matters is neither appropriate nor consistent with Congressional intent under RCRA or the CWA.

Thus, we decline to follow the decision in RII outside the Ninth Circuit because we conclude there is not an adequate legal basis on which to conclude that discharges of pollutants associated with solid waste landfills no longer need to be authorized by a CWA permit solely because the project receives a permit under Subtitle D of RCRA.

We nonetheless share the basic policy perspective expressed by the court in RII about the need to avoid unnecessary duplication and potential inconsistent application of regulatory programs under the CWA and RCRA. In fact, RCRA expressly vests EPA with the responsibility to "integrate all provisions of (RCRA) for purposes of administration and enforcement and (to) avoid duplication, to the maximum extent practicable, with the appropriate provisions of the * * * (CWA). * * * Such integration shall be effected only to the extent that it can be done in a manner consistent with the goals and policies of this chapter and the CWA. * * *" RCRA section 1006(b). EPA has sought such integration first by promulgating location restrictions for landfills that are consistent with the criteria for issuance of section 404 permits. See 40 CFR 258.12; 230.10. Among other requirements, a landfill may not be located in wetlands unless it is demonstrated to the State that there

[Page 31139]

are not less environmentally damaging practicable alternatives, the facility will not cause significant degradation of wetlands, and that appropriate and practicable steps have been taken to mitigate the loss of wetlands from the facility. However, EPA never purported to substitute Subtitle D regulation for the CWA permitting requirement, a result that would violate both section 1006(a) and (b). Instead, the Subtitle D RCRA regulations make clear that owners or operators of municipal solid waste landfills "must comply with any other applicable Federal rules, laws, regulations, or other requirements." 40 CFR 258.3. At the time EPA promulgated this regulation, the agency expressly noted that such requirements include those arising under the CWA. See 56 FR 51042 (October 9, 1991).

We do not believe, however, that the Subtitle D and section 404 programs are redundant. Rather, each program has a distinct focus. The
State RCRA permitting process addresses a much broader range of issues, including technical operating and design criteria, ground water monitoring, corrective action, closure and post-closure care and financial assurances. In contrast, the section 404 process is focused exclusively on the impacts of discharges of dredged or fill material on the aquatic ecosystem, and ways of ensuring that those impacts are avoided, minimized and compensated. Because of the Corps' expertise in protecting aquatic ecosystems, we have found that State RCRA permitting agencies often incorporate by reference the requirements of section 404 permits. (For example, the State RCRA permit for the RII landfill required the applicant to implement the wetlands and mitigation plan to be approved by the Corps through the 404 permit process.) We believe that, in these and other ways, State and Federal permitting authorities can create efficiencies by relying on each other's expertise in making regulatory decisions.

We intend to make additional efforts to avoid unnecessary duplication in the Federal and State permitting process. As explained in section II. C of this final preamble, we intend that the Corps will rely on decisions by the State RCRA authority about the siting, design and construction of solid waste landfills in waters of the U.S. to the extent allowed by law and regulations. Appropriate deference to State decision-making will help avoid duplication, while still ensuring that the Corps fulfills its responsibilities to authorize discharges of fill material associated with solid waste landfills in accordance with CWA requirements.

This does not mean that, in every single case, State and Federal decision-makers will agree on whether a particular project or configuration is environmentally acceptable. Nevertheless, instances of disagreement have been rare. We intend to further enhance our efforts to ensure effective coordination between State and Federal officials. However, we do not agree with the court in RII that the only way to avoid unnecessary duplication is to eliminate the CWA permitting requirement altogether.

We next address commenters' assertions that the decision in RII continues to preclude us from regulating solid waste landfills under section 404 within the Ninth Circuit. These comments also argue that, given the 'statutory' basis for the court's decision, we cannot change the result in the Ninth Circuit through this rulemaking.

As noted in this preamble, the court construed administrative materials of the Corps and EPA as supporting the conclusion that the agencies did not intend to regulate solid waste landfills under section 404 of the CWA. In light of this agency intent, the court concluded that subjecting landfills to regulation solely under RCRA would "harmonize" the statutes and "give effect to each [statute] while preserving their sense and purpose." 151 F.3d at 1169. The court found that this harmonization "is consistent with the sense of the CWA that discharges of solid waste materials are beyond the scope of section 404 . . . and avoids unnecessary duplication of Federal and State efforts in the area of wetlands protection." Id.

We again emphasize the distinction between "discharges of solid waste material," as referenced by the court and discharges of fill material associated with the construction of infrastructure. In this rulemaking, we have clarified that discharges having the effect of raising the bottom elevation of a water or replacing water with dry land, including fill used to create landfills such as liners, berms and other infrastructure associated with solid waste landfills are discharges of fill material subject to the section 404 program. Therefore, we have altered the landscape as understood by the court in RII (i.e., that these facilities were entirely outside the intended purview of section 404). We do not agree with commenters who argued that there was a "statutory" basis to the court's decision in the sense that the holding of the decision turned on an interpretation of Congressional intent in the CWA or RCRA. The court did not cite any provision of the CWA or RCRA to support its conclusions. Rather, the court derived the "sense and purpose" of the CWA based on agency regulations, guidance and correspondence. By clarifying the scope of
section 404 authorities in this rulemaking, we have altered the "sense and purpose" of the CWA underlying the court's conclusion that regulation solely under RCRA would "harmonize" the statutes. Because the premises before the court have changed, we do not view the court's decision as continuing to bar the regulation under section 404 of discharges associated with solid waste landfills within the Ninth Circuit. At a minimum, today's rule calls into question the continuing vitality of the court's reasoning and conclusions and, should a case be brought within the Ninth Circuit challenging our authority to regulate solid waste landfills, we would ask the court to address the question anew in light of the clarification of our authorities in today's rule.

III. Administrative Requirements

A. Plain Language

In compliance with the principle in Executive Order 12866 regarding plain language, this preamble is written using plain language. Thus, the use of "we" in this notice refers to EPA and the Corps, and the use of "you" refers to the reader. We have also used active voice, short sentences, and common every day terms except for necessary technical terms.

B. Paperwork Reduction Act

This action does not impose any new information collection burden under the provisions of the Paperwork Production Act, 44 U.S.C. 3501 et seq. This rule merely reconciles EPA and Corps CWA section 404 regulations defining the term "fill material" and amends our definitions of "discharge of fill material." Thus, this action is not subject to the Paperwork Reduction Act.

Burden means the total time, effort, or financial resources expended by persons to generate, maintain, retain, or disclose or provide information to or for a Federal agency. This includes the time needed to review instructions; develop, acquire, install, and utilize technology and systems for the purposes of collecting, validating, and verifying information, processing and maintaining information, and disclosing and providing information; adjust the existing ways to comply with any previously applicable instructions and requirements; train personnel to be able to respond to a collection of information; search data sources; complete and review the collection of information; and transmit or otherwise disclose the information.

An Agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number. The OMB control numbers for EPA's regulations are displayed in 40 CFR part 9 and 48 CFR chapter 15. For the CWA section regulatory 404 program, the current OMB approval number for information requirements is maintained by the Corps of Engineers (OMB approval number 0710-0003, expires December 31, 2004).

C. Executive Order 12866

Under Executive Order 12866 (58 FR 51735, October 4, 1993), EPA and the Corps must determine whether the regulatory action is "significant" and therefore subject to review by the Office of Management and Budget (OMB) and the requirements of the Executive Order. The Order defines "significant regulatory action" as one that is likely to result in a rule that may:

(1) Have an annual effect on the economy of $100 million or more or adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or Tribal governments or communities;
(2) Create a serious inconsistency or otherwise interfere with an action taken or planned by another agency;

(3) Materially alter the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof; or

(4) Raise novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in the Executive Order.

Pursuant to the terms of Executive Order 12866, it has been determined that this rule is a "significant regulatory action" in light of the provisions of paragraph (4) above. As such, this action was submitted to OMB for review. Changes made in response to OMB suggestions or recommendations will be documented in the public record.

D. Executive Order 13132

Executive Order 13132, entitled "Federalism" (64 FR 43255, August 10, 1999), requires EPA and the Corps to develop an accountable process to ensure "meaningful and timely input by State and local officials in the development of regulatory policies that have Federalism implications."

"Policies that have Federalism implications" is defined in the Executive Order to include regulations that have "substantial direct effects on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government."

This final rule does not have Federalism implications. It will not have substantial direct effects on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government, as specified in Executive Order 13132. Currently, under the CWA, any discharge of pollutants into waters of the U.S. requires a permit under either section 402 or 404 of the CWA. Today's rule conforms our two regulatory definitions of "fill material" and thereby clarifies whether a particular discharge is subject to regulation under section 402 or Section 404. It is generally consistent with current agency practice and does not impose new substantive requirements. Within California, Oregon, Washington, Idaho, Wyoming, Nevada, Arizona, Hawaii, Guam, and the Northern Mariana Islands, after today's rule, the Corps will again be issuing Section 404 permits for the construction of solid waste landfills in waters of the U.S., which the Corps had ceased doing after the decision in RII (the decision did not affect the permitting requirement outside these states). See section II. D. of this preamble. However, resuming the issuance of section 404 permits for construction of solid waste landfills in waters of the U.S. in these areas does not have Federalism implications. None of the States within the Ninth Circuit will incur administrative costs as a result of today's rule, because none currently administer the section 404 program and, in any event, the administrative costs of permitting solid waste landfills are minimal in the context of the overall section 404 permitting program. In addition, this change does not impose any additional substantive obligations on State or local governments seeking to construct solid waste landfills in waters of the U.S. since Subtitle D of RCRA currently requires such facilities to meet comparable conditions for receiving a section 404 permit. See section II. D of this preamble. Finally, we do not believe that requiring any State or local governments seeking to construct solid waste landfills in waters of the U.S. to undergo the Section 404 permitting process itself will have substantial direct effects on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government. Thus, Executive Order 13132 does not apply to this rule.

E. Regulatory Flexibility Act (RFA), as Amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA), 5 U.S.C. 601 et seq.
The RFA generally requires an agency to prepare a regulatory flexibility analysis of any rule subject to notice-and-comment rulemaking requirements under the Administrative Procedure Act or any other statute unless the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities. Small entities include small businesses, small organizations and small governmental jurisdictions.

For purposes of assessing the impacts of today's rule on small entities, a small entity is defined as: (1) A small business based on SBA size standards; (2) a small governmental jurisdiction that is a government of a city, county, town, school district, or special district with a population of less than 50,000; and (3) a small organization that is any not-for-profit enterprise which is independently owned and operated and is not dominant in its field.

After considering the economic impacts of today's final rule on small entities, we certify that this action will not have a significant economic impact on a substantial number of small entities. Currently, under the CWA, any discharge of pollutants into waters of the U.S. requires a permit under either section 402 or 404 of the CWA. Today's rule conforms our two regulatory definitions of "fill material" and thereby clarifies whether a particular discharge is subject to regulation under section 402 or section 404. Today's rule is generally consistent with current agency practice, does not impose new substantive requirements and therefore would not have a significant economic impact on a substantial number of small entities.

F. Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA), Public Law 104-4, establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and Tribal governments and the private sector. Under section 202 of the UMRA, the agencies generally must prepare a written statement, including a cost-benefit analysis, for proposed and final rules with "Federal mandates" that may result in expenditures to State, local, and Tribal governments, in the aggregate, or to the private sector, of $100 million or more in any one year. Before promulgating an EPA or Corps rule for which a written statement is needed, section 205 of the UMRA generally requires the agencies to identify and consider a reasonable number of regulatory alternatives and adopt the least costly, most cost-effective or least burdensome alternative that achieves the objectives of the rule. The provisions of section 205 do not apply when they are inconsistent with applicable law. Moreover, section 205 allows EPA and the Corps to adopt an alternative other than the least costly, most cost-effective or least burdensome alternative if the Administrator and Secretary of the Army publish with the final rule an explanation why that alternative was not adopted. Before EPA or the Corps establishes any regulatory requirements that may significantly or uniquely affect small governments, including Tribal governments, they must have developed under section 203 of the UMRA a small government agency plan. The plan must provide for notifying potentially affected small governments, enabling officials of affected small governments to have meaningful and timely input in the development of EPA or Corps regulatory proposals with significant Federal intergovernmental mandates, and informing, educating, and advising small governments on compliance with the regulatory requirements.

We have determined that this rule does not contain a Federal mandate that may result in expenditures of $100 million or more for State, local, and Tribal governments, in the aggregate, or the private sector in any one year. Currently, under the CWA, any discharge of pollutants into waters of the U.S. requires a permit under either section 402 or 404 of the CWA. Today's rule conforms our two regulatory
definitions of "fill material" and thereby clarifies whether a particular discharge is subject to regulation under section 402 or section 404. Today's rule is generally consistent with current agency practice, does not impose new substantive requirements and therefore does not contain a Federal mandate that may result in expenditures of $100 million or more for State, local, and Tribal governments, in the aggregate, or the private sector in any one year. Thus, today's rule is not subject to the requirements of sections 202 and 205 of the UMRA.

For the same reasons, we have determined that this rule contains no regulatory requirements that might significantly or uniquely affect small governments. Thus today's rule is not subject to the requirements of section 203 of UMRA.

G. National Technology Transfer and Advancement Act

As noted in the proposed rule, Section 12(d) of the National Technology Transfer and Advancement Act of 1995 (the NTTAA), Public Law 104-113, section 12(d) (15 U.S.C. 272 note) directs us to use voluntary consensus standards in our regulatory activities unless to do so would be inconsistent with applicable law or otherwise impractical. Voluntary consensus standards are technical standards (e.g., materials specifications, test methods, sampling procedures, and business practices) that are developed or adopted by voluntary consensus standards bodies. The NTTAA directs us to provide Congress, through OMB, explanations when we decide not to use available and applicable voluntary consensus standards.

This rule does not involve technical standards. Therefore, we did not consider the use of any voluntary consensus standards.

H. Executive Order 13045

Executive Order 13045: "Protection of Children from Environmental Health Risks and Safety Risks" (62 FR 19885, April 23, 1997) applies to any rule that: (1) Is determined to be "economically significant" as defined under Executive Order 12866, and (2) concerns an environmental health or safety risk that we have reason to believe may have a disproportionate effect on children. If the regulatory action meets both criteria, we must evaluate the environmental health or safety effects of the planned rule on children, and explain why the planned regulation is preferable to other potentially effective and reasonably feasible alternatives considered by us.

This final rule is not subject to the Executive Order because it is not economically significant as defined in Executive Order 12866. In addition, it does not concern an environmental or safety risk that we have reason to believe may have a disproportionate effect on children.

I. Executive Order 13175

Executive Order 13175, entitled "Consultation and Coordination with Indian Tribal Governments" (65 FR 67249, November 6, 2000), requires the agencies to develop an accountable process to ensure "meaningful and timely input by tribal officials in the development of regulatory policies that have tribal implications." "Policies that have tribal implications" is defined in the Executive Order to include regulations that have "substantial direct effects on one or more Indian tribes, on the relationship between the Federal government and the Indian tribes, or on the distribution of power and responsibilities between the Federal government and Indian tribes."

Today's rule does not have tribal implications. It will not have substantial direct effects on tribal governments, on the relationship between the Federal government and the Indian tribes, or on the distribution of power and responsibilities between the Federal government and Indian tribes, as specified in Executive Order 13175. Currently, under the CWA, any discharge of pollutants into waters of the U.S. requires a permit under either section 402 or 404 of the CWA. Today's rule conforms our two regulatory definitions of "fill
material" and thereby clarifies whether a particular discharge is subject to regulation under section 402 or section 404. It is generally consistent with current agency practice and does not impose new substantive requirements. Within California, Oregon, Washington, Idaho, Wyoming, Nevada, Arizona, Hawaii, Guam, and the Northern Mariana Islands, after today's rule, the Corps will again be issuing Section 404 permits for the construction of solid waste landfills in waters of the U.S., which the Corps had ceased doing after the decision in RII (the decision did not affect the permitting requirement outside these states). See section II. D. of this preamble. However, resuming the issuance of section 404 permits for construction of solid waste landfills in waters of the U.S. in these areas does not have tribal implications. No tribes within the Ninth Circuit will incur administrative costs as a result of today's rule, because none currently administer the section 404 program and, in any event, the administrative costs of permitting solid waste landfills are minimal in the context of the overall section 404 permitting program. In addition, this change does not impose any additional substantive obligations on any Tribe seeking to construct solid waste landfills in waters of the U.S. since Subtitle D of RCRA currently requires such facilities to meet comparable conditions for receiving a section 404 permit. See section II.D. of this preamble. Finally, we do not believe that requiring any tribal government seeking to construct solid waste landfills in waters of the U.S. to undergo the Section 404 permitting process itself will have substantial direct effects on one or more Indian tribes, on the relationship between the Federal government and the Indian tribes, or on the distribution of power and responsibilities between the Federal government and Indian tribes. Thus, Executive Order 13175 does not apply to this rule.

J. Environmental Documentation

As required by the NEPA, the Corps prepares appropriate environmental documentation for its activities affecting the quality of the human environment. The Corps has prepared an environmental assessment (EA) of the final rule. The Corps' EA ultimately concludes that, since the adoption of this rule will not significantly affect the quality of the human environment, the preparation and coordination of an EIS is not required. The EA, included in the administrative record for today's rule, explains the rationale for the Corps' conclusion.

K. Congressional Review Act

The Congressional Review Act, 5 U.S.C. 801 et seq., as added by the Small Business Regulatory Enforcement Fairness Act of 1996, generally provides that before a rule may take effect, the agency promulgating the rule must submit a rule report, which includes a copy of the rule, to each House of the Congress and to the Comptroller General of the United States. We will submit a report containing this rule and other required information to the U.S. Senate, the U.S. House of Representatives, and the Comptroller General of the United States prior to publication of the rule in the Federal Register. A major rule cannot take effect until 60 days after it is published in the Federal Register. This rule is not a "major rule" as defined by 5 U.S.C. section 804(2). This rule will be effective June 10, 2002.

L. Executive Order 12898

Executive Order 12898 requires that, to the greatest extent practicable and permitted by law, each Federal agency must make achieving environmental justice part of its mission. Executive Order 12898 provides that each Federal agency conduct its programs, policies,
and activities that substantially affect human health or the
environment in a manner that ensures that such programs, policies, and
activities do not have the effect of excluding persons (including
populations) from participation in, denying persons (including
populations) the benefits of, or subjecting persons (including
populations) to discrimination under such programs, policies, and
activities because of their race, color, or national origin.

Today's rule is not expected to negatively impact any community,
and therefore is not expected to cause any disproportionately high and
adverse impacts to minority or low-income communities. Today's rule
relates solely to whether a particular discharge is appropriately
authorized under section 402 or section 404 of the Clean Water Act.
Moreover, the proposed allocation of authority between these programs
is generally consistent with existing agency practice.

M. Executive Order 13211

This rule is not a "significant energy action" as defined in
Executive Order 13211, "Actions Concerning Regulations That
Significantly Affect Energy Supply, Distribution, or Use" (66 FR 28355
(May 22, 2001)) because it is not likely to have a significant adverse
effect on the supply, distribution, or use of energy. Today's rule
conforms our two regulatory definitions of "fill material" and
thereby clarifies whether a particular discharge is subject to
regulation under section 402 or section 404. Today's rule is generally
consistent with current agency practice, does not impose new
substantive requirements and therefore will not have a significant
adverse effect on the supply, distribution, or use of energy.

List of Subjects

33 CFR Part 323

Water pollution control, Waterways.

40 CFR Part 232

Environmental protection, Intergovernmental relations, Water
pollution control.

Corps of Engineers

33 CFR Chapter II

Accordingly, as set forth in the preamble 33 CFR part 323 is
amended as set forth below:

PART 323--[AMENDED]

1. The authority citation for part 323 continues to read as
follows:


2. Amend Sec. 323.2 as follows:
   a. Paragraph (e) is revised.
   b. In paragraph (f), in the second sentence: add the words "or
      infrastructure" after the words "for the construction of any
      structure"; add the word "`, infrastructure," after the words
      "building of any structure"; remove the words "residential, and"
      and add in their place the words "residential, or"; and add the words
      "place of fill material for construction or maintenance of any
      liner, berm, or other infrastructure associated with solid waste
      landfills; placement of overburden, slurry, or tailings or similar
      mining-related materials;" after the words "utility lines;".
      The revision reads as follows:
Sec. 323.2 Definitions.

* * * * *

(e)(1) Except as specified in paragraph (e)(3) of this section, the term fill material means material placed in waters of the United States where the material has the effect of:

(i) Replacing any portion of a water of the United States with dry land; or

(ii) Changing the bottom elevation of any portion of a water of the United States.

(2) Examples of such fill material include, but are not limited to: rock, sand, soil, clay, plastics, construction debris, wood chips, overburden from mining or other excavation activities, and materials used to create any structure or infrastructure in the waters of the United States.

(3) The term fill material does not include trash or garbage.

* * * *

Dominic Izzo,
Principal Deputy Assistant Secretary of the Army (Civil Works),
Department of the Army.

Environmental Protection Agency

40 CFR Chapter I

Accordingly, as set forth in the preamble 40 CFR part 232 is amended as set forth below:

PART 232--[AMENDED]

1. The authority citation for part 232 continues to read as follows:


2. Amend Sec. 232.2 as follows:

a. The definition of "Fill material" is revised.

b. In the definition of "Discharge of fill material", in paragraph (1): add the words "or infrastructure" after the words "for the construction of any structure"; add the word "infrastructure," after the words "building of any structure"; remove the words "residential, and" and add in their place the words "residential, or"; and add the words "placement of fill material for construction or maintenance of any liner, berm, or other infrastructure associated with solid waste landfills; placement of overburden, slurry, or tailings or similar mining-related materials;" after the words "utility lines;".

   The revision reads as follows:

   [[Page 31143]]

Sec. 232.2 Definitions.

* * * * *

Fill material. (1) Except as specified in paragraph (3) of this definition, the term fill material means material placed in waters of the United States where the material has the effect of:

(i) Replacing any portion of a water of the United States with dry land; or

(ii) Changing the bottom elevation of any portion of a water of the United States.
(2) Examples of such fill material include, but are not limited to: rock, sand, soil, clay, plastics, construction debris, wood chips, overburden from mining or other excavation activities, and materials used to create any structure or infrastructure in the waters of the United States.

(3) The term fill material does not include trash or garbage.

* * * * *

Christine Todd Whitman,
Administrator, Environmental Protection Agency.
[FR Doc. 02-11547 Filed 5-8-02; 8:45 am]
BILLING CODE 3710-92-P
IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF WEST VIRGINIA
CHARLESTON DIVISION

KENTUCKIANS FOR THE COMMONWEALTH, INC.,

Plaintiff,

v. CIVIL ACTION NO. 2:01-0770

COLONEL JOHN RIVENBURGH, Colonel,
District Engineer; ROBERT B. FLOWERS,
Lieutenant General, Chief of Engineers
and Commander of the U.S. Army
Corps of Engineers; and MICHAEL D. GHEEN,
Chief of the Regulatory Branch, Operations
and Readiness Division, U.S. Army Corps
of Engineers, Huntington District,

Defendants,

and

KENTUCKY COAL ASSOCIATION,
POCAHONTAS DEVELOPMENT COMPANY, and
AEI RESOURCES, INC.,

Intervenor-Defendants

MEMORANDUM OPINION AND ORDER

Pending are cross motions for summary judgment by Plaintiff Kentuckiians for the Commonwealth, Inc. (KFTC), Defendant officers of the Army Corps of Engineers (Corps), and Intervenor-Defendants on Count One.

The Court holds that § 404 of the Clean Water Act does not allow filling the waters of the United States solely for waste
disposal. Agency rulemaking or permit approval that holds otherwise is *ultra vires*, beyond agency authority conferred by the Clean Water Act. Only the United States Congress can rewrite the Act to allow fills with no purpose or use but the deposit of waste. Accordingly, Plaintiff's motion is **GRANTED** and Defendants' motions are **DENIED**.

I. FACTUAL AND PROCEDURAL BACKGROUND

Purportedly acting under the CWA, 33 U.S.C. § 1344 (§ 404), the Corps has permitted surface coal mining operations to dispose of overburden waste from mountaintop removal coal mining by filling hundreds of miles of streams in Appalachia. Appalachian coal occurs in narrow seams separated by dirt and rock called "overburden" or "spoil." In mountaintop removal mining, the overburden is blasted with explosive charges and pushed out of way to expose the coal seams. The overburden, which is nothing but waste, is disposed of by creating valley fills, that is, literally, filling the valleys with waste rock and dirt. Because mountain streams run into the valleys, creating massive valley fills has the inevitable effect of covering and obliterating many streams and the lifeforms within.

In June 2000 the Huntington (West Virginia) District office of
the Corps' authorized Martin County Coal Corporation's (MCCC's) mountaintop removal coal mining project in Martin County, Kentucky. Authorized under a § 404 nationwide permit, the project would create 27 valley fills, filling 6.3 miles of streams. The vast majority of the nation's valley fills are approved in the Huntington District by the Corps' officials who are Defendants here. Of the 306 NWP-21 permits issued nationwide in the year 2000, 257 were issued in the Corps' Huntington District. Kentuckians for the Commonwealth v. Rivenburgh, 204 F.R.D. 301, 305 n.3 (S.D. W. Va. 2001). All year-2000 NWP-21 permits in the nation impacted a total of 460,575 linear feet (approximately 87 miles) of stream. Id. Ninety-seven percent of stream length affected, or 449,896 linear feet (approximately 85 miles), occurred in the Huntington district under NWP-21 permits authorized here. Id.

In Count One Plaintiff complains that the primary purpose of

1The Corps' Huntington District comprises roughly half the state of Ohio, more than half of West Virginia, portions of eastern Kentucky and western Virginia, and a relatively small area in North Carolina. See Kentuckians for the Commonwealth v. Rivenburgh, 204 F.R.D. 301, 305 (S.D. W. Va. 2001)(explaining Corps' district boundaries are based on the watersheds of major rivers, rather than state lines).

2Nationwide permits (NWPs) are available for activities that "will cause only minimal adverse environmental effects when performed separately, and will have only minimal cumulative adverse effect on the environment." 33 U.S.C. § 1344(e)(1). NWP-21 permits issue for activities associated with surface coal mining.
valley fills is to dispose of waste. Under the Corps' longstanding regulations, waste disposal is not an authorized purpose for a CWA § 404 permit. See 33 C.F.R. § 323.2(e). KFTC asks the Court to find and conclude the Corps has violated § 404 of the CWA, 33 U.S.C. § 1344, and the Administrative Procedures Act (APA), 5 U.S.C. § 706(2), because its actions are arbitrary, capricious, an abuse of discretion, and otherwise contrary to law.

The Corps acknowledges, as it must, that under current Corps' regulations waste disposal cannot be permitted under § 404. According to Defendants, this is a problem created by differences between the Corps' and the EPA's definitions of "fill material," which have "admittedly resulted in confusion." (U.S. Cross Mot. for Summ. J. at 1). For that reason, the agencies have undertaken rulemaking "reconciling" the definitions and "clarifying" that overburden waste may be disposed of in valley fills under CWA § 404.3 (Id.) Additionally, Defendants argue the Court should defer to the Corps' longstanding practice of approving valley fills as "fill material" under § 404.

Both parties moved for summary judgment on these contrary

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3On May 3, 2002, while the Court had these matters under consideration, EPA and the Corps signed for publication in the Federal Register their final rules on fill material and its discharge. The Court considers the proffered rule at II.D.2.
interpretations of CWA § 404 and the Corps' authority to permit waste disposal under the guise of discharge of fill material.

An examination of the Clean Water Act (CWA), its legislative history, its predecessor statutes and regulations, its companion statutes, its longstanding administrative interpretation and judicial gloss has convinced the Court that § 404 was enacted for the purpose and with the effect of allowing disposal of only one type of pollutant or waste: dredged spoil. Permits for disposal of all other pollutants into national waters are to issue under CWA § 402. "Fill material," as regulated under § 404, refers to material deposited for some beneficial primary purpose: for construction work, infrastructure, improvement and development in waters of the United States, not waste material discharged solely to dispose of waste. Accordingly, approval of waste disposal as fill material under § 404 is ultra vires, that is, beyond the authority of either administrative agency, the Corps or Environmental Protection Agency (EPA). To approve disposal of waste other than dredged spoil, in particular mountaintop removal overburden, in waters of the United States under § 404 dredge and fill regulations rewrites the Clean Water Act. Such rewriting exceeds the authority of administrative agencies and requires an act of Congress.
II. DISCUSSION

A. Summary Judgment Standard

Summary judgment is appropriate where there is no genuine issue as to any material fact and judgment may be rendered as a matter of law. Fed. R. Civ. P. 56(c). The parties agree there are no issues of material fact, and the question for the Court is one of law: interpretation of § 404 of the CWA.

B. Agency Authority and the APA

Agency power is "not the power to make law. Rather, it is 'the power to adopt regulations to carry into effect the will of Congress as expressed by the statute.'" Brown & Williamson Tobacco Corp. v. Food & Drug Admin., 153 F.3d 155 (4th Cir. 1998)(quoting Ernst & Ernst v. Hochfelder, 425 U.S. 185, 213-14 (1996)(quoting Manhattan Gen. Equip. Co. v. Comm'n, 297 U.S. 129, 134 (1936))). It is fundamental, even "axiomatic that an administrative agency's power to promulgate legislative regulations is limited to the authority delegated by Congress." Bowen v. Georgetown Univ. Hosp., 488 U.S. 204, 208 (1988). The issue presented is whether Congress intended to delegate to the Corps the authority to permit waste disposal as discharge of fill material under its § 404 dredge and fill permit program, absent a primary constructive purpose.

If a statute is silent or ambiguous on a specific question, a
reviewing court must defer to any reasonable construction of that statute by the administering agency. *Chevron, U.S.A. v. Nat'1 Res. Defense Council*, 467 U.S. 837, 843 (1984). The agency's construction need not be the one the Court itself would adopt or the one the Court feels would best implement Congressional policy. It need only be a reasonable construction of the statutory question at issue. *Id.* at 844-45.

If, however, the Court can ascertain Congress' intent on a particular question by applying the traditional rules of statutory construction, then it must give effect to that intent. *Brown & Williamson*, 153 F.3d at 162 (citing *Chevron* 467 U.S. at 843 n.9). Although the inquiry begins with the language of the statute, it must be considered in context of the whole law, its object and policy. *See id.* Congressional intent may be ascertained further through the overall statutory scheme, legislative history, "the history of evolving congressional regulation in the area," and other relevant statutes. *Id.* (quoting *Dunn v. CFTC*, 519 U.S. 465 (1967))(other citations omitted).

Official actions are *ultra vires* when the official engages in conduct that the sovereign has not authorized. *Larson v. Domestic & Foreign Commerce Corp.*, 337 U.S. 682 (1949). Because administrative agencies have no power to act beyond authority
conferred by Congress, the APA requires a court to “hold unlawful and set aside agency action . . . found to be . . . in excess of statutory jurisdiction, authority, or limitations, or short of statutory right.” 5 U.S.C. § 706(2)(C).

C. The Clean Water Act

The objective of the CWA is “to restore and maintain the chemical, physical, and biological integrity of the nation’s waters.” 33 U.S.C. § 1251(a). To that end, no pollutants may be discharged into the waters of the United States without a CWA permit. See 33 U.S.C. §§ 1311(a), 1362(7) & (12). “Pollutant” includes, inter alia, “dredged spoil,” “solid waste,” “rock, sand, cellar dirt and industrial . . . waste discharged into water.” 33 U.S.C. § 1362(6). The parties agree overburden from mountaintop removal coal mining is a pollutant under the definition and requires a CWA permit.

Two major permit programs, §§ 402 and 404, authorize discharge of pollutants into waters of the United States.\textsuperscript{4} Id. §§ 1342, 1344. Section 402 creates the National Pollutant Discharge

\textsuperscript{4}A third permit program provides for discharge of pollutants “under controlled conditions associated with an approved aquaculture project under Federal or State supervision.” 33 U.S.C. § 1328(a). These three programs are the exclusive permitting programs. See id. § 1342(a).
Elimination System (NPDES), providing permits for discharge of pollutants. Id. § 1342. Section 404 authorizes permits for dredged or fill material. Id. § 1344. Neither "dredged material" nor "fill material" is defined in the statute.\(^5\)

The Secretary of the Army (i.e., the Corps) issues § 404 permits for discharge of dredged or fill material at specified disposal sites. Id. § 1344(a). The EPA Administrator works with the Secretary to develop guidelines for disposal sites, id. § 1344(b), and may prohibit the use of a specified disposal site where a discharge "will have an unacceptable adverse effect on municipal water supplies, shellfish beds and fishery areas (including spawning and breeding areas), wildlife, or recreational areas. Id. § 1344(c).\(^6\) Examination of the legislative history of

\(^5\)Because discharge of all pollutants requires either a § 402 permit or a § 404 dredge and fill permit, Defendants argue "fill material" must be a "pollutant," a waste material, for which § 404 permits are available. As philosophers say, this argument begs the question. It assumes what it wishes to prove. Section 402 only says that "the discharge of any pollutant" must have a permit under § 402, "except as provided" in § 404. It does not say everything provided for in § 404 is pollutant disposal.

\(^6\)Section 1344(c) oversight was invoked by the Deputy Administrator of EPA, W. Michael McCabe, with regard to the MCCC Martin County surface coal mine permit at issue here. After the Corps refused to suspend the NWP-21 permit while EPA investigated, McCabe elevated the issue to the civilian head of the Corps and asked him to overrule the district office.

McCabe stated it was "incredibl[e]" that the Corps believed the MCCC project would only cause minimal adverse environmental (continued...)}
the CWA, which established these central functions and relationships in § 404, demonstrates Congress did not intend § 404 permits to apply to fill discharges solely for waste or pollutant disposal, other than disposal of dredged spoil.

1. Legislative History of the CWA

The initial Senate version of the Federal Water Pollution Control Act (FWPCA)\(^7\) regulated permits for discharge of all pollutants under § 402. Section 402(m) of the original bill treated the discharge of dredged spoil like any other pollutant. See S. Conf. Rep. No. 92-1236 (1972), reprinted in 1 Legislative History of the Water Pollution Control Act Amendments of 1972 (Legt. Hist.), 177.

The American Association of Port Authorities (AAPA) was

\(^6\) (...continued) impacts and that it would qualify for an NWP-21. McCabe explained that EPA had invoked its 404(c) veto authority only 11 times since 1972 and once in the last ten years, and that it takes this action “in only the most serious circumstances out of an unequivocal concern for the protection of human health and the environment.” Compl. ¶ 22.

In March 2001 the Corps denied EPA’s request. It said it would review the project if MCCC began work. In August 2001 MCCC transferred its coal mining permit to Beechfork, which began work.

After KFTC moved for a preliminary injunction, the Corps modified Beechfork’s NWP-21 permit to require compensatory mitigation for the 33,120 feet of stream impacted by the project and prohibit fill discharge until the mitigation plan is approved by the Corps. KFTC then withdrew its motion. Beechfork has informed the Corps it intends to continue mining at the site.

\(^7\) Now commonly known as the “Clean Water Act.”
"extremely concerned" with this proposal. Bills Amending the Federal Water Pollution Control Act and Other Pending Legislation Relating to Water Pollution Control: Hearing Before the Senate Subcommittee on Air and Water Pollution of the Committee on Public Works, 92nd Cong. (Appendix Mar. 15, 1971)(letter from Paul A. Amundsen, Executive Director AAPA).

[S]eaport facilities are dependent on Federal and private channel and pierside dredging, which, in turn, would be affected by the spoil disposal permitting procedure contained in the subject legislation. . . . The handling of spoil material from the dredging site to the containment or disposal area, like [its] planning, is an engineering function. Local conditions and the distance the material is to be transported must be weighed on the basis of economics. This is a thoroughly integrated decision having a strong bearing on the overall cost of the project. We believe this function should remain with the U.S. Army Corps of Engineers as it has historically. . . . We respectfully point out that [additional restrictive legislation in the dredge spoil disposal area] would inhibit the orderly development of a national port system which handled 559 million tons of foreign trade in 1970 [and] will be expected to handle the potentially vast increases in trade resulting from our nation's new trade policies with China and with the Soviet Union.

Id. (emphasis added). The port authority Association proposed to except "dredged or fill material" from § 402 and add a new section, to be numbered 404, which maintained permitting authority for dredged or fill material under the Secretary of Army (i.e., the Corps), as it currently existed. Id.

In floor debate, Senator Ellender, Democrat from Louisiana,

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offered an amendment that essentially followed the AAPA proposal, adding a new section, 404, under which the Secretary of the Army would issue permits for the discharge of dredged materials into the navigable waters at specified disposal sites. The Secretary would evaluate impact on navigation and anchorage and, in cooperation with the EPA Administrator, would determine those sites that would not adversely affect shellfish beds, fisheries (including spawning and breeding areas) or recreation areas. See 117 Cong. Rec. 38797 (Sen. debate, 92nd Cong., Nov. 2, 1971).

In support of the amendment Sen. Ellender explained it “simply retains the authority of the Secretary of the Army to issue permits for the disposal of dredged materials[, which] is essential since the Secretary of the Army is responsible for maintaining and improving the navigable waters of the United States.” Id. (emphasis added). Ellender described a deficiency of the current bill: “that it treats dredged materials the same as industrial waste” and other refuse. Id. In contrast, Sen. Ellender argued, “The disposal of dredged material does not involve the introduction of new pollutants; it merely moves the material from one location to another.”

Despite Sen. Ellender’s assurances, many other legislators had concerns about the polluting effects of dredged spoil. While (continued...
dredged spoil disposal, Ellender argued, "90 percent of the ports and harbors of the United States" would be closed, a "catastrophic situation." \textit{Id.}

Sen. Muskie, chief sponsor of the legislation, responded that "mission-oriented agencies whose mission is something other than concern for the environment simply do not adequately protect environmental values. That is not their mission." \textit{Id.} He urged dredged spoil not be differentiated from other pollutants. A substitute amendment agreeable to both factions was proposed, which kept dredged spoil under § 402(m) with all other pollutants subject to EPA approval, but also required dredged spoil disposal areas in navigable water to be certified by the Secretary of the Army as the only reasonable alternative and by the EPA Administrator not to recognize the economic arguments for open water disposal of dredged spoil, the Conference Committee reported:

\[\text{[T]he Committee expects the Administrator and the Secretary to move expeditiously to end the process of dumping dredged spoil in water - to limit to the greatest extent possible the disposal of dredged spoil in the navigable inland waters of the United States including the Great Lakes - to identify land-based sites for the disposal of dredged spoil and, where land-based disposal is not feasible, to establish diked areas for such disposal.}\]

\cite{Legt. Hist. 179}. Consequently, while dredged spoil was excepted from § 402, Congress never expected its water-based disposal to continue under the CWA.
adversely affect municipal water supplies, shellfish beds, wildlife, fisheries or recreation areas.

Throughout these discussions, only dredged spoil was discussed or considered as a potential exception from the general treatment to be accorded pollutants under § 402.9

When the Conference Committee met to reconcile the House and Senate versions of the FWPCA bills, a major difference between the bills related to “the issue of dredging.” 1 Legt. Hist. 179. Like the AAPA proposal and the Ellender amendment, but unlike the final Senate version, the House bill kept regulatory authority for dredged material disposal with the Secretary of the Army under the existing dredge and fill permit program. The Conference Committee adopted the House version. As the Committee reported:

The Conferees were uniquely aware of the process by which the dredge and fill permits are presently handled and did not wish to create a burdensome bureaucracy in light of the fact that a system to issue permits already existed. At the same time, the Committee did not believe there could be any justification for permitting the Secretary of the Army to make determination as to the environmental implications of either the site to be selected or the specific spoil to be disposed of in a site. Thus, the Conferees agreed the Administrator of the [EPA] should have the veto over the selection of the site for dredged spoil disposal and over any specific spoil to be disposed of in any selected site.

9 “Dredged spoil” means “material that is excavated or dredged from waters of the United States.” 40 C.F.R. § 232.2. No one argues mountaintop removal overburden is dredged spoil.
Id. (emphasis added). The Conference agreement became 33 U.S.C. § 1344(a)-(d).

Throughout Congressional consideration, dredged spoil was the single pollutant of concern. Section 404 was enacted to allow harbor dredging and dredged spoil disposal to continue expeditiously under the then-existing dredge and fill permit program administered by the Corps. Examination of that permit program, adopted by Congress as CWA § 404, shows fill permits were never issued nor authorized for waste disposal.

2. Dredge and Fill Permits

The Corps' dredge and fill permit program to which the Congressional Conference Committee deferred in 1972 was found at 33 C.F.R. §§ 209.120 (1972), entitled "Permits for work in navigable waters." 10 Statutory authority for those 1972 dredge and fill permits was provided under Section 10 of the Rivers and Harbors Act of 1899 (RHA), 33 U.S.C. § 403. See id. Section 10 concerns "Obstruction of navigable waters generally; wharves; piers, etc.; excavations and filling in." 11 Section 10 does not control waste

10Regulations related to the permit program also were codified in the two subsections immediately following: § 209.125 Dams and dikes across waterways and § 209.130 Piers, dredging, etc. in waterways.

11RHA § 10 remains in effect and reads now, as it did in 1899 and 1972:

(continued...)
or refuse disposal, permits for which were required and issued under a separate section of the RHA, Section 13, commonly known as the "Refuse Act." 33 U.S.C. § 407 (discussed below).

The Corps' 1972 dredge and fill permit regulations covered all excavation and construction in navigable waters. For example, the location and plans of dams and dikes across navigable waters must be approved. Id. at § 209.120(b)(1)(a). In addition, "Plans for wharves, piers, dolphins, booms, weirs, breakwaters, bulkheads, jetties, or other structures, and excavation or fill in navigable waters must be recommended by the Chief of Engineers and approved

11 (...continued)
The creation of any obstruction not affirmatively authorized by Congress, to the navigable capacity of any of the waters of the United States is prohibited; and it shall not be lawful to build or commence the building of any wharf, pier, dolphin, boom, weir, breakwater, bulkhead, jetty, or other structures in any port, roadstead, haven, harbor, canal, navigable river, or other water of the United States, outside established harbor lines, or where no harbor lines have been established, except on plans recommended by the Chief of Engineers and authorized by the Secretary of the Army; and it shall not be lawful to excavate or fill, or in any manner to alter or modify the course, location, condition, or capacity of, any port, roadstead, haven, harbor, canal, lake, harbor or refuge, or inclosure within the limits of any breakwater, or of the channel of any navigable water of the United States, unless the work has been recommended by the Chief of Engineers and authorized by the Secretary of the Army prior to beginning the same.

by the Secretary of the Army." Id. at (b)(1)(b). Throughout the dredge and fill permitting section are references to "work and construction in navigable waters," 33 C.F.R. § 209.120(f), "including such work and construction performed by the Corps of Engineers in the capacity of a construction agency for other branches and services," id., "work and structures in or over navigable waters," 33 C.F.R. § 209.120(c)(iii), "improvements of any navigable river," 33 C.F.R. § 209.120(e), and "structures and improvements," 33 C.F.R. § 209.120(d)(3) (all emphases added). These are just examples of numerous references throughout the section that support the conclusion the fill operations contemplated were for work, construction, structure building, and improvement, and never for waste disposal.

Prior to the CWA, waste disposal was overseen, also by the Corps, under the Refuse Act in a separate permit program for discharges or deposits into navigable waters, then found at § 209.131 (1972). This program, authorized by § 13 of the RHA, 33 U.S.C. § 407, provided for permits for discharge or deposit of "refuse matter of any kind or description whatever other than that flowing from streets and sewers and passing therefrom in a liquid state into any navigable water of the United States[.]" 33 C.F.R.

The Refuse Act permit program for disposal of waste, refuse, and pollutants was explicitly replaced by § 402 NPDES permits. No Refuse Act permits were to issue after enactment of the CWA amendments on October 18, 1972. See 33 U.S.C. § 1342(a)(5). Instead, EPA-administered NPDES permits were deemed to be permits issued under the Refuse Act. Id. at (a)(4). Refuse Act permit applications pending when the CWA became law were converted into NPDES permit applications. Id. at (a)(5).

To recapitulate, prior to 1972 the Refuse Act, § 13 of the RHA, governed waste disposal in navigable waters, while other non-waste-related activities involving excavation and construction in navigable waters were controlled by § 10 of the RHA. Section 10 authorized the dredge and fill permit program. The CWA perpetuated that longstanding distinction: Section 402, which replaced the

12Although dealing with refuse disposal, § 13, like the other sections of the RHA, was enacted for the purpose of protecting navigation and anchorage by keeping navigable waterways free of obstructions, and not as a general pollution control statute. See Guthrie v. Alabama By-Products Co., 328 F. Supp. 1140, 1145-47 (N.D. Ala. 1971)(providing extensive legislative history of the RHA); see also United States v. Republic Steel Corp., 362 U.S. 482 (1960)(holding industrial discharges reduced river channel depth and created an obstruction within the meaning of § 13 of the RHA); but cf., United States v. Standard Oil Co., 384 U.S. 224 (1996)(extending § 13 violations to commercially valuable gasoline accidentally discharged into navigable river).
Refuse Act permit program, regulated waste disposal. Section 404 maintained the Corps' dredge and fill permit program for excavation and construction. While Congress recognized dredged spoil was a form of waste and a pollutant, for reasons of economics and administrative efficiency its disposal was excepted from § 402 and continued to be regulated by RHA § 10 dredge and fill permits, for which § 404 was created. With the exception of dredged spoil disposal, dredge and fill activities permitted under § 404 involved maintenance, construction, work, and structures, not disposal of pollutants or waste.

3. 1977 CWA Amendments

The remainder of the current § 404 permit program became law by amendment in 1977 during the only major Congressional revisit of the CWA. Nothing added or discussed regarding the 1977 amendments altered the understanding that § 404 fill material and fill discharge activities do not include waste disposal. See 1977 U.S. Code Cong. & Admin. News. 4326-488. Instead the amendments clarified that § 404 fills were permitted for useful purposes: activities having the "purpose" of bringing an area of the

13One purpose of the 1977 amendments was "to ease unnecessary regulation and redtape" by adding general permits and exempting certain activities not involving point source discharges, id. at 4400; see also 33 U.S.C. §§ 1334(e), (f). State-administered permit programs were also created. Id. § 1344(g)-(j).
Navigable waters into a "use." 33 U.S.C. § 1334(f).

Legislators sought to except from § 404 regulation what the Senate Report called "gray area" types of activities about which there had been confusion whether permits were required. S. Rep. 95-370, U.S. Code Cong. Admin. News 1977 4401. A section was added to gather those § 404 exceptions, which include, for example, "normal farming, silviculture, and ranching," maintenance of "existing structures such as dikes, dams, and levees," and "temporary roads for moving mining equipment." 33 U.S.C. § 1344(f)(1)(A), (B), & (D).

To distinguish exempt ("gray areas") from non-exempt § 404 activities, Congress added 33 U.S.C. 1344(f)(2):

Any discharge of dredged or fill material into the navigable waters incidental to any activity having as its purpose bringing an area of the navigable waters into a use to which it was not previously subject, where the flow or circulation of navigable waters may be impaired or the reach of such waters be reduced, shall be required to have a permit under this section.

33 U.S.C. § 1344(f)(2). According to Congress, the definitive characteristic of dredge and fill discharges requiring § 404 permits is that they have a purpose for which the discharge is undertaken, to use the land created. Consonant with the long history of the § 404 permit program, discharge "purpose" is tied to a "use" to which the area will be put. The purpose is not to get
rid of waste and dispose of pollutants. Section 404 permits authorize discharge of fill material incident to some use of the filled area.

Congress clarified in 1977 that the permitted uses for § 404 fill are useful and constructive: for the purpose of bringing an area into a use. Waste disposal, of course, is undertaken to dispose of waste, not to build useful land. Under the statute, section 404 Clean Water Act permits are not available for fill discharges for the sole purpose of waste disposal.

4. Longstanding Regulatory Interpretations

Agencies' regulations reflect an agency's own longstanding interpretation, which should be accorded "particular deference." North Haven Bd. of Ed. v. Bell, 456 U.S. 512, 522 n.12 (1982). Where agencies' interpretations are consistent with Congress's express intent, they are entitled to "substantial deference." Thomas Jefferson Univ. v. Shalala, 512 U.S. 504, 512 (1994).

a. Corps' regulations

The Corps' regulations governing the dredge and fill program, found at 33 C.F.R. Pt. 323, accord precisely with the statutory, regulatory and legislative history recounted above. The Corps' definition of fill material was offered as a final rule in 1977. 42 Fed. Reg. 37122, 37145 (July 19, 1977); 33 C.F.R. §
Since 1977 the Corps has defined "fill material" as:

any material used for the primary purpose of replacing an aquatic area with dry land or of changing the bottom elevation of a [waterbody]. The term does not include any pollutant discharged into the water primarily to dispose of waste, as that activity is regulated under section 402 of the Clean Water Act.

Under the Corps' definition, "discharge of fill material" means:

the addition of fill material into waters of the United States. The term generally includes, without limitation, the following activities: Placement of fill that is necessary for the construction of any structure in a water of the United States; the building of any structure or impoundment requiring rock, sand, dirt, or other material for its construction; site-development fills for recreational, industrial, commercial, residential, and other uses; causeways or road fills; dams and dikes; artificial islands; property protection and/or reclamation devices such as riprap, groins, seawalls, breakwaters, and revetments; beach nourishment; levees; fill for structures such as sewage treatment facilities, intake and outfall pipes associated with power plants and subaqueous utility lines; and artificial reefs.

Exactly as designated by Congress, see 33 U.S.C. 1344(f)(2), § 404 fill is material discharged into water for construction, development, or property protection, activities defined by their ultimate use and purpose. Similarly reflecting the basic structure of the CWA permit programs, waste disposal (except dredged spoil) is regulated under § 402.
Since 1977 the Corps' definitions of "fill material" and "discharge of fill material" have correctly stated the law.

b. EPA regulations

The Corps administers the § 404 dredge and fill permit program, with environmental oversight of § 404 disposal sites from the EPA. Longstanding EPA definitions of "fill material" and "discharge," while not identical to Corps' definitions, when considered together, point to the same use and purpose requirement. The EPA defines "fill material" as "any 'pollutant' which replaces portions of the 'waters of the United States' with dry land or which changes the bottom elevation of a water body for any purpose." 40 C.F.R. § 232.2 (emphasis added).

Through this simple language, the EPA definition introduces a

14Defendants argue because EPA has ultimate administrative authority to construe the CWA and in particular § 404, EPA's definition of "fill material" governs. For the proposition of EPA authority, they rely on an Opinion of the Attorney General finding such authority to construe the jurisdictional term "navigable waters" and § 404(f) of the Act. See 43 U.S. Op. Atty. Gen 197, 1979 WL 16529 (1979). The Attorney General relied on legislative history, as discussed above, showing "hot[] debate[]" whether the Secretary of the Army should play any role in issuing permits and the ultimate resolution, in which the EPA Administrator retained substantial responsibility over administration and enforcement of § 404. See id. at 199.

Without deciding whether EPA administrative authority extends from jurisdictional issues through every aspect of regulation under § 404, the Court is willing to accept Defendants' premise arguendo. Nonetheless, any EPA definition also must accord with the CWA and Congressional intent.
crucial ambiguity. Compare the statute:

Any discharge of dredged or fill material into the navigable waters incidental to any activity having as its purpose bringing an area of the navigable waters into a use to which it was not previously subject, where the flow or circulation of navigable waters may be impaired or the reach of such waters be reduced, shall be required to have a permit under [§ 404].

33 U.S.C. § 1344(f)(2). Under the statute, filling is for a purposeful activity, to carry out some use that requires the waters be filled. Under the EPA definition, the purpose could be construed solely as that of the discharge. So, for example, under the statute, one could not discharge a pollutant for the sole purpose of waste disposal; ironically, under the EPA definition, waste disposal could be potentially permissible.

Despite this ambiguity, which the EPA definition introduces into an otherwise clear regulatory scheme, EPA’s similarly longstanding definition of “discharge of fill material” makes clear the agency never before now proposed that waste disposal would be a proper § 404 purpose for filling waters of the United States. Historically, EPA has defined “discharge of fill material” as:

the addition of fill material into waters of the United States. The term generally includes, without limitation, the following activities: Placement of fill that is necessary for the construction of any structure in a water of the United States; the building of any structure or impoundment requiring rock, sand, dirt, or other material for its construction; site-development fills for recreational, industrial, commercial, residential, and
other uses; causeways or road fills; dams and dikes; artificial islands; property protection and/or reclamation devices such as riprap, groins, seawalls, breakwaters, and revetments; beach nourishment; levees; fill for structures such as sewage treatment facilities, intake and outfall pipes associated with power plants and subaqueous utility lines; and artificial reefs.

40 C.F.R. § 232.2 (emphasis added). As the EPA has said always, until May 3, 2002, the purpose for discharging § 404 fill is the construction or development or use for which the fill is needed, not the purpose for which the material is discharged. Nowhere is waste disposal cited as a proper purpose.

Agency regulations, in place virtually since the CWA's inception, authorize § 404 permits only for fill discharges for uses and purposes served by the filled area. As the Corps' regulations have made clear, waste disposal is not permitted under § 404. These portions of the regulations remain consistent with Congressional intent. The EPA definition introduces an ambiguity present nowhere else in the statutory or regulatory scheme when it allows that fill discharges might be "for any purpose." But the EPA's longstanding specified purposes for discharge of fill material all have the primary purpose of placing the fill for some use. The filling authorized is not the incidental result of waste

15The EPA definition of "discharge of fill material" is identical to the Corps' longstanding definition of the same term.
disposal. The agencies' longstanding regulations, with the exception of EPA's potential permitting of § 404 discharges "for any purpose," are consistent with Congressional intent, and are otherwise due substantial deference, which the Court accords to them.

5. 1986 Memorandum of Agreement on Solid Waste and RCRA

The differing "fill material" definitions from EPA and the Corps earlier raised a similar question to that before the Court today. The Resource Conservation and Recovery Act Amendments of 1984 (RCRA), 42 U.S.C. §§ 6901, et seq., required steps be taken to improve the control of solid waste. Concerned whether § 402 or § 404 should regulate such discharges of solid waste materials into waters of the United States for the purpose of disposal of waste, the two agencies entered into an interim agreement, Memorandum of Agreement on Solid Waste. 51 Fed. Reg. 8871 (Mar. 14, 1986)(1986 MOA). The main focus of the arrangement was to ensure an effective enforcement program under the CWA. See 33 U.S.C. § 1319.

Under the MOA, the agencies agreed a "discharge will normally

16RCRA explicitly excepts coal mine overburden where hazardous wastes are involved. See 42 U.S.C. § 6905(c). The Secretary of the Interior has exclusive responsibility in that area under the Surface Mining Control and Reclamation Act, 30 U.S.C. § 1201 et seq. Id.

17Although characterized as "interim," the MOA has not been superseded or renounced in the decade and a half since.
be considered to meet the [Corps'] definition of 'fill material'” by consideration of the following factors:

a. The discharge has as its primary purpose or has as one principle purpose of multi-purposes to replace a portion of the waters of the United States with dry land or to raise the bottom elevation.

b. The discharge results from activities such as road construction or other activities where the material to be discharged is generally identified with construction-type activities.

c. A principal effect of the discharge is physical loss or physical modification of waters of the United States, including smothering of aquatic life or habitat.

d. The discharge is heterogeneous in nature and of the type normally associated with sanitary landfill discharges.18

1986 MOA at B.4. (The list does not indicate whether it is disjunctive or conjunctive.)

Of particular note, the first factor maintains in slightly attenuated, but not unrecognizable form, the primary purpose test. Section 404 fill material is discharged to create dry land or raise the bottom elevation. Implicit is that some useful purpose is required to justify the filling. Understandably, under the CWA, with its purpose to maintain the integrity of the nation's waters,

18By definition, a “sanitary landfill” is a facility for solid waste disposal which meets criteria published under section 6944. 42 U.S.C. § 6903(26). At a minimum, a sanitary landfill has “no reasonable probability of adverse effects on health or the environment from disposal of solid waste.” Id. at § 6944.
filling of rivers and streams cannot be undertaken simply to turn them into dry land, that is, simply to destroy them. As “fill” has been understood, at least since inception of the Corps’ dredge and fill permit program, filling to create dry land or elevate a bottom must be undertaken for some constructive or useful purpose.

To the extent the MOA supports a primary purpose test for fill material, the agreement is consonant with the statute and the legislative and regulatory history. Additionally, the effect of “physical loss or physical modification” of waters in the third factor comports with Congress’ concern that § 404 permits issue “where the flow or circulation of navigable waters may be impaired or the reach of such waters be reduced.” 33 U.S.C. § 1344(f)(2). As agency interpretation, consistent with Congressional intent, the agreement is due substantial deference.

Under the 1986 MOA, however, § 404 permits are not available for disposal of surface coal mine overburden solely for the purpose of waste disposal. Our Court of Appeals made the same observation concerning the 1986 MOA. The issue concerned EPA oversight of permits for instream treatment ponds and fills for disposal of waste associated with surface coal mining operations. West Virginia Coal Assoc. v. Reilly, 932 F.2d 964, 1991 WL 75217 (4th Cir. 1991)(unpublished decision aff’g 728 F. Supp. 1276)(S.D. W. 28
Having examined the 1986 MOA, the Circuit Court observed,

It is apparent from the MOA that the types of fills and discharges at issue in this case fall under [§ 402]. The discharge of fill material at issue here is expressly for the purpose of disposing of waste or spoil from mining operations.

Id. at *4.

When overburden is dumped into valleys and streams to get rid of it, the disposal has the effect of creating dry land, but not the purpose. Because land creation or elevation is not a principle purpose of overburden disposal in streams, such a discharge would not meet the Corps' definition of "fill material" as agreed in the MOA, nor be permittable under § 404.

Again, longstanding regulatory interpretation of both the Corps and EPA supports the conclusion that § 404 fill permits shall issue only for fills with a constructive primary purpose, not waste disposal.

6. CWA Consistency with the Surface Mining Control and Reclamation Act

Clean Water Act, the State laws enacted pursuant thereto, or other Federal laws relating to preservation of water quality." 30 U.S.C. § 1292(a)(3). Accordingly, if SMCRA regulation condoned overburden waste disposal in streams that would be inconsistent with the CWA and it would be trumped by the CWA. SMCRA, however, does not condone overburden waste disposal in streams. SMCRA is consistent with the CWA. Two central features of the SMCRA scheme support CWA protections for overburden disposal: approximate original contour (AOC) provisions and the buffer zone rule.

Under SMCRA, surface coal mine operators are required "as a minimum" to "restore the approximate original contour of the land." 30 U.S.C. § 1265(b)(3). Where the volume of overburden is large relative to the amount of coal removed, and where that volume is increased due to the "swell factor" associated with earth removal, not all the earth and rock removed during mining is needed to restore AOC. See Bragg v. Robertson, 72 F. Supp. 2d 642, 646 (S.D. W. Va. 1999), affirmed in part, vacated in part on other grounds, 248 F.3d 275 (4th Cir. 2001). The unneeded overburden or "excess
spoil" is the waste material disposed of and deposited in valley fills, ostensibly authorized by § 404 permits, and the subject of this Memorandum Opinion.

Waivers to AOC requirements are available when land will be put to "an equal or better economic or public use." 30 U.S.C. § 1265(e)(3)(A). AOC waivers may be allowed for "industrial, commercial, agricultural, residential, or public facilit[ies] (including recreational facilities)." 30 C.F.R. § 824.11. SMCRA's statutory and regulatory scheme thus assumes overburden will be returned to the mountaintop removal site recreating AOC unless a constructive primary purpose is designated for the site. Only where the site will be improved for "an equal or better economic or public use," does the statute contemplate overburden or excess spoil placement elsewhere.

This Court previously noted the consonance between these SMCRA presumptions and provisions of the CWA as regulated by the Corps since 1977. Bragg, 72 F. Supp.2d at 656. Section 404 fill material, under the Corps' longstanding definition, is placed for a constructive "primary purpose." 33 C.F.R. § 232.2(e). "Discharge of fill material" includes numerous approved uses

19(...continued)
SMCRA, AOC, the state and federal buffer zone rules, or their interrelations with the CWA.

31
including "site-development fills for recreational, industrial, commercial, residential, and other uses." 33 C.F.R. § 323.2(f).

In SMCRA, when Congress dealt specifically with surface coal mining overburden, it reinforced its plan that fills were appropriate where, and only where, they were justified by some constructive end use and purpose served by the fill itself. Otherwise, such overburden is just waste, to be returned to the mine site to recreate the AOC of the landscape mined. SMCRA contains no provision authorizing disposal of overburden waste in streams, a conclusion further supported by the buffer zone rule.

In 1977 the Office of Surface Mining (OSM) promulgated the so-called "buffer zone rule," which provides:

No land within 100 feet of a perennial stream or an intermittent stream\(^{20}\) shall be disturbed by surface mining activities, unless the regulatory authority specifically authorizes surface mining activities closer to, or through such a stream. The regulatory authority may authorize such activities only upon finding that –

1. Surface mining activities will not cause or contribute to the violation of applicable State or Federal water quality standards, and will not adversely affect the water quantity and quality or other

\(^{20}\)"Intermittent stream" means "(a) a stream or reach of a stream that drains a watershed of at least one square mile, or (b) a stream or reach of a stream that is below the local water table for at least some part of the year, and obtains its flow from both surface runoff and ground water discharge."

"Perennial stream" means "a stream or part of a stream that flows continuously during all of the calendar year as a result of ground-water discharge or surface runoff." 30 C.F.R. § 701.5.
environmental resources of the stream.

30 C.F.R. § 816.57 (emphasis added). Under SMCRA, the buffer zone rule protects perennial and intermittent streams and their parts and reaches from surface mining incursions that affect their water quality and quantity or other environmental resources, consonant with the Clean Water Act. See Bragg, 72 F. Supp. 2d at 649-52. For fill placement, these values are supposed to be protected by § 404 permits, which may not authorize destruction of perennial or intermittent streams solely for waste disposal. 21 SMCRA further supports this plan by requiring overburden waste to be returned to the mine site unless a higher and better constructive purpose is served by the fill.

Having considered the legislative history and statutory scheme of the CWA, its longstanding regulatory and administrative interpretation and its consistency with RCRA and SMCRA, the Court is led inexorably to the conclusion § 404 of the CWA authorizes permits for fill material only for a constructive primary purpose,

21Ephemeral streams, not protected by the buffer zone rule, flow “only in direct response to precipitation in the immediate watershed or in response to the melting of a cover of snow and ice, and which has a channel bottom that is always above the local water table.” 30 C.F.R. § 701.5. Because the buffer zone rule does not extend to these drainways above intermittent and perennial streams, it suggests the regulatory scheme was intended specifically to protect waterways without absolutely forbidding overburden disposal on land, even though water might at times run over it.
not solely for waste disposal. Authorization of § 404 permits for waste disposal generally, and specifically for coal mining overburden at mountaintop removal mines, is *ultra vires*, exceeding the statutorily granted authority of EPA or the Corps. Only Congress can rewrite the Clean Water Act to allow otherwise.

**D. Defendants' Arguments in Support of § 404 Permits for Valley Fill Waste Disposal**

Defendants counter that EPA's longstanding definition allows § 404 permits "for any purpose," and so authorizes coal overburden waste disposal practices. Using the EPA definition, the Corps has approved valley fills for overburden disposal for years. The Court should defer to the agency's longstanding regulatory practice.

Further, if the current EPA definition is not clear enough, rulemaking will shortly eliminate any potential confusion by replacing the Corps' primary purpose definition with a "final effect" version, which will expressly allow § 404 permitting of mountaintop removal waste disposal in valley fills constructed solely to dispose of waste. Defendants argue the new rule moots any objections.  

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22 Defendants also assert the Court upheld their version of § 404 when it approved a Settlement Agreement between the Corps and West Virginia citizens in Bragg, the jurisdiction of which was upheld on appeal. See *Bragg v. Robertson*, 54 F. Supp. 2d 653 (S.D. W. Va. 1999). According to Defendants, the Settlement Agreement (continued...)

34
1. Longstanding Regulatory Practice

The Corps and Intervenors argue § 404 permits have been issued for valley fills designed for waste disposal for decades under the EPA definition of fill. The same rationale is offered in the proposals for a final rule, where the agencies lean heavily on past practice. One benefit of the rule change, according to the agencies, is the final rule “is generally consistent with current agency practice.” (Corps Status Report (May 6, 2002), Ex. 1, 19 (Final Rule).)

Until May 3, 2002 the Corps' definition, in complete accord with the CWA, explicitly excluded waste disposal as a purpose for § 404 fills. All § 404 fills approved by the Corps solely for waste disposal were illegal.\footnote{How the Corps came to issue § 404 permits for mountaintop removal waste disposal in flagrant disregard of the statute and its}

\footnote{22(. . .continued) presumed coal mining overburden would continue to be permitted under § 404, and this determination by the Court has precedential effect. Under the Settlement Agreement, which the Court reviewed and found to be fair and reasonable, Plaintiff reserved the “right to challenge under the APA any future Corps’ CWA section 404 authorization for any valley fill in waters of the United States that may be authorized by the Corps” after the Settlement. (Pl.’s Mot. for Prelim. Inj., Ex. 19 ¶ 16.) The Settlement Agreement left the issue of the agencies’ authority to issue § 404 permits for valley fills open and undetermined. Under any legal analysis of the Settlement Agreement’s preclusive effects, therefore, this issue was explicitly left undecided and its merits undetermined.

23}
Until May 3, 2002 EPA defined "fill material" as "any 'pollutant' which replaces portions of the 'waters of the United States' with dry land or which changes the bottom elevation of a water body for any purpose." 40 C.F.R. § 232.2 (emphasis added). As discussed above, this definition introduced a potential ambiguity into the statutory and regulatory scheme. Under the statute, § 404 permits are required where the fill has the purpose of bringing an area into a new use. See 33 U.S.C. § 1344(f)(2). The EPA definition, however, might be understood to apply to the use or purpose, not of the fill, but of the discharge. Under that reading, however, the regulation would be inconsistent with the statute. It would also conflict with the EPA's own definition of "discharge of fill material," which involved constructive, purposeful and useful fills, not fills constructed solely for waste disposal. Accordingly, the reading of the ambiguous EPA definition of fill material that would allow discharges "for any purpose" is necessarily incorrect. Section 404 fills permitted solely for

23(...continued)

own regulations is a historical question that the Court does not have information or expertise to determine. Knowing that mountaintop removal mines have expanded exponentially over the past two decades, one might speculate, as the Corps' Rodney Wood testified, the Corps didn't necessarily intend to regulate valley fills, but "they just sort of oozed into that." (Pl.'s Mot. for Prelim. Inj., Ex. 17, p. 23.)
waste disposal were not legal then and are not now.

An illegal agency practice has no precedential value and is due no deference. The fact the Corps approved § 404 permits solely for massive waste disposal in the past two decades, with EPA's approval, is an admission against interest, not a mitigating factor, much less an argument the Court should approve the practice. Tacitly recognizing the futility of this argument, the agencies attempted to fix the problem by changing the law, without benefit of Congressional amendment.

2. Rulemaking: The "Final Effect"

On April 20, 2000 the Corp and EPA jointly proposed to revise their definitions of "fill material." See 65 Fed. Reg. 21292 (Apr. 20, 2000). According to news reports, more than 17,000 comments, most of them negative, delayed the rule's adoption. On May 3rd, 2002 while the Court was considering these matters, the agencies signed for publication the final version of their rule.

Both agencies' proposed final rule defines "fill material" as "material placed in waters of the United States where the material has the effect of" either "replacing any portion of a water of the

24Summarizing the comments, the agencies acknowledge, "We received over 17,200 comments on the proposed rule[.]. Most of the comments were form letters which opposed the rule." Final Rule at 11 (emphasis added).
United States with dry land or changing the bottom elevation of any portion of a water." Final Rule at 59 (emphasis added). Consequently, the narrow use and purpose exception authorizing fill activities under Corps' dredge and fill permits is eliminated by administrative fiat with the stroke of a pen. Without the necessity of legislation, and by design, surface coal interests are assured:

With regard to proposed discharges of coal mining overburden, we believe that the placement of such material into waters of the U.S. has the effect of fill and therefore, should be regulated under CWA section 404. 65 Fed. Reg. at 21295 (emphasis added).

The new rule now incorporates expansive examples:

Examples of such fill material include, but are not limited to: rock, sand, soil, clay, plastics, construction debris, wood chips, overburden from mining or other excavation activities, and materials used to create any structure or infrastructure in the waters of the United States.

Final Rule at 59. The rule also excludes certain other materials:

"The term fill does not include trash or garbage." Id.

The agencies' new definitions of "discharge of fill material" continue to consist of their lists of constructive uses and purposes. Sensibly, "infrastructure" will be added wherever "structure" appears. Almost at the end of the definition, after "utility lines," the agencies will add this language:
placement of fill material for construction or maintenance of any liner, berm or other infrastructure associated with solid waste landfills;\textsuperscript{[25]} placement of overburden, slurry, or tailings or similar mining-related materials[.]

Final Rule at 58-9 (emphasis added). Interestingly, the only exception to the long list of uses and purposes for fill discharges is the new addition of mining-related waste disposal.

These new agency definitions set forth in the final rule are fundamentally inconsistent with the CWA, its history, predecessor statutes, longstanding regulations, and companion statutes. Under the guise of regulatory harmony and consistency, the agencies have taken an ambiguous interpretation, that of the EPA, seized the unsupportable horn of the ambiguity, and now propose to make their original error and administrative practice the law. Section 404 fill permits have always been allowed for beneficial uses and purposes of the fill. It is the constructive use and purpose that justify filling the waters of the United States.

The agencies now, however, propose in their final rule to ignore fill use and purpose entirely. Only "fill effect" will be considered. As a child could explain, the effect of filling things

\textsuperscript{[25]}This language addresses another litigation-related § 404 problem involving the definition of fill material. See Resource Investments Inc. v. United States Army Corps of Engineers, 151 F.3d 1162 (9\textsuperscript{th} Cir. 1998).
is that they get full. By expunging the use and purpose doctrine for fills and replacing it with an effect test, the agencies expand the Corps' CWA authority. The definition is a tautology; all fills have the effect of filling. Through this empty definition, the agencies allow the waters of the United States to be filled, polluted, and unavoidably destroyed, for any purpose, including waste disposal. Pointedly, the rule is intended to and does allow the massive filling of Appalachian streams with mine waste under auspices of the CWA. The justification under the new definition is no longer to foster a beneficial use and purpose. A fill is now justified merely because it has the effect of creating a convenient repository of waste.

The agencies' explanations that regulatory harmony and consistency will result and regulatory practice be maintained are disingenuous and incomplete. The Court does not rule in a vacuum. It is aware of the immense political and economic pressures on the agencies to continue to approve mountaintop removal coal mining valley fills for waste disposal, and to give assurances that future legal challenges to the practice will fail. Some may believe that reasonably priced energy from coal requires cheap disposal of the vast amounts of waste material created when mountaintops are removed to get at the natural resource. For them, valley fill
disposal is the most efficient and economical solution.

Congress did not, however, authorize cheap waste disposal when it passed the Clean Water Act. The purpose of the Act was, and is, to "restore and maintain the chemical, physical, and biological integrity of the Nation's waters." 33 U.S.C. § 1251(a). The statutory scheme is already consistent and harmonized. The agencies' new final rules are inconsistent with the statutory scheme. Thus, the purported rulemaking is ultra vires: it exceeds the agencies' statutory authority granted by the CWA. Only Congress can rewrite the CWA to allow the fundamental changes proposed by the agencies to the § 404 dredge and fill permit program.

III. CONCLUSION

When the Clean Water Act was passed in 1972 and amended in 1977, the Army Corps' dredge and fill permit program was maintained for political and economic reasons relating largely to port maintenance. The program became § 404. Generally, permits for pollutant discharge issued under § 402, the National Pollutant Discharge and Elimination System (NPDES). After heated debate, Congress excepted dredged spoil and allowed the dredge and fill permit program, begun under § 10 of the Rivers and Harbor Act, to continue under Corps' supervision, with environmental oversight
from EPA. Under the § 10 program, as grandfathered in, fills were allowable to underpin structures, support roads, protect and improve development, that is, for purposes or uses for which the fill was needed. Congress never intended § 10 fills, nor § 404 fills, to be permitted solely to dispose of waste.

To read the Act otherwise presumes Congress intended the Clean Water Act to protect the nation's waterways and the integrity of its waters with one major exception: the Army Corps was to be given authority to allow the waters of the United States to be filled with pollutants and thus destroyed, even if the sole purpose were disposal of waste. This obviously absurd exception would turn the "Clean Water" Act on its head and use it to authorize polluting and destroying the nation's waters for no reason but cheap waste disposal.

Nevertheless, for the past twenty years, particularly in the Huntington Corps District, § 404 permits have been issued for mountaintop removal overburden disposal in valley fills that have obliterated and destroyed almost a thousand miles of streams, by the Corps' own account. The valley fills are used solely to dispose of the waste rock and dirt that overlies the coal. Past § 404 permit approvals were issued in express disregard of the Corps' own regulations and the CWA. As such, they were illegal.
When the illegitimate practices were revealed by court decisions in this district, the agencies undertook to change not their behavior, but the rules that did not support their permit process.

The agencies' final rules attempt to legalize filling the waters of the United States under the CWA solely for waste disposal. The obvious perversity of this proposal forced the agencies to suggest baseless distinctions among wastes: "trash" and "garbage" are out; plastic, construction debris and wood chips are in. The final rule for "discharge of fill material" highlights that the rule change was designed simply for the benefit of the mining industry and its employees. Only one type of waste is added to the otherwise constructive list: "overburden, slurry, or tailings or similar mining-related" waste are now permissible fill in the nation's waters.

The agencies' attempt to legalize their longstanding illegal regulatory practice must fail. The practice is contrary to law, not because the agencies said so, although their longstanding regulations correctly forbade it. The regulators' practice is illegal because it is contrary to the spirit and the letter of the Clean Water Act.

Accordingly, the Court FINDS and CONCLUDES § 404 fills may not be permitted solely to dispose of waste. Plaintiff's motion is
GRANTED. The motions of the Corps Defendants and Defendant-Intervenors are DENIED. The Corps Defendants are ENJOINED from issuing any further § 404 permits that have no primary purpose or use but the disposal of waste. In particular, issuance of mountaintop removal overburden valley fill permits solely for waste disposal under § 404 is ENJOINED.

The agencies' new final rules address political, economic and environmental concerns to effect fundamental changes in the Clean Water Act for the benefit of one industry. However important to the energy requirements of the economy and to employment in the region, amendments to the Act should be considered and accomplished in the sunlight of open Congressional debate and resolution, not within the murk of administrative after-the-fact ratification of questionable regulatory practices.

The Clerk is directed to send a copy of this Order to counsel of record and publish it on the Court's website at http://www.wvsd.uscourts.gov.

ENTER: May 8, 2002

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NATIONAL ENVIRONMENTAL POLICY ACT (NEPA) UPDATE

NEPA Compliance in Corps of Engineers Permitting:
"Scope of Analysis" and Other Issues

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SECTION I
National Environmental Policy Act (NEPA) Update

NEPA Compliance in Corps of Engineers Permitting: “Scope of Analysis” and Other Issues

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I. NEPA Basics

A. The Statute: The National Environmental Policy Act, 42 U.S.C. § 4321 et seq. (“NEPA”), was enacted to create a framework within the Federal government for including environmental considerations among factors ordinarily examined in the decision-making process. The heart of NEPA is the environmental impact statement (“EIS”), which must be prepared for all major federal actions significantly affecting the quality of the human environment. The EIS requirement must be satisfied by the federal agency responsible for the proposed action. An EIS must include a detailed statement of:

1. the environmental impact of the proposed action;
2. any adverse environmental effects which cannot be avoided should the proposal be implemented;
3. alternatives to the proposed action;
4. the relationship between local short-term uses of the human environment and the maintenance and enhancement of long-term productivity; and
5. any irreversible and irretirvable commitments of resources which would be involved in the proposed action should it be implemented.


An EIS has two primary purposes: to ensure that the federal agency makes a fully informed decision in light of the potential environmental consequences of its actions, and to keep the public informed about those consequences and allow them an opportunity to comment on the proposed action. However, NEPA does not mandate any particular outcome. It is a procedural statute that specifies particular procedures that must be followed and information that must be presented before a federal agency may make a project decision. NEPA does not require the agency to select the environmentally preferable alternative.
The CEQ NEPA Regulations: The Council on Environmental Quality ("CEQ") adopted regulations to implement the requirements of NEPA in 1978. Those regulations, which apply to all federal agencies, have been codified at 40 C.F.R. parts 1500-1508. Individual federal agencies also are encouraged to develop their own NEPA implementing regulations, and many agencies have developed either such regulations or guidance documents to better integrate the NEPA process into the agency's specific mission.

1. **Categorical Exclusions:** The CEQ regulations provide for certain "categorical exclusions," which are categories of actions which do not individually or cumulatively have a significant effect on the human environment, and therefore do not require either an environmental assessment or an environmental impact statement. 40 C.F.R. § 1508.4. Individual federal agencies are empowered to identify such categorical exclusions in their specific NEPA implementing regulations.

2. **Environmental Assessment:** If a proposed action does not fit within a categorical exclusion, some NEPA documentation is required. In that case, an environmental assessment ("EA") may be prepared. An EA is a concise document that serves to provide sufficient information to determine whether the project will have "significant" effects on the environment and thus requires an EIS. (Alternately, if an EIS is clearly required, an EA need not be prepared, and the agency may proceed directly to preparation of the EIS.) The EA must describe briefly the need for and alternatives to the proposal, the environmental impacts of the proposed action and alternatives, and a listing of agencies and persons consulted. 40 C.F.R. § 1508.9.

If the EA demonstrates that the agency’s proposed action will not have a significant impact on the human environment, the agency will prepare a Finding of No Significant Impact, or "FONSI." This document presents the reasons why the action will not have a significant impact on the environment. The agency may proceed with the proposed action based on the FONSI, after sufficient notice to the public. See 1501.4(e).

NB: The determination of whether an agency’s proposed action will have a significant impact on the human environment is often one of the most contentious issues in a NEPA review. It determines whether a simple EA will suffice, or a much more complex, costly, and time-consuming EIS must be prepared. This issue arises frequently in the CWA Section 404 permitting context.

3. **Environmental Impact Statement:** An EIS must be prepared if the proposed action will have significant impacts on the human environment.
a. Contents: Major elements of an EIS include: a Statement of Purpose and Need (the underlying purpose and need to which the agency is responding); an Alternatives Analysis (presenting the proposed action and a "reasonable range" of alternatives, and comparing their environmental impacts); the Affected Environment (i.e., the area and resources to be affected); and the Environmental Consequences of the proposed action and alternatives (including direct, indirect and cumulative effects on the environment). An EIS also will include a summary, a list of preparers, and various appendices with material related to the EIS and its analyses. See 40 C.F.R. § 1502.10-1502.19.

b. Process: An EIS is prepared in two stages. A Draft Environmental Impact Statement ("DEIS") must be prepared first, and then published in order to obtain comments from the public and from governmental agencies. Following a public comment period, a Final Environmental Impact Statement ("FEIS") is prepared. The FEIS must respond to all comments received on the DEIS. In response to comments received and in preparing the FEIS, the agency may modify the alternatives, information, or analyses contained in the DEIS. See 40 C.F.R. part 1503.

c. Record of Decision: The EIS process is completed by the agency’s publication of a Record of Decision, or "ROD." This concise statement of the agency’s decision should identify all alternatives considered and specify the alternative(s) deemed to be environmentally preferable. The agency should explain the rationale for its decision concerning which alternative to implement. The agency also must state whether all practicable means to avoid or minimize environmental harm have been adopted in the decision, and if not, why they were not. 40 C.F.R. § 1505.2.

4. Agency Cooperation: If more than one agency is involved in the proposed action, a "lead agency" shall supervise the preparation of the EIS. Other federal agencies with jurisdiction by law over all or a portion of the project or its impacts will be "cooperating agencies." Agencies with special expertise also may be cooperating agencies, upon the request of the lead agency. Cooperating agencies participate in the NEPA process from the outset, including scoping, preparing the environmental documentation, and commenting on the EIS. See 40 C.F.R. §§ 1501.5-1501.6.

EISs also should, to the extent possible, be prepared concurrently and in integration with environmental analyses and studies under the Fish and Wildlife Coordination Act (16 U.S.C. § 661 et seq.), the National Historic Preservation Act (16 U.S.C. § 470 et seq.), the Endangered Species Act
(16 U.S.C. § 1531 et seq.), and other environmental review laws and executive orders. 40 C.F.R. § 1502.25. EISs should include a discussion of Environmental Justice issues, pursuant to Executive Order No. 12898.

II. Judicial Review Under NEPA

A. Private right of action: NEPA itself does not provide a private right of action for violations of its provisions. Absent any right of action in the statute, the courts have found that agency actions are reviewable under the judicial review provision of the Administrative Procedure Act, 5 U.S.C. § 701 et seq. ("APA"). Under that provision, an agency decision may be set aside only if it is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law," or was undertaken "without observance of procedures required by law." Id. § 706(2)(A), (D). This review standard is narrow, and the reviewing court may not substitute its judgment for that of the agency. Marsh v. Oregon Natural Resources Council, 109 S. Ct. 1851, 1861-62 (1989). The reviewing court must determine whether the decision was based on a consideration of the relevant factors and whether there has been a clear error of judgment.

B. Constitutional and statutory standing: In order to bring a NEPA challenge under the APA, prospective plaintiffs first must satisfy Constitutional and statutory standing requirements. Because Article III of the U.S. Constitution limits the role of the federal judiciary to resolving cases and controversies, plaintiff standing is a necessary predicate to federal court jurisdiction. Thus, any potential NEPA plaintiff must satisfy the following Constitutional standing requirements:

1. Injury-in-fact. The injury must be concrete and particularized, rather than conjectural or hypothetical.

2. Causation. It must be substantially probable that the challenged acts of the defendants will cause the particularized injury of the plaintiff.

3. Redressability. The relief sought must be shown to be likely to alleviate the particularized injury alleged by the plaintiff.

C. Final agency action and zone of interest: In addition, to bring an action under the APA, a prospective plaintiff also must identify some "final agency action" (e.g., issuance of a ROD) and must demonstrate that its claims fall within the "zone of interests" protected by the statute forming the basis of its claims (e.g., NEPA). The courts generally have found that economic injuries are not within the zone of interests protected by NEPA. It is clear, on the other hand, that injuries to a part of the environment that the plaintiff enjoys on a regular basis would satisfy the zone of interests test and establish plaintiff's standing.

III. NEPA and the Army Corps of Engineers: Scope of Analysis and Other Issues

The issuance of a permit under Section 404 of the Clean Water Act ("CWA"), 33 U.S.C. § 1344, or Section 10 of the Rivers and Harbors Act ("RHA"), 33 U.S.C. § 403,
constitutes a federal action subject to the requirements of NEPA, including the preparation of an EIS if the environmental effects of the permit issuance are deemed to be significant. The application of NEPA to the Corps’ permitting program has been the source of considerable controversy and continues to raise important issues.

A. The Corps’ Regulations and the “Scope of Analysis”: The Army Corps of Engineers (the “Corps”) has adopted its own NEPA implementing regulations, which are codified at 33 C.F.R. part 325, Appendix B (hereinafter “Appendix B”). The current Appendix B regulations were proposed by the Corps in 1984, and went into effect in 1988. The most controversial aspect of the Appendix B regulations is the “scope of analysis,” which seeks to establish the scope of the action subject to NEPA analysis, and thus the scope of the NEPA document, in instances where the application for a Corps permit covers only a part of a larger project that may have both federal and nonfederal elements. The scope of analysis will determine “what portion of the total project will the Corps cover in its EA describing the work, the range of environmental effects of that work, alternatives to the proposed work, etc.” 53 Fed. Reg. 3120, 3121 (1988) (Corps preamble to 1988 regulations).

The debate over the Corps’ scope of analysis presents one of the most common and controversial examples of what is often called the “small federal handle” problem. The issue is at what point does federal involvement in a project proposed by a non-federal entity (private party, state or local government, etc.) “federalize” the entire action and subject it to the requirements of NEPA. In the case of Corps permitting decisions, the particular issue is whether the issuance of a Corps permit causes the non-federal portion of a project with both federal and non-federal elements to be included within the scope of the NEPA analysis—and if so, how and to what extent. This issue is not simply academic. It will determine whether the reasonable range of alternatives evaluated in the NEPA document must include alternatives to the specific elements within Corps jurisdiction, or alternatives to the overall project. It also often may mean the difference between the preparation of a relatively simple EA and the preparation of a much more costly and time-consuming EIS. For these reasons, much energy has been expended identifying the proper scope of analysis for NEPA review of Corps permitting decisions.

1. Pre-1988 Regulations: Before 1988, the Corps’ NEPA regulations provided that NEPA documentation prepared for permit actions should focus “primarily on whether or not the entire project subject to the permit requirement could have significant effects on the environment . . . . (For example, where a utility company is applying for a permit to construct an outfall pipe from a proposed power plant, the EA must assess the direct and indirect environmental effects and alternatives of the entire plant.)” 45 Fed. Reg. 56760, 56779 (Aug. 25, 1980), codified at 33 C.F.R. part 230, App. B, § 8(a) (1981).
2. **Judicial Interpretation:** Two federal appeals court decisions in 1980 addressed the “small federal handle” problem in the Corps permitting context. Those decisions indicated that the Corps could adopt a more limited scope in the NEPA review of some permitting decisions than indicated in its 1980 NEPA regulations.

   a. **Winnebago Tribe of Nebraska v. Ray,** 621 F.2d 269 (8th Cir. 1980): The Corps was asked to permit a 1.25-mile river crossing on a proposed 67-mile, nonfederal power line. The Corps’ EA focused solely on the river crossing and concluded that no significant environmental impacts could be expected. Plaintiffs challenged the Corps’ EA, arguing that, “but for” the Corps’ permit, the power line could not be built, and therefore, the Corps had sufficient control over the proposal to require an environmental analysis of the entire 67-mile power line.

   The Eighth Circuit analyzed the situation under both an “enablement” (or legal control) framework and under a factual control test. In this case, the Corps permit was not found to be “a legal condition precedent” to the entire nonfederal power line project. Likewise, the court found that the Corps lacked sufficient factual, or “veto,” control over the project. The court outlined a three-part test to determine factual control, including:

   1. the degree of discretion exercised by the agency over the federal portion of the project;
   2. whether the federal government has given any direct financial aid to the project; and
   3. whether the overall federal involvement with the project is sufficient to turn essentially private action into federal action.

   621 F.2d at 272. These factors were found lacking in this case.

   b. **Save the Bay v. U.S. Army Corps of Engineers,** 610 F.2d 322 (5th Cir. 1980): The Corps was asked to issue a permit for the construction of a 2200-foot wastewater discharge pipeline associated with a proposed massive nonfederal titanium dioxide manufacturing facility adjacent to Bay St. Louis, Louisiana. In its EA, the Corps only analyzed the effects of building the outfall pipeline, not the associated nonfederal facility. In upholding the Corps’ action, the Fifth Circuit determined that there was an insufficient nexus between the Corps and the construction of the nonfederal plant to make the agency a partner in that construction and thereby “federalize” its construction. Although it explicitly refused to adopt a “but for” test, the court nevertheless noted that
the pipeline was not necessary to operate the plant (because another method of discharge, not requiring a Corps permit, was available), and therefore, the Corps lacked factual control over the construction as well.

3. **1988 Regulations:** The Corps adopted new NEPA regulations in 1988 in response to the Winnebago and Save the Bay decisions. 53 Fed. Reg. 3120, 3121-22 (1988). However, prior to taking effect, those regulations were the subject of a significant dispute between the Corps and EPA over their adequacy in satisfying the Corps’ NEPA responsibilities.

   a. **Proposal and Adoption.** The Corps first proposed an amendment to its NEPA regulations in 1984 in response to the Fifth and Eighth Circuits' decisions. The new language proposed for Appendix B closely tracked the rationale behind those two appeals court decisions. However, the U.S. Environmental Protection Agency determined that the proposed regulations were “unsatisfactory” and referred the proposed amendments to CEQ, pursuant to Section 309 of the Clean Air Act. EPA stated that the proposed changes would adversely affect the Corps’ and EPA’s NEPA review responsibilities and their ability to prevent unacceptable adverse effects from activities permitted under Section 404. After an extensive public review and comment period, CEQ upheld the Corps’ proposed changes, with some modifications, as being “within reasonable, implementing agency discretion.” 52 Fed. Reg. 22,517, 22,518-19 (1987).

   The Ninth Circuit subsequently held that the Corps’ Appendix B regulations do not conflict with NEPA or the CEQ regulations, and should be accorded judicial deference. Sylvester v. U.S. Army Corps of Engineers, 884 F.2d 394, 399 (9th Cir. 1989). The Sylvester court found that “the Corps’ regulations fixing the scope of its NEPA analysis strike an acceptable balance between the needs of the NEPA and the Corps’ jurisdictional limitations.” Id. The court also stated that CEQ’s approval of the Corps’ regulations was meant to “provide guidance to all who may be concerned, including the courts.” Id.

   b. **The Regulations:** The Appendix B regulations state:

   In some situations, a permit applicant may propose to conduct a specific activity requiring a [Corps] permit . . . which is merely one component of a larger project . . . . The district engineer should address the scope of the NEPA document (e.g., the EA or EIS) to address the impacts of the specific activity requiring a [Corps] permit and those
portions of the entire project over which the district engineer has sufficient control and responsibility to warrant Federal review. . . . The district engineer is considered to have control and responsibility for portions of the project beyond the limits of Corps jurisdiction where the Federal involvement is sufficient to turn an essentially private action into a Federal action. These are cases where the environmental consequences of the larger project are essentially products of the Corps permit action.


4. **Judicial Interpretation:** In addressing the “small federal handle” problem, the federal courts have identified two primary ways in which nonfederal portions of a project may become federalized and therefore subject to NEPA review. These concepts, known generally as “legal control” and “factual control,” also are consistent with the factors identified in the Appendix B regulations.

a. **Legal Control:** A project may become federalized when a federal agency exercises sufficient “legal control” over the entire project. The Winnebago court referred to this as “enablement,” which occurs when “federal action is a legal condition precedent to accomplishment of an entire nonfederal project.” 621 F.2d at 272. In that case, the court held that the proposed power line had not been federalized because the Corps’ permitting authority under Section 10 extended only to the portion of the power line located in jurisdictional waters—not the construction of the entire power line.

The Appendix B regulations incorporate this concept in the discussion of the “typical factors to be considered in determining whether sufficient ‘control and responsibility’ exists.” 33 C.F.R. part 325, App. B, § 7(b)(2). Those factors include: “the extent to which the entire project will be within Corps jurisdiction,” and “the extent of cumulative Federal control and responsibility.” Id. The regulations explain:

Federal control and responsibility will include the portions of the project beyond the limits of Corps jurisdiction where the cumulative Federal involvement of the Corps and other Federal agencies is sufficient to grant legal control over such additional portions of the project. These are cases where the environmental consequences of the additional portions of the projects are essentially products of Federal financing, assistance, direction, regulation, or approval . . . .
The regulations also include several examples, one of which is remarkably similar to the facts of Winnebago. See 33 C.F.R. part 325, App. B, §7(b)(3).

See Macht v. Skinner, 916 F.2d 13 (D.C. Cir. 1990). Although a state light rail project required a Section 404 permit to cross wetlands, the Corps’ ability to prevent the proposed route was insufficient to “federalize” the project, even coupled with additional federal funding for preliminary engineering studies and state EISs. The Corps had jurisdiction over only 3.58 acres on a 22.5-mile-long project.

See also Landmark West! V. U.S. Postal Service, 840 F. Supp. 994 (S.D.N.Y. 1993), aff’d, 41 F.3d 1500 (2d Cir. 1994). Although this case did not arise within the Corps permitting context, Landmark West! provides one of the most thorough, exhaustive treatments of this issue and provides an excellent introduction to the “small federal handle” problem.

b. Factual Control: The courts also have indicated that a nonfederal project may become federalized where the federal agency has sufficient factual, or “veto,” control over the nonfederal action. Four general factors have been identified by the courts in determining whether an agency has “veto” control over a nonfederal project:

1. The degree of discretion exercised by the agency over the federal portion of the project, see, e.g., Winnebago, 621 F.2d at 272 (while Corps has broad discretion in considering environmental factors in granting permit, discretion does not extend beyond navigable waters over which Corps has jurisdiction);

2. Whether the federal government has given any direct financial aid to the nonfederal project, see, e.g., Winnebago, 621 F.2d at 273 (no federal funding involved in power line);

3. Whether the overall federal involvement with the project is sufficient to turn an essentially nonfederal action into a federal action, see, e.g., Winnebago, 621 F.2d at 273 (no federal involvement other than Section 10 permit); and

4. Whether the nonfederal project will go forward even if the federal action does not (known as the “but for” test), see, e.g., Save the Bay, 610 F.2d 322 (entire plant was not
"federalized," because alternative method of effluent discharge was available which did not require Corps permit); Sylvester v. U.S. Army Corps of Engineers, 884 F.2d 394, 400-01 (9th Cir. 1989) (Corps lacked sufficient control over nonfederal resort complex where resort could have gone forward without federal wetlands permit for golf course).

The Corps also has identified another factor in its regulations that relates to the "factual" relationship between the federal and nonfederal portions of a project, i.e., "whether there are aspects of the upland facility in the immediate vicinity of the regulated activity which affect the location and configuration of the regulated activity." 33 C.F.R. part 325, App. B, § 7(b)(2)(ii).

c. Sylvester v. U.S. Army Corps of Engineers, 884 F.2d 394, 400-01 (9th Cir. 1989): This Ninth Circuit decision is one of the most significant federal court decisions on this subject following the Corps' adoption of its 1988 NEPA regulations. Sylvester concerned the Corps' NEPA review of a proposed resort that included a golf course located on wetlands and a ski resort located on adjacent uplands. In addition to upholding the Corps' NEPA regulations as an acceptable interpretation of its NEPA obligations, the Sylvester court held that the Corps could limit its NEPA review to the construction of the golf course on the wetlands, even though the golf course was part of a larger development. 884 F.2d at 401. The court found that the golf course and the rest of the resort were not "two links of a single chain," because "each could exist without the other, although each would benefit from the other's presence." Id. Sylvester is significant because it often serves as the basis for arguing that the Corps' NEPA review should be restricted to those areas over which it has jurisdiction.

d. Wetlands Action Network v. U.S. Army Corps of Engineers, 222 F.3d 1105 (9th Cir. 2000): This is another Ninth Circuit decision that recently addressed the scope of analysis issue. The case involved a challenge to the Corps' decision to grant a permit to fill 16 acres of wetlands and to mitigate the fill by creating a 51-acre wetlands system for a large scale mixed use development. The Corps agreed to a division of the overall project into three phases for permitting purposes. The Corps also limited its analysis to the impacts resulting from the filling of the 16.1 acres of wetlands for the first phase of development.

The court first reiterated that it had upheld the Corps' NEPA regulations in Sylvester, particularly with respect to the scope of
The court also cited the federalization analysis contained in the \textit{Sylvester} decision with approval. With respect to the scope of analysis in the present action, the court stated:

The district court's determination that the project would not be able to proceed as planned without the permit and the filling of the wetlands would not occur without the project is correct. The conclusion that the district court drew from these findings [that the analysis should have included all of the upland development], however, is in error. The linkage that the district court found between the permitted activity and the specific project planned is the type of "interdependence" that is found in any situation where a developer seeks to fill a wetland as part of a large development project. If this type of connection alone were sufficient to require a finding that an entire project falls within the purview of the Corps' jurisdiction, the Corps would have jurisdiction over all such projects including those which the Corps' regulations cite as examples of situations in which the Corps would not have jurisdiction over the whole project.

222 F.3d at 1116-17. The court applied the factors identified in the Corps' NEPA regulations and concluded that the Corps' decision to limit its review to the specific activity requiring the permit was not arbitrary or capricious. \textit{Id.}, at 1117-18. (The court also found that the Corps had not improperly "segmented" NEPA analysis of the first phase of the project from the second and third phases, based on the preliminary and uncertain nature of those subsequent phases. "Neither the CEQ regulations nor our precedent support the conclusion that the Corps was required to consider the three phases together as cumulative actions." \textit{Id.} at 1119.)

e. But see \textit{Friends of the Earth v. U.S. Army Corps of Engineers}, 109 F. Supp. 2d 30 (D.D.C. 2000): Plaintiffs brought suit to challenge the Corps' determination that an EIS was not required for the permitting of three casinos on the Mississippi coast. Among the claims, the plaintiffs objected to the Corps' refusal to consider the effects of the upland portion of the casino projects. In finding for the plaintiffs, the court distinguished \textit{Winnebago} and \textit{Save the Bay}, noting that those cases involved very different situations than the casino permitting: "Here by contrast, the agency's jurisdiction encompasses the heart of the development projects—the permitting of the floating casinos themselves. All upland development results
from and is entirely conditional on the permitted activity. Because the ‘environmental consequences of the larger project’ therefore ‘are essentially products of the Corps permit action,’ 33 C.F.R. § 325 App. B § 7(b), the Court finds that the development here is akin to the shipping terminal example provided by the Corps’ own regulations for which the scope of NEPA analysis was extended to the upland development.” 109 F. Supp. 2d at 40.

f. But see Stewart v. Potts, 996 F. Supp. 668 (S.D. Tex. 1998): An applicant sought a Section 404 permit for impacts to approximately 2 acres of wetlands to construct a golf course on a 400-acre tract. The Corps limited its scope of analysis to the impacted wetlands. The District Court found that because the wetlands were scattered throughout the proposed golf course site, the filling of the wetlands and the clearing of upland forest necessary to construct the golf course were interrelated, thereby bringing the entire project within the Corps’ NEPA analysis. The court expressly distinguished the decisions in Winnebago, Save the Bay, and Sylvester. The court stated that in those cases, the activities “invoking Corps jurisdiction and NEPA, were physically, functionally, and logically separable from the activities held not subject to NEPA analysis.” 996 F. Supp. at 682. The court observed that “the two acres of wetlands that will be directly impacted are scattered throughout the 200-acre tract .... [T]he Corps’ characterization of the project as a filling of the wetlands separate and distinct from the clearing of the forest located on those wetlands is irrational.” Id. The court described the Corps’ position as “asinine on its face, and an impermissible abdication of a federal agency’s duties under NEPA.” Id. at 682-83.

5. Causation and Assessment of Effects: While the Corps’ scope of analysis inquiry is intended to identify the scope of the work, whether federal or nonfederal, over which the Corps’ assessment of effects will occur, the considerations of “legal” and “factual” control discussed above often recur in determining the extent of the effects that must be disclosed in the NEPA document once the scope of analysis has been identified. Thus, even where the scope of analysis inquiry may have demonstrated that the Corps lacks sufficient control and responsibility to federalize the nonfederal portion of a project, the extent of the Corps’ legal or factual control over the nonfederal portions of the project may become an issue again in trying to determine whether those nonfederal portions of the project should be considered the effects (whether direct, indirect, or cumulative) of the portion of the project included within the scope of analysis. This analysis often will turn on notions of causation, i.e., whether the Corps’ action (issuing a permit) is a legal or factual “cause” of the nonfederal portions of the project. This often presents a difficult
and confusing sense of “déjà vu,” as issues addressed in defining the scope of analysis (i.e., the extent of the action or work subject to NEPA review) are revisited in determining the scope of effects that must be identified.

See Colorado River Indian Tribes v. Marsh, 605 F. Supp. 1425 (C.D. Cal. 1985); Sierra Club v. Marsh, 769 F.2d 868 (1st Cir. 1985). These cases were cited by the EPA as support for its objections to the Corps’ proposed scope of analysis regulations in 1984. In the former case, a developer planning a 156-acre residential and commercial development applied for a Corps permit to stabilize an adjacent river bank, which was necessary for the development to proceed. The court there required the private development to be evaluated in the NEPA document as a likely occurrence resulting from the issuance of a permit. See generally, 605 F. Supp. at 1428-1434. The latter involved the proposed construction of a causeway from the mainland to an island, and required the NEPA analysis to include among the effects of permit issuance the industrial development on the island that would be stimulated by construction of the causeway. 769 F.2d at 877-78. As noted by the Corps in its response to EPA’s objections:

These cases did not hold the Corps permits “federalized” the unregulated private development so as to render the private action Federal actions for NEPA purposes. Rather, among the numerous legal problems found by each court, the cases required the Corps to consider the private development likely to occur as a result of the issuance of the Corps permit. Such analysis is part of an accepted NEPA requirement to consider the environmental effects of Federal action . . . .

See also Landmark West! v. U.S. Postal Service, 840 F. Supp. 994, 1010 (S.D.N.Y. 1993) (skyscraper not indirect effect of Postal Service participation in project where building would be built regardless of Postal Service decision); Natural Resources Defense Council v. EPA, 822 F.2d 104, 121 n.27 (D.C. Cir. 1987) (impacts of siting of private facility are not “effects” of EPA issuance of NPDES permit)

B. Relationship Between NEPA and Section 404(b)(1) Guidelines: Difficult issues often can arise in harmonizing the procedural requirements of NEPA with the substantive and procedural requirements of the Section 404(b)(1) Guidelines, 40 C.F.R. part 230, which have been issued by the U.S. EPA and which are the primary substantive environmental criteria that guide Corps permitting decisions.

1. Purpose and Alternatives: NEPA requires the identification of a proposed action’s “purpose and need,” which helps to guide the identification of a “reasonable range” of alternatives and the evaluation of how well those alternatives satisfy the project’s underlying goals. The Section 404(b)(1)
Guidelines also require the identification of “overall project purpose,” which also serves as the basis for an analysis of alternatives, known as the “practicable alternatives test.” In the latter case, the Corps may not issue a Section 404 permit “if there is a practicable alternative to the proposed discharge which would have less adverse impact on the aquatic ecosystem, so long as the alternative does not have other significant adverse environmental consequences.” 40 C.F.R. § 230.10(a). An alternative is “practicable” if it is “available and capable of being done after taking into consideration cost, existing technology, and logistics in light of overall project purposes.” Id. at § 230.10(a)(2). Moreover, where special aquatic sites, including wetlands, will be affected, and the activity is not “water dependent,” “practicable alternatives that do not involve special aquatic sites are presumed to be available, unless clearly demonstrated otherwise,” and are presumed to have less adverse impact on the aquatic ecosystem, unless clearly demonstrated otherwise. Id. at § 230.10(a)(3).

With respect to actions subject to NEPA, the Section 404(b)(1) Guidelines specifically state:

[W]here the Corps of Engineers is the permitting agency, the analysis of alternatives required for NEPA environmental documents . . . will in most cases provide the information for the evaluation of alternatives under these Guidelines. On occasion, these NEPA documents may address a broader range of alternatives than required to be considered under [the Section 404(b)(1) Guidelines] or may not have considered the alternatives in sufficient detail to respond to the requirements of these Guidelines. In the latter case, it may be necessary to supplement these NEPA documents with this additional information.

40 C.F.R. § 230.10(1)(4). Thus, the range of reasonable alternatives identified for NEPA purposes can have a significant and potentially controlling effect on the analysis of practicable alternatives under Section 404. But see Sylvester v. U.S. Army Corps of Engineers, 882 F.2d 407, 410 (9th Cir. 1989) (“Sylvester II”) (“A relationship required to be considered in determining reasonable and practicable alternatives need not be of such significance as would be necessary to ‘federalize’ the entire project.” Thus, it is possible for an alternative not to be practicable for Section 404 purposes, but still to be possible so as to avoid the federalization of the entire project under NEPA.)

See also Simmons v. U.S. Army Corps of Engineers, 120 F.3d 664 (7th Cir. 1997): The Corps issued a permit for the construction of a dam and water reservoir to supply water to the City of Marion, Illinois, and the Lake Egypt Water District. The Corps only evaluated alternatives for supplying the water for the two users from a single source. The court
concluded that the Corps had impermissibly narrowed its range of alternatives by defining the project purpose in terms of a single source. “To conclude that a common problem necessarily demands a common solution defies common sense. We conclude that the U.S. Army Corps of Engineers defined an impermissibly narrow purpose for the contemplated project. The Corps therefore failed to examine the full range of reasonable alternatives and vitiated the EIS.” 120 F.3d at 667.

2. **Substance vs. Process:** NEPA is a purely procedural statute. It does not mandate any particular outcome, not even the most environmentally preferable outcome (although that alternative must be identified in the document). NEPA is essentially a “stop, look, and listen” statute designed to ensure informed agency decision making and public disclosure of environmental information. In contrast, as noted above, the Section 404(b)(1) Guidelines impose a substantive standard, which requires the selection of the practicable alternative with the least adverse impact on the aquatic ecosystem. See Carmel-by-the-Sea v. U.S. Dept. of Transp., 123 F.3d 1142, 1152 (9th Cir. 1997) (“[T]his scenario serves to highlight the distinction between the National Environmental Policy Act and the Clean Water Act: the former is procedural and is simply not as demanding as the Clean Water Act on the issue of wetlands.”) In addition, where special aquatic sites are involved, the burden is placed on the permit applicant to demonstrate that there are no practicable alternatives that would avoid special aquatic sites, or that if such alternatives do exist, that they have more severe impacts on the aquatic ecosystem. Thus, the identification of project purpose and alternatives is all the more important in the Section 404 context, because the identification of an alternative as “practicable” can control the agency’s ultimate decision. This has led to significant controversy over the definition of project purpose for Section 404 permitting actions, and over whether certain alternatives are “practicable.” It also highlights the need for care in identifying project purpose and alternatives in the NEPA context, as those decisions may have significant effects within the Section 404 process.

3. **Assessment of Effects.** NEPA requires an assessment of the effects—direct, indirect and cumulative—of an agency’s proposed action on the human environment. That assessment includes effects on a wide range of resources, including air, water, cultural resources, animal and plant species, human communities, etc. The sweep of NEPA is very broad. In contrast, the Section 404(b)(1) Guidelines focus more narrowly on impacts to the “aquatic ecosystem”—although the requirement to pick the practicable alternative with the least adverse impact on the aquatic ecosystem includes the following qualifier: “so long as the alternative does not have other significant adverse environmental consequences.” The generally more narrow focus of the Section 404(b)(1) Guidelines can create some confusion in the review of the Corps’ NEPA analysis for
permit decisions—which should contain the broader focus required by NEPA—and its findings and decisions under Section 404—which are generally more narrowly focused on the issues relevant under the Section 404(b)(1) Guidelines concerning the aquatic ecosystem. (The Corps' own "public interest review" does provide a more expansive scope of review concerning the potential effects of the Corps' permitting decisions, and is more similar in scope to the NEPA review. See 33 C.F.R. § 320.4(a). However, the public interest review criteria are much less specific than the standards and procedures established under Section 404(b)(1), and the more stringent Section 404(b)(1) Guidelines tend to be the greater source of controversy.)

C. **Secondary and Cumulative Impacts Assessment:** Another source of controversy in the NEPA review of Corps permitting decisions is the assessment of secondary and cumulative effects or impacts.

1. **The Regulations**

   a. "Effects" include "direct effects, which are caused by the action and occur at the same time and place," and "Indirect effects, which are caused by the action and are later in time or farther removed in distance, but are still reasonably foreseeable. Indirect effects may include growth inducing effects and other effects related to induced changes in the pattern of land use, population density or growth rate, and related effects on air and water and other natural systems, including ecosystems.

   Effects and impacts as used in these regulations are synonymous. Effects includes ecological . . . aesthetic, historic, cultural, economic, social, or health, whether direct, indirect, or cumulative."

   40 C.F.R. § 1508.8 (emphasis added).

   b. "Cumulative impact" is "the impact on the environment which results from the incremental impact of the action when added to other past, present, and reasonably foreseeable future actions regardless of what agency (Federal or non-Federal) or person undertakes such other actions. Cumulative impacts can result from individually minor but collectively significant actions taking place over a period of time." 40 C.F.R. § 1508.7 (emphasis added).

2. **Judicial Interpretation**
Preliminary Note: Disputes over the analysis of growth-inducing and cumulative impacts often occur in the context of determining whether a proposed action may have a “significant impact” on the human environment, and thus, whether an EIS must be prepared. The goal of the proponent often is to avoid having to “take ownership” of the effects of other actions that may or may not occur in the area. This issue is often particularly relevant in the Section 404 permitting context, where a Corps permit often is required for limited wetlands impacts associated with a much larger nonfederal project, such as a residential or commercial development. The goal of proponents normally will be to limit the extent of the Corps’ analysis in order to avoid the EIS requirement, while opponents will seek a more expansive review.

Fritiofson v. Alexander, 772 F.2d 1225, 1245-46 (5th Cir. 1985): Cumulative effects analysis for Corps permit issuance must identify “(1) the area in which effects of the proposed project will be felt, (2) the impacts that are expected in that area from the proposed project, (3) other actions – past, proposed, and reasonably foreseeable—that have had or are expected to have impacts in the same area, (4) the impacts or expected impacts from these other actions, and (5) the overall impact that can be expected if the individual impacts are allowed to accumulate.” EA should “consider (1) past and present actions without regard to whether they themselves triggered NEPA responsibilities and (2) future actions that are ‘reasonably foreseeable,’ even if they are not yet proposals and may never trigger NEPA-review requirements.” See also City of Carmel-by-the-Sea v. Dep’t of Transportation, 772 F.2d 1225, 1245 (5th Cir. 1985) (adopting Fifth Circuit’s Fritiofson analysis of cumulative impact analysis requirements).

Landmark West! V. U.S. Postal Service, 840 F. Supp. 994 (S.D.N.Y. 1993), aff’d, 41 F.3d 1500 (2d Cir. 1994) (cumulative impact analysis considers other actions as context/background against which incremental effect of proposed action is measured; agency sponsoring proposed action need not “take ownership” of environmental consequences of other actions that provide background for proposed action); see also Coalition on Sensible Transportation v. Dole, 826 F.2d 60, 70-71 (D.C. Cir. 1987) (It “makes sense to consider . . . cumulative effects by incorporating the effects of other projects into the background ‘data base’ of the project at issue, rather than by restating the results of the prior studies.” In this case, the EA and FONSI were “sufficient to alert interested members of the public to any arguable cumulative impacts.”); Piedmont Heights Civic Club v. Moreland, 637 F.2d 430, 441-42 (5th Cir. 1981) (“NEPA does not require an agency to
restate all of the environmental effects of projects presently under consideration. Where the underlying data base includes approved project and pending proposals, the ‘statutory minima’ of NEPA has been met.”)

d. Friends of the Earth v. U.S. Army Corps of Engineers, 109 F. Supp. 2d 30 (D.D.C. 2000): The court found fault with the Corps’ analysis of both indirect (or secondary) and cumulative impacts in its EAs for three casinos on the Mississippi coast. With respect to indirect effects, the court stated: “Even more problematic is the Corps’ total lack of analysis of growth-inducing effects of the casino projects. . . . The Corps . . . contends that it was not required to analyze such impacts because it determined that they are ‘highly speculative and indefinite.’ On this issue, the Corps is simply wrong. . . . The administrative record in this case firmly establishes that increased growth in the area is the only reasonable prediction of what will occur if the casinos are built.” 109 F. Supp. 2d at 41 (citations omitted). Compare Hoosier Environmental Council v. U.S. Army Corps of Engineers, 105 F. Supp. 2d 953, 975-76 (S.D. Ind. 2000): “[T]he riverboat casino project’s purpose is to provide an attractive resort destination to which people would travel on existing roads. This does not automatically lead to the conclusion that, once there, they will build homes, retail stores and service stations. . . . No facts were presented to the [Corps] that would make this assessment unreasonable, nor were there any making the likelihood of secondary development reasonably foreseeable. Thus, the [Corps’] consideration of the indirect effects of the riverboat project was not arbitrary or capricious.” With respect to cumulative impacts, the Friends of the Earth court concluded that “while the Corps dedicated nine or ten pages of each EA to cumulative impacts, the discussion provides no analysis at all. All three EAs merely recite the history of development along the Mississippi coast and then conclude that the cumulative direct impacts ‘have been minimal.’ There is no actual analysis, only that conclusory statement.” 109 F. Supp. 2d at 42.

e. Davis v. Coleman, 521 F.2d 661, 674-76 (9th Cir. 1975): This is the classic case of “growth-inducing impacts,” a form of indirect effect. The court held that the DOT must analyze the growth effects of constructing a new highway interchange in an otherwise undeveloped area. Compare Sierra Club v. Marsh, 769 F.2d 868, 878-79 (1st Cir. 1986) (“[A]gencies should have taken account of the ‘secondary impacts.’ First. . . . building the causeway [to Sears Island] and port [on island] will lead to further development [on island] . . . . Once Maine completes the causeway and port, pressure to develop the rest of the island could well prove
irreversible.''); with Laguna Greenbelt, Inc. v. Dep’t of Transportation, 42 F.3d 517, 525-26 (9th Cir. 1994) (‘Discussion and documentation in the EIS, however, support the EIS’s conclusion that the tollroad will not affect the amount and pattern of growth in Orange County.’ ‘Record shows that 98.5% of all land in the project’s ‘area of benefit’ is already accounted for by either existing or committed land uses not contingent on construction of the corridor.’)
The SWANCC Decision

On January 9, 2001, the U.S. Supreme Court issued its decision in Solid Waste Agency of Northern Cook County v. U.S. Army Corps of Engineers ("SWANCC"), 531 U.S. 159 (2001), in which the Court held that the Corps exceeded its authority under the Clean Water Act ("CWA") when it asserted jurisdiction over isolated ponds that were used as habitat by migratory birds. The Court based its judgment on the CWA itself, holding that the Corps' regulation at "33 C.F.R. 328.3(a)(3), as clarified and applied . . . pursuant to the 'Migratory Bird Rule,' 51 Fed. Reg. 41217 (1986), exceeds the authority granted to [the Corps] under § 404(a) of the CWA." This decision, which affected the geographic scope of the Corps' jurisdiction under Section 404, will have potentially far-reaching effects on the Corps' regulatory program—although the precise extent of those effects is still becoming apparent as lower courts grapple with the implications of the Court's decision.

SWANCC involved the Corps' attempt to assert jurisdiction over an abandoned sand and gravel mining pit that over the years had developed into a successional stage forest with over 200 permanent and seasonal ponds that provided habitat to over 100 species of migratory birds. When a consortium of Chicago-area municipalities purchased the site to use for the disposal of baled, solid waste, the Corps regulatory asserted jurisdiction over the site based on the use of the site by migratory birds. This assertion was based on the so-called Migratory Bird Rule, under which, since 1985, the Corps and EPA had maintained that "waters of the United States" included isolated waters that were used as habitat by migratory birds. See 51 Fed. Reg. 41206, 41217 (1986). After the Corps twice denied its permit applications, the consortium challenged the Corps' jurisdictional authority in court.

Both the district court and the Court of Appeals for the Seventh Circuit upheld the Corps' authority. The Seventh Circuit held that where isolated, intrastate waters were used by migratory birds, jurisdiction was proper under both the CWA and the Commerce Clause of the U.S. Constitution. The appeals court found that the destruction of migratory bird habitat and the resulting decrease in migratory bird populations substantially affects interstate commerce, and thus discharges into isolated waters that may have such an effect are regulable under the Commerce Clause. The court also found that the Corps had interpreted the CWA to extend to such waters and under established principles, its interpretation should be upheld because it was a reasonable reading of the statute. The court concluded that the CWA reaches as far as the Commerce Clause allows.
The Supreme Court reversed the Seventh Circuit, holding that the CWA itself did not support the Corps' assertion of jurisdiction under the Migratory Bird Rule. 531 at 584. The Court acknowledged that it had previously stated that "the term 'navigable' [in the statutory term 'navigable waters'] is of 'limited import' and that Congress evidenced its intent to 'regulate at least some waters that would not be deemed "navigable" under the classical understanding of the term.'" Id. at 587. However, the Court proceeded to state, "But it is one thing to give a word limited effect and quite another to give it no effect whatever. The term 'navigable' has at least the import of showing us what Congress had in mind as its authority for enacting the CWA: its traditional jurisdiction over waters that were or had been navigable in fact or which could reasonably be made so." Id. at 587-88.

Under traditional Chevron analysis, the Corps asked the Court to defer to its administrative interpretation because the Corps alleged that the statute was ambiguous. However, the Court found that statute to be clear on its face, and deference to the agency was unnecessary. Moreover, the court added that, even if the statute were ambiguous, it would not defer to the Corps:

Where an administrative interpretation of a statute invokes the outer limits of Congress' power, we expect a clear indication that Congress intended that result. . . . This concern is heightened where the administrative interpretation alters the federal-state framework by permitting federal encroachment upon traditional state power . . . . Permitting [the Corps] to claim federal jurisdiction over ponds and mudflats falling within the 'Migratory Bird Rule' would result in a significant impingement of the States' traditional and primary power over land and water use.

Id. at 588.

The Court also expressed concern about the constitutional issues raised by the Corps' position, but refused to resolve them. Instead, the Court cited the proposition that "where an otherwise acceptable construction of a statute would raise serious constitutional problems, the Court will construe the statute to avoid such problems unless such construction is plainly contrary to the intent of Congress." Id. After expressing doubt about whether the commerce power extended as far as the Corps claimed, the Court concluded: "We thus read the statute as written to avoid the significant constitutional and federalism questions raised by respondents' interpretation, and therefore reject the request for administrative deference." Id. at 589. The Court therefore held that the Corps lacks jurisdiction over nonnavigable, isolated, intrastate waters, as clarified and applied pursuant to the Migratory Bird Rule.

On January 19, 2001, shortly after the Court's decision, the Corps and EPA issued a joint legal interpretation of SWANCC, in which they took a very narrow view of its effect on their jurisdiction. They noted that the holding was limited to a finding that the Migratory Bird Rule, as applied to nonnavigable, isolated, intrastate waters on the consortium's site, exceeded the Corps' authority under the CWA. They stated that the Court did not strike down the underlying regulation or any other part of the Corps' definition of "waters of the United States."
advised field staff not to rely on the Migratory Bird Rule as the sole basis for asserting jurisdiction, but that they should continue to assert jurisdiction to the full extent of their authority under the statute and regulations for all waters other than nonnavigable, isolated, intrastate waters. The agencies also emphasized that traditionally navigable waters, interstate waters, their tributaries, and wetlands adjacent to each continued to be subject to Corps regulation, consistent with previous Court precedent. Although waters formerly subject to Corps jurisdiction pursuant to the Migratory Bird Rule are no longer jurisdictional, all other waters covered by 33 C.F.R. § 328.3(a)(3) which have a different interstate commerce connection are to be examined on a case-by-case basis by agency legal counsel. Finally, the agencies cited to prior Supreme Court and lower court decisions that have broadly upheld CWA jurisdictional authority.

Selected Post-SWANCC Decisions

- **Headwaters, Inc. v. Talent Irrigation District**, 243 F.3d 526 (9th Cir. 2001): Citizen group sued irrigation district alleging violation of CWA based on application of aquatic herbicide to irrigation canals without obtaining discharge permit under Section 402 of the CWA. District court ruled that irrigation canals were “waters of the United States” under the CWA, but no permit was required because the label on the herbicide approved by EPA under federal pesticide law did not require such a permit. The Ninth Circuit reversed, holding that pesticide approval and labeling under federal law does not preclude need for a permit under the CWA. The Ninth Circuit also concluded that the irrigation canals, which exchange water with a number of natural streams and at least one lake, were “waters of the United States,” as the district court had found. The Ninth Circuit distinguished SWANCC, explaining that the irrigation canals were not “isolated.” “Because the canals receive water from natural streams and lakes, and divert waters to streams and creeks, they are connected as tributaries to other ‘waters of the United States.'” 243 F.3d at 533. The fact that the canals were isolated from natural streams by gates during the application of herbicide did not change the court’s conclusion. The court noted that leaks had occurred, and in any event, the canals were tied to “waters of the United States” at some times, comparing them to jurisdictional tributaries that flow only intermittently. *Id.* at 534.

- **Rice v. Harken Exploration Co.**, 250 F.3d 264 (5th Cir. 2001): Ranch owner sued oil and gas company operating on the ranch under a lease, alleging that the company had discharged oil into a stream and its tributaries in violation of the Oil Pollution Act of 1990 (“OPA”). The Fifth Circuit upheld the district court’s rejection of the ranch owner’s claim. The Fifth Circuit noted that Congress generally intended “waters of the United States” to be synonymous under the CWA and the OPA. The court then confirmed the long-standing conclusion that the term “waters of the United States” does not include “groundwater,” and therefore, those statutes do not regulate discharges to groundwater. With respect to surface water, the court concluded that “a body of water is protected under the Act only if it is actually navigable or is adjacent to an open body of navigable water.” 250 F.3d at 270. The court noted that in this case the creek and its tributaries were intermittent streams that only infrequently contained running water, and that some of the time, the flow of water in the creek is entirely underground. *Id.* In conclusion, the court stated: “[T]here is nothing in the record that could convince a reasonable trier of fact that either Big Creek or any of the
unnamed other intermittent creeks on the ranch are sufficiently linked to an open body of navigable water as to qualify for protection under the OPA.” *Id.* at 271.

- **United States v. Lamplight Equestrian Center,** 2002 U.S. Dist. LEXIS 3694 (N.D. Ill., Mar. 8, 2002): In this district court case, a landowner did not obtain a permit to build a small road across a wetland on his property. The government brought a civil enforcement action against the landowner. The court ruled in the government’s favor, rejecting the landowner’s claim that the Corps lacked jurisdiction. The court concluded that the landowner had conceded facts sufficient to establish a “significant nexus” between the wetland and truly navigable water. A drainage ditch carried water away from the wetland to a tributary of Brewster Creek, which then drained to the Fox River, which is navigable. The court also found that the surface flow was in an unbroken line to the tributary, even though the drainage ditch ends 50 feet away from a drainage swale leading to the tributary. The court noted that water need not flow in an unbroken line at all times, but that an intermittent flow would be sufficient to establish a connection to navigable water. Addressing the issue of what is to be considered a “contiguous” wetland, the court noted that “adjacent,” which is used in the Corps’ definition of “contiguous,” means “being in actual contact [or] touching along a boundary or at a point.” “By virtue of the path of water, whether it be a delta, a meandering swale, or a drainage connection, the wetlands come into actual contact with the tributary of Brewster Creek,” and thus are jurisdictional.

- **United States v. Buday,** 138 F. Supp. 2d 1282 (D. Mont. 2001): Landowner pled guilty to violating the CWA as a result of filling wetlands to create berms along Fred Burr Creek, which subsequently washed out, resulting in the deposition of dirt and debris downstream. Shortly after pleading guilty, the landowner learned of the *SWANCC* decision and moved to withdraw his plea. The court denied the motion. There was no dispute about whether the wetlands were adjacent to Fred Burr Creek. The question the court addressed was whether that creek was a water of the United States subject to Corps jurisdiction under the CWA. Although the creek itself was not navigable-in-fact, it flowed into Flint Creek, which in turn flowed into the Clark Fork River, which became navigable-in-fact about 190 miles downstream from the location of the wetland fill. Despite this long distance, the court noted that case law on “tributaries” clearly established that waters like Fred Burr Creek were subject to CWA jurisdiction. The court stated that “just as wetlands adjacent to navigable waters fall under the Act, tributaries that are distant from but connected to navigable waters are ecologically capable of undermining the quality of navigable waters.” 138 F. Supp. 2d at 1291. “Therefore, Congress must have intended to reach them.” *Id.* at 1291-92.

- **United States v. Rapanos,** 2002 U.S. Dist. LEXIS 3957 (E.D. Mich., Feb. 21, 2002): Landowner was convicted of violating CWA for filling wetlands on his property. The landowner appealed, ultimately petitioning for Supreme Court review. After *SWANCC,* the Court remanded for reconsideration. The district court vacated the conviction on remand and dismissed the case. The court ruled that a wetland with a “surface hydrological connection” through a ditch and a creek to a river that becomes navigable about 20 miles distant is not a “water of the United States” under the CWA. The court cited Congress’ intent to assert jurisdiction over waters that traditionally “were or had been navigable in fact or which reasonably could be so made.” The court stated, “In other words, the plain text of the statute
mandates that navigable waters must be impacted by [the landowner’s] activities.” In this case, the government was unable to prove that the land containing the wetlands, which was roughly twenty miles from the nearest body of navigable water, had any effect on navigable waters.

- **Other cases:**

  * **United States v. Newdunn Associates**, Nos. 2:01cv508 and 4:01cv86 (E.D. Va., Mar. 8, 2002): Corps does not have jurisdiction over wetland that had had its hydrological connection with navigable waters severed by construction of a road.

  * **Colvin v. United States**, 181 F. Supp. 2d 1050 (C.D. Cal. 2001): Salton Sea (in California) is a water of the United States. Sea is a popular destination for out-of-state and foreign tourists who fish, ski, hunt, etc.; and it ebbs and flows with the tide. “Under most any meaning of the term, the Salton Sea is a body of ‘navigable water’ . . . .”

  * **United States v. Interstate General**, 152 F. Supp. 2d 843 (D. Mass. 2001): Where defendant was convicted of filling wetlands regulated by Corps under regulatory subsections other than the one invalidated by the Supreme Court, and under a theory that those wetlands were adjacent to or abutting tributaries impacting navigable waters, *SWANCC* did not require conviction to be reversed.


  * **Brace v. United States**, 51 Fed. Cl. 649 (2002): Court denied U.S. summary judgment motion. More facts needed to determine whether sufficient nexus between property and navigable water. “Should the facts indicate that the 30 acres are not connected to an interstate water in any manner, then the Supreme Court’s ruling in *SWANCC* renders the issue of whether a taking occurred moot, as the Army Corps of Engineers no longer has authority to regulate . . . .”
SPURIOUS INTERPRETATION REDUX:
MEAD AND THE SHRINKING DOMAIN
OF STATUTORY AMBIGUITY

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SECTION J
Spurious Interpretation Redux: *Mead* and the Shrinking Domain of Statutory Ambiguity

Michael P. Healy

Introduction

[T]he object of spurious interpretations is to make, unmake, or remake, and not merely to discover. It puts a meaning into the text as a juggler puts coins, or what not, into a dummy’s hair, to be pulled forth presently with an air of discovery. It is essentially a legislative, not a judicial process, . . . .

In skewering the Supreme Court’s recent decision in *United States v. Mead Corp.*, Justice Scalia’s rhetoric is exceptional. He derides the decision as “one of the most significant opinions ever rendered by the Court dealing with the judicial review of administrative action. Its consequences will be enormous, and almost uniformly bad.” Although Justice Scalia objects to *Mead*’s new and uncertain limits on the applicability of the *Chevron* doctrine, this article will

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1Roscoe Pound, *Spurious Interpretation*, 7 Colum. L. Rev. 379, 382 (1907).


3Id. at 2189 (Scalia, J., dissenting); see also id. at 2177 (“Today’s opinion makes an avulsive change in judicial review of federal administrative action.”).

4See *Chevron U.S.A. v. NRDC*, 467 U.S. 837 (1984). In *Chevron*, the Court established the following two-step analysis of the legality of an agency’s legal interpretation: When a court reviews an agency’s construction of the statute which it administers, it is confronted with two questions. First, always, is the question whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress. If, however,
focus instead on *Mead*'s use of a method of interpretation that imputes a clear intent to Congress and authorizes courts to discern statutory meaning without strong deference to an agency’s expert and political interpretation of the statute.

The article begins by briefly describing the interpretive regime defined by *Chevron*. That regime found in statutory ambiguity an implied delegation of lawmaking power to agencies. The article then discusses how *Mead* changes that default rule to one that delegates principal interpretive lawmaking power to courts in the absence of affirmative evidence of congressional intent to delegate that power to agencies. This shift resulted from an interpretive method that spuriously imputed intent to Congress. Although the *Mead* Court purported to accept the rule of deference dictated by Congress, the Court itself was the source of the imputed intent. The article concludes by discussing how *Mead*'s interpretive approach is similar to the approach in an important and growing line of Rehnquist Court decisions that loads the interpretive dice in favor of results not clearly intended by Congress and thereby arrogates to itself lawmaking power better exercised by the legislature or the agency.

*Chevron*'s Interpretive Regime: Ambiguity and Implied Delegation to Agencies as the Default Rule

Judges identify and promote their political values when they adopt and apply particular methods and canons of statutory interpretation. Moreover, the consistent use of canons of construction should enable all actors in the process of lawmaking – legislatures, agencies, and courts – to adjust their conduct in ways that will make the law more transparent, determinate and

the court determines Congress has not directly addressed the precise question at issue, the court does not simply impose its own construction on the statute, as would be necessary in the absence of an administrative interpretation. Rather, if the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute.

467 U.S. at 842-44.

See Cass R. Sunstein, Legal Reasoning and Political Conflict 168-69 (1996) (“People trying to choose an interpretive method must decide how to allocate power among various groups and institutions - indeed, allocating power is what the choice of an interpretive method does.”); id. at 174 (“a system of legal interpretation is inevitably a function of decisions that are, broadly speaking, political in character.”); John F. Manning, Constitutional Structure and Statutory Formalism, 66 U. Chi. L. Rev. 685, 691-92 (1999) (“Selecting an interpretive methodology thus involves inevitable choices about the institutional allocation of power. If courts give strong deference to agencies' interpretations of the statutes they administer, that arrangement shifts law elaboration authority away from judges and toward the executive. If courts reject the authority of legislative history, they shift power away from committees and bill sponsors and toward agencies and courts. If courts start from an assumption of strong legislative supremacy in statutory cases, they define themselves as subordinates of the legislature.” (footnotes omitted)).
predictable.\textsuperscript{6}

The canon of construction identified in \textit{Chevron}\textsuperscript{7} has played a critical role in defining the relative roles of legislature, agency, and court in developing the content of public law. The canon clearly recognizes the primacy of the legislature by holding that “unambiguously expressed” congressional intent determines the content of law and “must [be] give[n] effect.”\textsuperscript{8} When a statute is ambiguous, however, \textit{Chevron} located lawmaking primacy in the agency, whose interpretation of law must be upheld by a court unless it is unreasonable.\textsuperscript{9}

The default rule of \textit{Chevron}, therefore, is that Congress has delegated to the agency the authority to resolve any statutory ambiguity because, relative to the court, the agency is in a preferred position to make the unresolved policy decision.\textsuperscript{10} This default rule applies regardless

\textsuperscript{6}Professor Eskridge has argued that consistent application of the canons of construction “might constitute an interpretive regime that both restrains judges and enables the citizenry to predict how those judges will apply ambiguous as well as clear statutes. Not least important, such an interpretive regime could serve democracy values . . . as legislators and their staffs could predict how different proposed statutory language would be applied.” William N. Eskridge, Jr., Norms, Empiricism, and Canons in Statutory Interpretation, 66 U. Chi. L. Rev. 671, 679 (1999) (footnote omitted). See also William N. Eskridge, Jr. & Philip P. Frickey, Foreword: Law as Equilibrium, 108 Harv. L. Rev. 26, 86 (1994) (“canons are designed, as we believe and the Court maintains they are, to create a predictable interpretive regime”).

\textsuperscript{7}This canon is presented at \textit{supra} note 4.

\textsuperscript{8}467 U.S. at 842-44.

\textsuperscript{9}Decisions rejecting agency interpretations under the second part of the \textit{Chevron} analysis are quite rare. The Court, however, has recently held that an agency had acted unreasonably in construing an ambiguous statute. See \textit{Whitman v. American Trucking Ass'ns.}, 121 S. Ct. 903, 918 (2001) (“The statute is in our view ambiguous concerning the manner in which Subpart 1 and Subpart 2 interact with regard to revised ozone standards, and we would defer to the EPA's reasonable resolution of that ambiguity. We cannot defer, however, to the interpretation the EPA has given.” (citations omitted)).

\textsuperscript{10}See, e.g., Thomas E. Merrill & Kristin E. Hickman, \textit{Chevron's Domain}, 89 Geo. L.J. 833, 861 (2001) (footnotes omitted), where the authors stated that:

One reason for preferring agency interpretations, which is alluded to by \textit{Chevron} itself, is that agencies are more politically accountable than are courts. Choosing between two or more permissible interpretations of a statute is a political act, involving the exercise of discretion in channeling the coercive powers of the state in one direction rather than another. A robust deference doctrine therefore helps minimize the occasions in which courts are tempted to employ statutory interpretation to impose their policy preferences on a public to which they are not accountable.
of whether the delegation to the agency was intended or unintended. The delegation is a consequence of the statute’s ambiguity. Chevron’s assignment of lawmaking power was based on the Court’s view that the agency is appropriately responsive to political judgment and Congress would be assumed to have intended agency decisionmaking, rather than judicial decisionmaking, when implementation of a statute necessitated a determinate statutory meaning.\footnote{See id. at \_\_ where the Court stated that: Judges are not experts in the field, and are not part of either political branch of the Government. Courts must, in some cases, reconcile competing political interests, but not on the basis of the judges’ personal policy preferences. In contrast, an agency to which Congress has delegated policymaking responsibilities may, within the limits of that delegation, properly rely upon the incumbent administration's views of wise policy to inform its judgments. While agencies are not directly accountable to the people, the Chief Executive is, and it is entirely appropriate for this political branch of the Government to make such policy choices -- resolving the competing interests which Congress itself either inadvertently did not resolve, or intentionally left to be resolved by the agency charged with the administration of the statute in light of everyday realities. When a challenge to an agency construction of a statutory provision, fairly conceptualized, really centers on the wisdom of the agency's policy, rather than whether it is a reasonable choice within a gap left open by Congress, the challenge must fail. In such a case, federal judges -- who have no constituency -- have a duty to respect legitimate policy choices made by those who do. The responsibilities for assessing the wisdom of such policy choices and resolving the struggle between competing views of the public interest are not judicial ones.}

\footnote{The Court made this point explicitly in Chevron, when it stated that: If Congress has explicitly left a gap for the agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation. Such legislative regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute. Sometimes the legislative delegation to an agency on a particular question is implicit rather than explicit. In such a case, a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency. 467 U.S. at \_. See also id. at \_\_ (“Perhaps [Congress] consciously desired the Administrator to strike the balance at this level, thinking that those with great expertise and charged with responsibility for administering the provision would be in a better position to do so; perhaps it simply did not consider the question at this level; and perhaps Congress was unable to forge a coalition on either side of the question, and those on each side decided to take their chances with the scheme devised by the agency. For judicial purposes, it matters not which of these things occurred.”).}
In sum, *Chevron*’s interpretive regime defined a background rule that yielded agencies significant lawmaking power in the absence of unambiguously expressed legislative intent.

*Mead* and the Imputation of Legislative Intent:  
A Narrowed Scope for *Chevron* Deference

The Court’s decision in *Mead* redefines the default rule for determining when the *Chevron* interpretive regime will apply. The redefinition is accomplished by the Court’s imputation of legislative intent. The Court concludes that statutory silence regarding delegation to the agency of *implied* decisionmaking authority means that Congress intended that an agency is not to be accorded *Chevron* deference in its interpretive decisions. *Chevron*, of course, had indicated that the same rule of deference should apply regardless of whether the delegation is express or implied. Indeed, in accounting for *Chevron*’s significance, commentators have focused on how *Chevron* worked a “fundamental” shift in administrative law by eliminating the distinction in degrees of deference drawn in earlier Supreme Court decisions between exercises of expressly or impliedly delegated authority.15


13 The limits on the scope of *Chevron* deference newly defined by *Mead* were not wholly surprising given the Court’s decision the previous term in *Christensen v. Harris County*, 120 S. Ct. 1655 (2000). There, the Court indicated that the scope of *Chevron*’s applicability was uncertain, but failed to identify a rationale for the inapplicability of *Chevron*, relying instead on *ipse dixit* to reject the agency’s request for deference:

we confront an interpretation contained in an opinion letter, not one arrived at after, for example, a formal adjudication or notice-and-comment rulemaking. Interpretations such as those in opinion letters -- like interpretations contained in policy statements, agency manuals, and enforcement guidelines, all of which lack the force of law -- do not warrant *Chevron*-style deference. Instead, interpretations contained in formats such as opinion letters are "entitled to respect" under our decision in *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944), but only to the extent that those interpretations have the "power to persuade," ibid.  

Id. at __. Only Justice Souter, the author of the Court’s opinion in *Mead* appeared to foretell *Mead*’s analytic approach: Justice Souter concurred in *Christensen*, stating that *Chevron* deference would have followed if the agency’s decision had been adopted through informal rulemaking. Id. at __. In that form, the agency decision would have met both of the *Mead* requirements that are identified and discussed infra.

14 See supra note __ and accompanying text.

15 See Merrill & Hickman, supra note __, at 833-34 (footnotes omitted), in which the authors stated that:
Justice Souter's decision in *Mead* twice alludes to the distinction in types of delegations the legal significance of which had been eliminated by *Chevron* and thereby indicates that full, *Chevron*-type deference will continue to apply in any case of an express delegation. He first signals this result when he offers a narrowed restatement of the rule of *Chevron* deference, focusing on express delegations:

> When Congress has "explicitly left a gap for an agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation," and any ensuing regulation is binding in the courts unless procedurally defective, arbitrary or capricious in substance, or manifestly contrary to the statute.\(^{16}\)

Justice Souter provides a second indication when he presents his argument regarding the background expectation of congressional intent about judicial deference, which focuses only on instances of implied delegation.\(^{17}\)

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*Chevron* expanded the sphere of mandatory deference through one simple shift in doctrine: It posited that courts have a duty to defer to reasonable agency interpretations not only when Congress expressly delegates interpretative authority to an agency, but also when Congress is silent or leaves ambiguity in a statute that an agency is charged with administering. The Court in *Chevron* blandly referred to such gaps and ambiguities as "implied" delegations of interpretative authority and treated these implied delegations as equivalent to express delegations. *Chevron*'s equation of gaps and ambiguities with express delegations turned the doctrine of mandatory deference, formerly an isolated pocket of administrative law doctrine, into a ubiquitous formula governing court-agency relations. With this one small doctrinal shift, the Court effected a fundamental transformation in the relationship between courts and agencies under administrative law.

See also Antonin Scalia, Judicial Deference to Administrative Interpretations of Law, 1989 Duke L.J. 511, ___ (reaching similar conclusion about *Chevron*'s change in the law of deference).

\(^{16}\)121 S. Ct. at 2171 (citations and footnote omitted).

\(^{17}\)See id. at 2172 (citations omitted), where the Court states that: This Court in *Chevron* recognized that Congress not only engages in express delegation of specific interpretive authority, but that "[s]ometimes the legislative delegation to an agency on a particular question is implicit." Congress, that is, may not have expressly delegated authority or responsibility to implement a particular provision or fill a particular gap. Yet it can still be apparent from the agency's generally conferred authority and other statutory circumstances that Congress would expect the agency to be able to speak with the force of law when it addresses ambiguity in the statute or fills a space in the enacted law, even one about which "Congress did not actually have an intent" as to a particular result. . .
It is in these cases of implied delegation that the *Mead* Court limits the applicability of *Chevron* deference. Such deference will be accorded to agency decisions only when a court concludes that Congress "expect[ed]" *Chevron*-type deference based on "statutory circumstances":

it can still be apparent from the agency's generally conferred authority and other statutory circumstances that Congress would expect the agency to be able to speak with the force of law when it addresses ambiguity in the statute or fills a space in the enacted law, even one about which "Congress did not actually have an intent" as to a particular result. When circumstances implying such an expectation exist, a reviewing court has no business rejecting an agency's exercise of its generally conferred authority to resolve a particular statutory ambiguity simply because the agency's chosen resolution seems unwise, but is obliged to accept the agency's position if Congress has not previously spoken to the point at issue and the agency's interpretation is reasonable ....

This reading of congressional intent is actually more elaborate than it might appear, because the Court's reference to "an agency's exercise of its generally conferred authority" carries a particular meaning. This meaning, expressed in the Court's statement of its holding, implicates the procedures employed by the agency in reaching the decision at issue. In the Court's view, Congress should be understood to have intended *Chevron* review in instances of an implied delegation only when the agency has been delegated relevant decisionmaking authority and reached its decision through a decisionmaking process that gives the decision procedural legitimacy.

The interpretive default rule defined by *Mead* is striking in two respects. First, the Court's position that it is simply and properly following the intent of the legislature rings hollow: on its face, the imputation of intent is too far reaching and the interpretive result is spurious.

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18Id. (citations omitted).

19The Court's holding was as follows:
We hold that administrative implementation of a particular statutory provision qualifies for *Chevron* deference when it appears that Congress delegated authority to the agency generally to make rules carrying the force of law, and that the agency interpretation claiming deference was promulgated in the exercise of that authority. Delegation of such authority may be shown in a variety of ways, as by an agency's power to engage in adjudication or notice-and-comment rulemaking, or by some other indication of a comparable congressional intent.

Id. at 2171.

20See Henry M. Hart, Jr. & Albert M. Sacks, The Legal Process: Basic Problems in the Making and Application of Law 1194-95 (William N. Eskridge, Jr. & Philip P. Frickey, eds., 1994), where the authors stated that:

[The principle of institutional settlement], obviously forbids a court to substitute its own ideas for what the legislature has duly enacted. What the legislature *has*
Can we reasonably believe that Congress intended that varied levels of deference should be accorded to administrative decisions on the basis of the indeterminate, inconsistent, and ambiguous factors weighed by the Court in deciding that Congress did not intend to accord *Chevron* deference to the Customs Service in its customs rulings? The factors considered by the Court range from delegation of rulemaking authority, to the regime of judicial review of Customs classifications, to the agency’s practice in issuing its classifications, to the number of such classifications.\(^{21}\)

Second, the *Mead* rule fundamentally shifts the default rule from one in which congressional silence related to an implied delegation yielded *Chevron* deference to the agency to one in which congressional silence results in a delegation of lawmaking primacy to the courts, which are to give an agency interpretation only as much deference as it has power to persuade the court. At least two flaws of this redefined presumption of nondelegation to agencies are apparent. First, by establishing a new background rule for understanding legislative action, *Mead* has shifted the context for understanding congressional action. The retroactive application of this new interpretive regime to statutes enacted prior to the Court’s decision in *Mead* can only be understood to unsettle the expectations of the legislature, assuming that they understand the background presumptions at all.\(^{22}\)

\(^{21}\)See 121 S. Ct. at 2174-75. Justice Scalia has argued that it was the difficulty of making just this sort of conclusion about legislative intent regarding implied delegations to agencies that had led to the broad application of the *Chevron* standard in the first place. See Antonin Scalia, supra note __, at ____ (“*Chevron*, however, if it is to be believed, replaced this statute-by-statute evaluation (which was assuredly a font of uncertainty and litigation) with an across-the-board presumption that, in the case of ambiguity, agency discretion is meant.”).

Two courts have applied this *Mead* test and, after considering the various factors suggestive of congressional intent determined that Congress intended *Chevron* deference to apply. See Federal Election Comm’n v. National Rifle Ass’n of Am., 254 F.3d 173, 186 (D.C. Cir. 2001); Fontana v. Caldera, 160 F. Supp. 2d 122, 128 (D.D.C. 2001).

\(^{22}\)The Court’s shifting background rules for understanding the meaning of congressional action have led to Professors Eskridge and Frickey criticism of the Court’s “‘bait and switch’” approach to statutory interpretation:

[Two recent] decisions surely came as a surprise to Congress. Indeed, there is a "bait and switch" feature to [these] cases . . . : when Congress enacted the statutes in question, the constitutionality of the state-infringing provisions was clear and Congress could not have anticipated the *Gregory* rule; nor could a reasonable observer have predicted the
More significantly, *Mead* is flawed because its presumptive implied delegation of interpretive authority to courts rather than agencies will mean that statutory law will be more often decided by courts, than by democratically responsive decisionmakers. When applicable, broad *Chevron* deference is, of course, only triggered when Congress itself has not dictated a particular statutory meaning. The problematic effect of *Mead* is that when a statute is ambiguous and accordingly in need of interpretation to determine the content of law, the court rather than the more democratically responsive agency will have ultimate decisionmaking power. Justice Scalia argues, moreover, that *Mead*'s rule of deference will result in ossification of statutory law, because once a court exercising the primary lawmaking authority recognized by *Mead* determines the meaning of a statute, that meaning can be changed only by amendment of the statute. To the extent Justice Souter's intent-based scope of *Chevron*-doctrine applicability can avoid this problem, the Court's attribution of congressional intent becomes even less believable. It seems fanciful that Congress would have intended that different standards of judicial review would apply, and the statute would have different meanings, based on the procedures pursued by the agency at the time it defined its interpretation of the statute.

In sum, the Court's interpretive turn in *Mead* can be seen only as spurious interpretation because the Court's analysis goes so far in imputing intent to Congress that the whole enterprise can only be seen as fictitious. There was, to be sure, fiction in defining the default rule in *Chevron*. The imputation of intent accomplished by the *Chevron* doctrine is far less

expansion of *Gregory* in [the second case]. When the Court's practice induces Congress to behave in a certain way and the Court then switches the rules, Congress justifiably feels taken.

Eskridge and Frickey, supra note __, at 85 (footnote omitted). The Court's regime of *Chevron* deference would have been understood by Congress to apply since 1984. The Court's analysis in *Mead* included consideration of the intent of statutory amendments enacted in 1993. See 121 S. Ct. at 2169 & 2175.

23See *Mead*, 121 S. Ct. at 2181-83.

24Recall that Justice Souter was the only Justice in *Christensen* (discussed supra at note (__)) to express the opinion that the agency there might be able to have a court approve its interpretation of the statute if it proceeded by notice-and-comment rulemaking, rather than by an informal letter. 120 S. Ct. at ____ (Souter, J., concurring) (“I join the opinion of the Court on the assumption that it does not foreclose a reading of the Fair Labor Standards Act of 1938 that allows the Secretary of Labor to issue regulations limiting forced use.”).

25Cf. *Mead Corp.*, 121 S. Ct. at 2180 (Scalia, J., dissenting) (“Is it likely--or indeed even plausible--that Congress meant, when such an agency chooses rulemaking, to accord the administrators of that agency, and their successors, the flexibility of interpreting the ambiguous statute now one way, and later another; but, when such an agency chooses case-by-case administration, to eliminate all future agency discretion by having that same ambiguity resolved authoritatively (and forever) by the courts?”).
objectionable for two reasons. First, the imputation of intent accepted a delegation to agencies rather than to the courts for the primary authority to resolve a statute’s ambiguities. *Chevron* was accordingly not self-serving in its understanding of congressional intent. Second, the legal actor to whom lawmaking authority is attributed by *Chevron* is the politically accountable decisionmaker, rather than the nonpolitically responsive courts.26

**Mead** and Presumptive Statutory Meaning

In assessing the significance of *Mead*’s imputation of legislative intent, one should not understand the case as an exceptional effort to rein in the scope of application of the *Chevron* doctrine. Rather, the case is yet another important example of the Rehnquist Court’s unwillingness to conclude that a statute’s meaning is ambiguous, due to the Court’s own imputation of clear meaning or intent. Considered in this light, the case shows that the Court is continuing a decisive move away from deference to agency interpretations based on a spurious claim of yielding to clear statutory meaning or legislative intent.27

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26Cf. Frank E. Horack Jr., The Disintegration of Statutory Construction, 24 Ind. L.J. 335, 342 (1949), in which the author makes the following comments about rules of presumptive meaning of statutes:

[Rules of interpretation in the nature of presumption] are fictional rules of interpretation and frequently lead to results exactly opposite those which legislatures intend. At best they are judicial standards requiring a particular form of legislative expression. As such, they are within limits defensible. Every system of government depends upon the ability of society to require of its people certain formalities as prerequisite to legal consequence. It is not too much to require this of the agencies of government as well. Formalities, however, become intolerable when they no longer reflect the normal expectations of the society for which they were constructed. . . .

27Understood in this light, Justice Scalia’s *cri de coeur* regarding *Mead*’s fundamental shift in administrative law, see supra note ___ and accompanying text, can only be understood as disingenuous. Because Justice Scalia typically concludes that a statute has a clear meaning, relying when necessary on the imputation of statutory meaning, see infra notes ___ - ___ and accompanying text (discussing Justice Scalia’s opinion for the Court in *American Trucking Ass’ns*.), he is less likely to get to the second step of the *Chevron* analysis – the step at which strong deference is present. See supra note ___. This point has been well stated in a recent article:

Justice Scalia has taken the position that it is appropriate for courts to take policy considerations into account as part of the ordinary tools of statutory construction deployed at step one. The upshot of this position is that Justice Scalia invokes *Chevron* more consistently than other Justices, but also ends up deferring to agency views less than other Justices. In Justice Scalia’s hands, *Chevron* has the paradoxical result of diluting, rather than strengthening, the practice of deference to executive understandings of law.
Two other decisions by the Court during its 2000 Term provide important examples of how the Court has come to restrain administrative discretion by constraining the scope of statutory ambiguity through rules of presumption. In Solid Waste Agency of Northern Cook County (SWANCC) v. United States Army Corps of Engineers, the Supreme Court held that, when it enacted the Clean Water Act, Congress did not delegate to the Corps of Engineers the authority to regulate the filling of “other waters.” The Corps supported the legality of its view of the Act’s jurisdictional scope by its claim that the statute was ambiguous in defining its jurisdictional reach and that the Court therefore had to defer to the Corps’ regulation under Chevron. The Court held, however, that the meaning of the statute’s text was plainly contrary to the Corps’ position and that even an ambiguous text would not have resulted in deference on this question. The Court held that the Corps could not rely upon an inferential delegation of discretionary power to the agency, but instead had to show clear statutory authority for its exercise of jurisdiction. For the Rehnquist Court, therefore, statutory ambiguity was no longer

Merrill & Hickman, supra note _, at 860 (footnotes omitted). Indeed, Justice Scalia has made much the same comment about his application of Chevron deference. See Scalia, supra note __, at ___ (“One who finds more often (as I do) that the meaning of a statute is apparent from its text and from its relationship with other laws, thereby finds less often that the triggering requirement for Chevron deference exists. It is thus relatively rare that Chevron will require me to accept an interpretation which, though reasonable, I would not personally adopt.”).


30 See 33 C.F.R. § 328.3(a)(3).

31 See 121 S. Ct. at 683. Indeed, the Court itself had found the definition of “navigable waters” to be ambiguous in United States v. Riverside Bayview Homes, Inc., 474 U.S. 121 (1985), and had deferred to the Corps’ exercise of regulatory jurisdiction over wetlands adjacent to navigable waters. See id. at 131.

32 The Court accordingly assumed the applicability of Chevron and then explained why, in its view, Chevron deference was unwarranted. Because the “Migratory Bird Rule” was an interpretation of the statute that had not been adopted following notice and comment rulemaking, see 121 S.Ct. at 678, the Court might have held that Chevron deference was inapplicable.

33 The Court stated that: These are significant constitutional questions raised by respondents' application of their regulations, and yet we find nothing approaching a clear statement from Congress that it intended § 404(a) to reach an abandoned sand and gravel pit such as we have here. Permitting respondents to claim federal jurisdiction over ponds
the sufficient basis for the Corps’ assertion of regulatory authority that it had been in *Riverside Bayview Homes*. The Court’s demand for a clear statement of regulatory authority in the Clean Water Act is quite important because it responds to a request for *Chevron* deference with a rule of construction that shifts the burden to the Corps to come forward with an express delegation of authority from Congress to support its jurisdiction, rather than mere ambiguity. 

"The Court’s use of this clear statement rule gave the Court license both to ignore strong evidence of legislative intent and purpose supporting the exercise of jurisdiction over ‘other waters’ and to trump the Corps’ long-standing interpretation of the Clean Water Act." 

Another recent decision similarly limiting the scope of statutory ambiguity is *Whitman v.*
American Trucking Ass'ns. There, Justice Scalia, writing for the Court, concluded that the Clean Air Act ("CAA") barred the Environmental Protection Agency ("EPA") from considering costs in defining the National Ambient Air Quality Standards ("NAAQS"): "The text of § 109(b), interpreted in its statutory and historical context and with appreciation for its importance to the CAA as a whole, unambiguously bars cost considerations from the NAAQS-setting process, and thus ends the matter for us as well as the EPA." The Court's decision that the statute was unambiguous followed from its application of clear statement rules similar to the one applied in SWANCC. The Court initially stated that, before it would recognize that the statute authorized the EPA to consider costs in defining the NAAQS, "respondents must show a textual commitment of authority to the EPA to consider costs [and] that textual commitment must be a clear one." In the Court's colorful view, "Congress . . . does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions -- it does not, one might say, hide elephants in mouseholes." Later, the Court again declined to conclude that the Clean Air Act's language was ambiguous in determining whether EPA had authority to consider costs: "we find it implausible that Congress would give to the EPA through these modest words the power to determine whether implementation costs should moderate national air quality standards." In the Court's view, Congress could be understood to have delegated in the Clean Air Act particular aspects of administrative discretion to the EPA only if there had been an explicit and clear

37 Id. at ___.
38 Id. at 909.
39 Id. at 909-10 (citing MCI Telecommunications Corp. v. American Telephone & Telegraph Co., 512 U.S. 218, 231 (1994) & FDA v. Brown & Williamson Tobacco Corp., ___ U.S. ___, 159-60). The Court, of course, decides itself whether an elephant is present and whether a mousehole is its hiding place.
40 Id. at 910 (citation omitted). The Court continued to express its opinion that only clearly stated text, rather than an ambiguous one, could be read as a delegation to EPA of discretion to consider costs:

Even if we were to concede those premises, we still would not conclude that one of the unenumerated factors that the agency can consider in developing and applying the criteria is cost of implementation. That factor is both so indirectly related to public health and so full of potential for canceling the conclusions drawn from direct health effects that it would surely have been expressly mentioned in §§ 108 and 109 had Congress meant it to be considered. Yet while those provisions describe in detail how the health effects of pollutants in the ambient air are to be calculated and given effect, see § 108(a)(2), they say not a word about costs.

Id.
delegation, rather than statutory ambiguity. This more exacting default rule, of course, turned on the Court’s own view that, in the particular statutory context, Congress can be expected to have spoken clearly to accomplish the delegation.

Notably, Justice Breyer disagreed with this aspect of the Court’s decision. He rejected the Court’s use of presumptions in giving a clear meaning to the statutory text and urged instead that, in the absence of a statute that clearly bars an agency’s consideration of costs, the agency should have discretion to consider costs in implementing the statute:

In order better to achieve regulatory goals—for example, to allocate resources so that they save more lives or produce a cleaner environment—regulators must often take account of all of a proposed regulation's adverse effects, at least where those adverse effects clearly threaten serious and disproportionate public harm. Hence, I believe that, other things being equal, we should read silences or ambiguities in the language of regulatory statutes as permitting, not forbidding, this type of rational regulation.\(^{41}\)

Justice Breyer, however, considered the CAA’s “legislative history and alternative sources of statutory flexibility” and, relying on these additional indicia of expressed congressional intent, came to the same conclusion as the majority: that, in enacting the Clean Air Act, Congress clearly intended to bar the EPA from considering costs in defining the NAAQS.\(^ {42} \) Under Justice Breyer’s approach, the agency would have the decisionmaking authority regarding the consideration of the costs of regulations when there was no clear evidence of congressional intent to bar its consideration of that factor.

In sum, through its application of rules of interpretation, the Supreme Court has placed important limitations on the domain of statutory ambiguity. *Mead* takes that same approach and thereby limits the scope of application of the *Chevron* doctrine.

**Conclusion**

To be sure, *Mead* is important for the limits that it imposes on the applicability of *Chevron* deference. The case is also important because it continues the provocative use by the Rehnquist Court of an interpretive regime that imputes a clear intent to Congress and identifies a meaning of the statute with a limited consideration of the agency’s expert and political interpretation.

\(^{41}\)Id. at ____ (Breyer, J., concurring).

\(^{42}\)Id. at ____.
ETHICAL CONCERNS FOR THE ENVIRONMENTAL LAW PRACTITIONER

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SECTION K
ETHICAL CONCERNS FOR THE ENVIRONMENTAL LAW PRACTITIONER

ASSESSMENT OF CONFLICT OF INTEREST

A HYPOTHEtical PROBLEM

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FACTUAL BACKGROUND

Mega Law Firm ("Mega") was hired by Will B. Against in January 2001 to prepare Articles of Incorporation for Clear Skies, Inc., a corporation being organized to sell medical products for treatment of eye disorders, and a lease of warehouse property by Will B. Against to Clear Skies, Inc. Will B. Against is the incorporater and an officer and director of Clear Skies, Inc. Mega informs Will B. Against that Mega's representation is of Clear Skies, Inc., not Will B. Against in his individual capacity. Mega does not perform any legal services for Will B. Against in his individual capacity. Following the filing of the Articles of Incorporation and the execution of the lease on March 1, 2001, Mega performs no further legal services for Clear Skies, Inc.

Belching Smokestacks, Inc. is a manufacturer that is a major source of air pollutants and subject to a Title V operating permit. A draft Title V permit is prepared by the Kentucky Division for Air Quality and public notice of the draft permit is given on May 1, 2001.

Will B. Against sees the public notice in the newspaper, and opposes the issuance of a Title V permit to Belching Smokestacks, since his mansion and horse farm are located in an area that is down wind from the Belching Smokestacks facility. Will B. Against contacts the corporate attorney at Mega who prepared the Articles of Incorporation and lease for Clear Skies, Inc., and asks whether Mega would represent Will B. Against to oppose the issuance of the Title V permit to Belching Smokestacks.

The corporate attorney makes inquiry to the environmental group within Mega to determine whether the environmental group would undertake a representation in opposition to issuance of the permit to Belching Smokestacks. The corporate attorney is informed that as a matter of policy, Mega will not represent a person opposing the issuance of an environmental permit because of the potential for establishing a legal position that might be inconsistent with
positions taken on behalf of other clients in similar permitting matters. The corporate attorney for Mega then informs Will B. Against that Mega will not accept the representation because of this policy.

Will B. Against then hires another law firm to file a Petition for Hearing on his behalf in opposition to the issuance of a permit to Belching Smokestacks. Belching Smokestacks then retains Mega to represent its interests in the administrative hearing.

Upon learning of the representation by Mega of Belching Smokestacks, Will B. Against informs Mega that it has a conflict of interest, and demands that Mega withdraw from further representation of Belching Smokestacks.

QUESTIONS AND ISSUES

Under these facts, is Mega required to withdraw from its representation of Belching Smokestacks?

Is Will B. Against a client of Mega? Refer to SCR 3.130 (1.13) Organization as Client.

Is Mega required to withdraw because Will B. Against is an officer and/or director of Clear Skies, Inc.? Refer to SCR 3.130 (1.13).

Is Clear Skies, Inc. a current or former client of Mega? Refer to SCR 3.130 (1.7) Conflict of Interest: General Rule, which prohibits representation of a client if representation of that client will be directly adverse to another client, and prohibits representation if the representation of that client may be materially limited by the lawyer’s responsibilities to another client or to a third person. (Undivided loyalty test.) Refer also to SCR 3.130 (1.9) Conflict of Interest: Former Client, which prohibits representation of another person in the same or substantially related matter in which that person’s interests are materially adverse to the interests of the former client. (Substantial relationship test.)

Is Mega required to withdraw if Mega is currently providing legal services to Clear Skies, Inc., but the services are limited to representation concerning labor-employment issues, and do not include environmental representation? Refer to SCR 3.130 (1.7). Refer also to SCR 3.130(1.2). Is Mega required to withdraw if Clear Skies, Inc. is a party to the Petition for Hearing?
Is Mega required to withdraw if Mega represented Will B. Against in his individual capacity by preparing a Will and Estate Plan for Mr. Against, but that work ceased prior to Mega’s engagement by Belching Smokestacks? Refer to SCR 3.130 (1.9).

Is Mega required to withdraw if Mega is currently providing legal services to Mr. Against concerning a real estate matter, that is unrelated to the property used by Belching Smokestacks? Refer to SCR 3.130 (1.7). Refer also to SCR 3.130(1.2).

Is Mega required to withdraw if Will B. Against discussed the reasons for his opposition to the Belching Smokestacks permit in his discussions with the corporate attorney of Mega? What if the discussion involved confidential information?
You are a member of a medium sized firm that has a varied practice including property acquisitions for major construction.

A large corporation, Erebus Motor International (Erebus) is looking for a site to build a plant making environmentally friendly vehicles that use passive electric energy to boost gas mileage. It has become good PR, and a boost for the stock price, for an international corporation to have an environmentally friendly and a family friendly image. Erebus always provides on site day care. The plant would create 300 good-paying jobs for your community and is highly sought after by other states as well. The corporation, in support of their image as a 'green' corporation, is looking for a tract of land that has no existing environmental issues. Your firm has been contacted about representing the Erebus in acquiring suitable land, which will put you in the position to have frequent contacts with high ranking members of your state government.

As part of your negotiations, your firm disclosed to Erebus that one or more of the properties in which they may be interested may be owned by persons or corporations that are current or former clients of your firm.

-Can your firm represent Erebus in its efforts to acquire the property it needs?

For the past decade, your most reliable client has been Reddy N. Able. Reddy is always in some kind of litigation and those fees can be counted on every month to pay the rent. Reddy is a good old boy who doesn't always take your advice, but who always pays his bill on time.

Reddy is the only son of Tuff N. Able, a venerable businessman, mover and shaker. Reddy works with the various family businesses and is viewed as his father's heir apparent, but there is no paperwork that defines his role. Technically the businesses are Tuff N. Able d/b/a Able Unlimited. Tuff's health has been declining steadily and Reddy is preparing to inherit most of a substantial estate including several large tracts of real estate.

The largest piece of real estate was also the location of an engine overhaul and machine shop (The Shop) that Tuff ran for forty years that specialized in overhauling engines, especially engines used in pipelines. Tuff used the strongest degreasers he could find. His favorite was "Gunk-off", which "did the job" for Tuff, but which has now been determined to be a dense non aqueous phase liquid (DNAPL), which tends to sink through soil into groundwater.

Tuff always poured the dirty solvents out behind the shed. If there were more than ten gallons of the stuff, Tuff would put it in an old tank on the back of a pick-up truck he had and drive off. He never said where he went, but Reddy knows about a sunken area on the back of the property that could take large amounts of liquid one day and be empty the next morning. Just before his latest illness, Tuff had some grading work done around the sunken area at the back of the property, brought in fill dirt to cover the surface and planted grass.

Your firm has accepted Erebus' offer of employment and Erebus has identified the Able Unlimited property as a key part of the tract of land it will need in order to build in your community.
-Are there additional disclosures you need to make to Erebus?
-Is there a disclosure you need to make to Reddy?

You have disclosed to Erebus your prior representation of Reddy and Able Unlimited. Reddy has decided he wants to go into stock car racing and wants his dad's land to be bought by Erebus. Reddy knows how they are about being a 'green' corporation and wants something to show them that the land is fine. You have talked to Reddy before about doing an environmental audit and he wants to look the property over himself and report that there are no problems, since the land looks fine. He wants you to advise him on preparing the audit and look it over when it is done.

-Can you represent Reddy?

You referred Reddy to a lawyer who rents space from your firm and has use of the firms secretarial staff and library for a set fee per month. The referral is on a limited basis for review of Reddy's environmental audit and you know this lawyer cannot try to steal Reddy's business from you because he will not risk his rent/secretary/library deal with your firm. Reddy has done his investigation which consisted of Reddy having walked around the property and not seeing anything bad. Reddy drafted the report himself and it says the property is fine. The report also discussed the sunken area at the back of the property and states that it was fully remediated by Tuff. Reddy gave a copy to Erebus and filed a copy with the referral lawyer. Since you were his lawyer for so long, Reddy dropped off a copy of the report that your secretary put in his file. In the meantime, Erebus has made quiet offers to the owners of the property it needs including an offer to Tuff for The Shop property.

-Can you continue to represent Erebus?

Tuff has passed away and Reddy has come in to talk about the estate. While you are talking, Reddy tells you that, over the course of the thirty years he worked with his dad, he went with Tuff on the tanker truck about half a dozen times and every time Tuff dumped the used liquid into the sunken area at the back of the property.

-Do you owe any duty to Erebus?
-Can you continue to represent Reddy in the administration of Tuff's estate.

Those darned environmental bureaucrats say they have found a problem with the groundwater in your area due to DNAPLs and are doing a regional assessment for facilities that used Gunk-off and similar degreasers. The pointy headed bureaucrats (PHB) want to identify all facilities that used Gunk-off and identify all possible areas that might be considered solid waste management units (SWMUs) or areas of concern (AOCs) for immediate soil removal and groundwater remediation. Your local newspaper, pesky pinko yellowsheet (PPY) is trailing after the PHBs and writing big stories about contamination killing children based on a new study that shows small amounts of the primary constituent in Gunk-off to cause brain damage in children.
under the age of 12 when ingested, particularly in water. All it takes to set off the PPY is for the PHBs to seem interested in a piece of property. One of the PHBs has started asking Reddy's employees about how the shop operated and how they disposed of their spent solvents. The employee didn't know what they meant, but they are likely to be back. One story about contamination will scare off Erebus due to their concern with their 'green' image. The PHBs have talked to Erebus which has offered to show its files to the PHBs including Reddy's environmental audit.

-Does Reddy still have an environmental audit privilege?
-Do you owe a duty to Erebus?
-Do you owe a duty to the PHBs?
-Anything you believe you should do?

Right before Erebus announced that it was planning to build a new plant, Reddy found an old 200 gallon tank half buried out behind the shed. Reddy wanted the tank taken out and found that it contained about 75 gallons of stuff that smelled like Gunk-off along with some water. Reddy had the liquid pumped out, excavated a small portion of the sunken area, dumped the liquid there and replaced the soil and vegetation.

Erebus has since put options on the land and published its plant plan. Erebus is relying, in part, on the environmental audit provided by Reddy. The on-site day care center will be some distance from the plant and will use well water. The old sunken area will be part of the playground for the children.

-Do you owe a duty to Erebus?
-Are there instructions you should give to Reddy?
-Do you owe a duty to the PHBs?