



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

JUN - 8 2009

OFFICE OF CONGRESSIONAL AND
INTERGOVERNMENTAL RELATIONS

The Honorable Joe Barton
Ranking Member
Committee on Energy and Commerce
U.S. House of Representatives
Washington, DC 20515

JUN 26 2009

Dear Congressman Barton:

Thank you for your May 7, 2009 letter to Administrator Jackson requesting information regarding the closed criminal case, United States v. Anne Masters Sholtz, involving fraudulent activity relating to the Regional Clean Air Incentives Market (RECLAIM) program, an emissions credit trading program run by the South Coast Air Quality Management District (SCAQMD) to control emissions that contribute to ozone and particulate pollution in Los Angeles and Orange Counties. I appreciate your interest in this matter as it pertains to pending legislation on climate change.

In your letter, you express concern about the potential implications of the Sholtz case for cap and trade programs generally and for the greenhouse gas cap and trade programs being considered by Congress as part of energy legislation this year. To address your concerns, it is helpful to provide some background on RECLAIM and on EPA's cap and trade programs.

RECLAIM is one form of a cap and trade program. It is different in several ways from the cap and trade programs that are run by EPA and that are models for the cap and trade programs being considered by Congress for reducing greenhouse gases. For example, in the RECLAIM program, each business faces an emissions cap for the year. Credits are assigned each year and can be bought or sold for use within that year. Facilities must hold credits equal to their actual emissions for the year. They can sell excess credits to firms that may not otherwise meet their limits. As a State Implementation Plan (SIP) program, RECLAIM is run by SCAQMD with oversight provided by the California Air Resources Board and EPA's Region 9.

In EPA's federal cap and trade programs, caps apply to the universe of affected facilities. Allowances are either allocated or auctioned, and can be traded among facilities and banked for future use. The first federal cap and trade program was proposed by President George H. W. Bush and mandated by Congress in the 1990 Clean Air Act Amendments. Subsequently, EPA by regulation established the NOx Budget Trading Program under Title I of the Clean Air Act.

EPA runs both programs at the federal level, with states providing assistance through the operating permit programs required by Title V of the Clean Air Act.

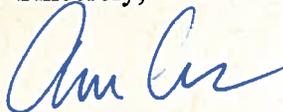
Your letter states that the "...[Sholtz] case arises from fraud in the sale of counterfeit pollution credits...". We would like to note that Ms. Sholtz represented herself as having pollution credits which she did not have and she forged documents between buyers and sellers. Since every RECLAIM trading credit is identified by vintage, compliance cycle, and zone, counterfeit credits could not have been substituted in the environmental program. In EPA's cap and trade programs, each allowance is identified by both vintage and a unique serial number, and anyone can verify online that the correct vintage and quantity of allowances are in the relevant account before any funds are exchanged. The job of the agencies responsible for the cap and trade programs is to make certain that, in the case of RECLAIM, a trading credit surrendered for compliance is equivalent to a pound of emissions, and in the case of the Acid Rain Program, a trading credit surrendered for compliance is equivalent to a ton of emissions, thus ensuring the environmental integrity of the programs.

EPA's experience has demonstrated the importance of adhering to several fundamental principles in the design and implementation of cap and trade programs: simplicity, transparency, accountability, and certainty. Stringent monitoring requirements, efficient electronic tracking systems for emissions and allowances, efficient allowance auctions, source-by-source compliance determinations, effective enforcement of monitoring and allowance holding requirements, and public availability of compliance information have allowed EPA's programs to achieve significant emissions reductions and very high levels of compliance by industry, while providing sources the flexibility to devise individual strategies to cost-effectively meet the program caps.

EPA understands the importance of ensuring that any greenhouse gas cap and trade program included in legislation be designed to operate with appropriate regulatory oversight and transparency, the hallmark of federal cap and trade programs since the 1990s. We welcome the opportunity to work with Congress in structuring a cap and trade program that Americans can trust will achieve its environmental objectives.

Thank you for the opportunity to answer your questions and respond to your concerns. Enclosed are responses to the specific questions in your letter. If you have any further questions, please contact Tom Dickerson in my office at (202) 564-3638.

Sincerely,



Arvin R. Ganesan
Deputy Associate Administrator

Enclosure

Question 1: Please describe EPA's regulatory oversight activities relating to the RECLAIM program since RECLAIM went into effect.

EPA approved the South Coast Air Quality Management District's (SCAQMD's) RECLAIM program as part of the California State Implementation Program (SIP) on November 8, 1996 (see 61 FR 57775). The SCAQMD's RECLAIM program is one of several emissions reduction strategies that are being implemented by the District in order to achieve attainment with California and Federal air quality standards. By approving the RECLAIM program into the California SIP, EPA Region 9 ensured that all of the program's requirements applicable to covered facilities are federally enforceable.

Region 9's oversight activities with respect to RECLAIM are based on the Clean Air Act framework created by Congress for attaining and maintaining national ambient air quality standards (NAAQS). That framework gives states a leading role in developing, implementing, and enforcing SIPs that contain control measures needed to attain and maintain the NAAQS. For RECLAIM, the SCAQMD has the primary role of implementing and enforcing the program. During the design of the RECLAIM program, Region 9 assisted the District in developing appropriate evaluation provisions that would monitor the overall effectiveness of the program. Under these provisions, the SCAQMD submits annual reports to EPA's Region 9 on key indicators of program effectiveness including credit costs, compliance issues, and technical issues. The Region reviews these reports and, based on the information supplied by the District or otherwise obtained by Region 9, investigates specific compliance-related matters.

In addition to the efforts described above, Region 9 also conducted an evaluation of the RECLAIM program and issued a report in November 2002 based on interviews with representatives of SCAQMD, EPA, industry and environmental groups. In the report Region 9 described the program and recommended potential improvements. The report is available at <http://www.epa.gov/region09/air/reclaim/index.html>.

Has EPA made any changes to its oversight activities of the RECLAIM program? If so, were any of these changes the result of the Sholtz case?

As mentioned above, EPA's role is to monitor SCAQMD's implementation of the area's approved state implementation plan and the area's progress toward attainment of the national ambient air quality standards. The Sholtz case has not altered that role.

Question 2: When and how did the EPA come to learn about the allegations against Ms. Sholtz of potential criminal misconduct?

EPA's Office of Criminal Enforcement, Forensics and Training (OCEFT) opened its criminal investigation of Anne Sholtz on August 1, 2002. The criminal enforcement office learned about this case from the SCAQMD, which, as noted above, has primary responsibility for implementing and enforcing the RECLAIM program.

Region 9's air enforcement resources are most often managed by industry sector. For this reason, the resources and time that Region 9 devotes to monitoring and detecting fraud in connection with the RECLAIM program is difficult to measure because the RECLAIM program encompasses several source categories or industry types. This results in focusing on both facilities which are subject to RECLAIM as well as those which are not subject to RECLAIM.

Question 5: Does EPA have sufficient authority and resources to monitor and deter fraudulent conduct in the RECLAIM program?

EPA's OCEFT agents have authority to investigate any alleged federal crime, including violations of the criminal code provisions most often used to combat fraud: 18 USC Sections 1001 (the false statement statute), 1341 (mail fraud) and 1343 (wire fraud). More specifically, EPA's authority to monitor and deter fraudulent conduct in the RECLAIM program is identical to that of any federally-approved SIP program. The Clean Air Act provides authority for inspection, entry, and information-gathering, which has proven effective in identifying areas of concern and also provides very substantial civil and criminal enforcement authority for pursuing and deterring violations. The resources devoted to enforcement of the Clean Air Act and SIP programs like RECLAIM have proved to be effective and sufficient.

Question 6: There was a three-year gap between Ms. Sholtz's guilty plea in 2005 and her sentencing in 2008. Why was there such a delay in the sentencing phase?

DOJ prosecuted the Sholtz case, and we therefore defer to DOJ to answer questions pertaining to sentencing in the case.

Question 7: Are there any other filed EPA criminal cases involving emissions trading programs, including the RECLAIM program?

Currently, there are no EPA criminal cases with filed charges involving emissions trading crimes.

Question 8: Does EPA agree with a statement reportedly made by an EPA air official in a June 25, 2004 article that there were similar cases of illegal activity that EPA was unable to investigate?

EPA's criminal enforcement program is unaware of any allegations of illegal activity similar to the Sholtz case, and we do not believe that there were similar criminal cases that EPA was unable to investigate.

Question 9: Are there mechanisms in place to ensure that individuals who have engaged in fraudulent conduct relating to the RECLAIM program are prevented from participating in the future in emissions trading markets?

One of the terms of Ms. Sholtz's probation is that for five years she not engage in any business that purchases, sells or trades in the RECLAIM program or other programs involving Emission

Reduction Credits under the jurisdiction of SCAQMD without the prior written approval of her Probation Officer. She must provide her Probation Officer with access to any and all business records to verify compliance with this provision. EPA expects that Ms. Sholtz's probation officer will consult with the Agency as well as the SCAQMD prior to granting Ms. Sholtz permission to resume participation in the RECLAIM or other ECR programs. Given the seriousness of Ms. Sholtz's misconduct, it is unlikely that EPA would support allowing her to resume emission trading.

Has Ms. Sholtz been prohibited from future trading involving the RECLAIM program and/or from any other emission trading programs established under EPA regulations?

Please see the response immediately above.

Does EPA keep a list of groups or individuals debarred from participating in emissions trading programs or bidding for government contracts? If not, why not?

The Agency, along with other Federal agencies, uses a database maintained by the General Services Administration to list parties who are excluded from participating in Federal procurement and assistance programs, which includes bidding on government contracts. This database, known as the Excluded Parties List System (EPLS) may be found at www.epls.gov.

EPA does not maintain a list of parties excluded from emission trading markets at this time. EPA has broad authority to exclude parties from federal programs when necessary to protect the integrity of the program. In the Acid Rain Program, EPA has by regulation reserved the right "to take any action necessary to protect the orderly and competitive functioning of the allowance system, including actions to prevent fraud and misrepresentations." 40 CFR 72.4(b).

Is the list available to the public? If not, why not?

You may access the GSA list of parties excluded from federal procurement and assistance programs (as well as other programs) at www.epls.gov. To our knowledge the Federal government does not currently maintain a list parties who are excluded from emission trading markets.

Under what circumstances does the EPA begin the debarment process?

EPA opens debarment matters in cases when information indicating a party poses a risk to the integrity of Federal procurement, assistance or environmental laboratory programs comes to the attention of the Agency suspension and debarment program. Cases typically involve fraud, waste, abuse or serious performance failures on EPA procurement contracts or assistance agreements or laboratory analyses that EPA would rely on for a regulatory decision. In addition, the Agency takes actions in response to environmental crimes committed by an entity that may enter into a Federal procurement or assistance transaction. EPA has a well-established suspension and disbarment program. For example, since the beginning of fiscal year 2005, EPA has suspended 156 parties and debarred 257.

Has Ms. Sholtz been debarred from participating in any emission trading programs or bidding for any Government contracts?

As discussed above, Ms. Sholtz is currently precluded from participating in the RECLAIM and other ECR programs under the jurisdiction of SCAQMD by the terms of her probation. The EPA opened a debarment case involving Ms. Sholtz in November 2008, and is in the process of reviewing the risk she may pose to the integrity of Federal procurement and assistance programs

Question 10: Why were so many of the documents (including the sentencing hearing transcript) in the criminal proceeding involving Ms. Sholtz placed under seal? Does the government plan to request that the documents be unsealed? If not, how can these documents be unsealed?

Questions pertaining to the prosecution and sentencing of the case should be addressed to DOJ.

Question 11: EPA's public website provides press releases about the sentencing of defendants in EPA criminal cases. However, it does not appear that EPA has posted any information on its public website about the sentence in the Sholtz case. Why?

Most environmental crimes are prosecuted by the Offices of the United States Attorneys, so the majority of press releases regarding criminal cases are issued by them. EPA's criminal enforcement program will often post the U.S. Attorney press releases on its website. In this case, the U.S. Attorney's Office, Central District of California, did not issue a press release on Anne Sholtz's sentencing.