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DOE efficiency enforcement

Stuff happens: Be ready

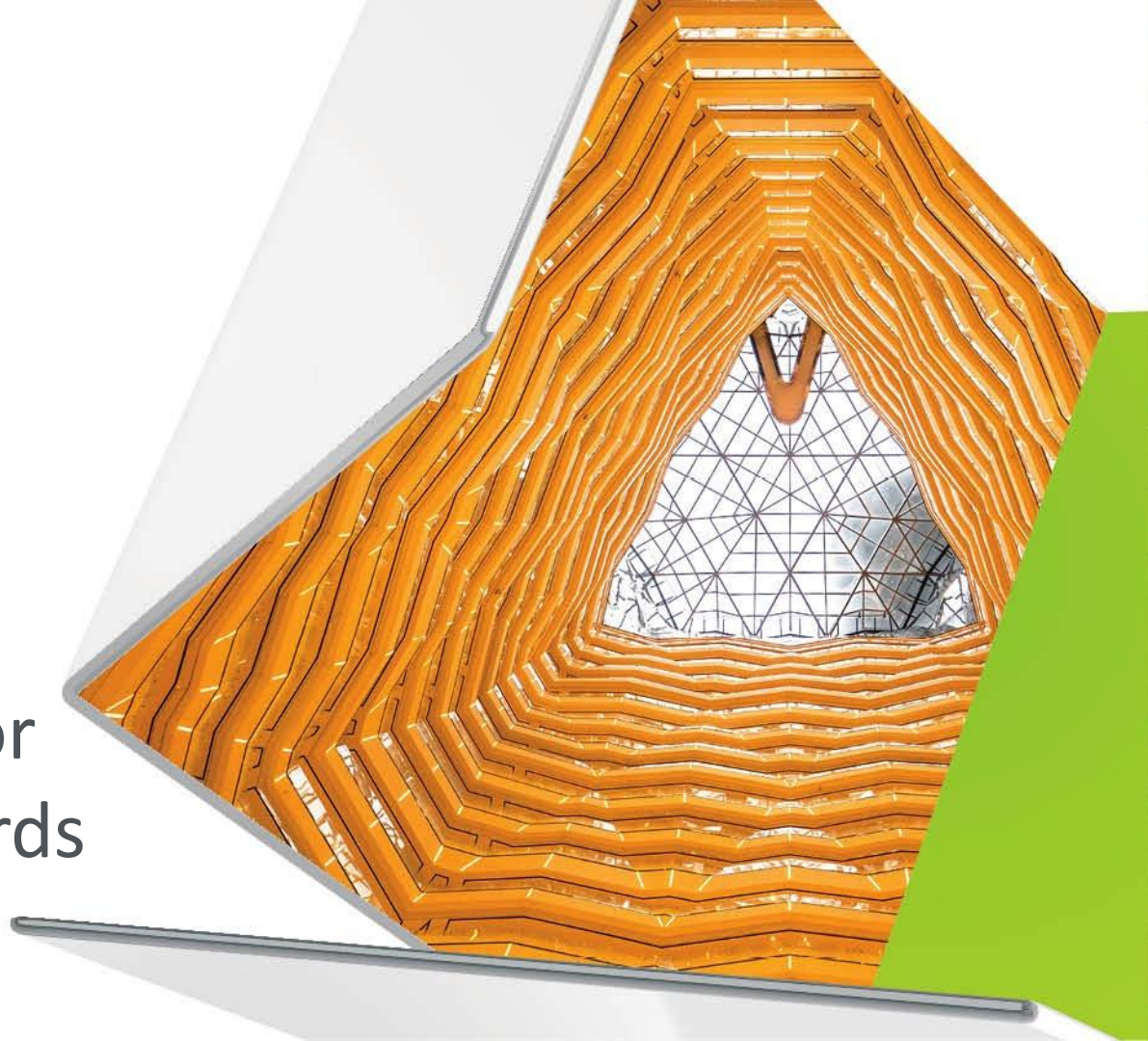
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Main Messages for Today

- A DOE efficiency enforcement case can be very expensive
 - DOE imposes among the largest penalties of any federal regulatory program
 - For mass-produced products, the per unit assessments can really add up
- There are things you can do in advance to protect yourself
- There are also strategies for responding once DOE brings a case
- In short, *stuff happens; be ready to respond*

The big picture for efficiency standards



What are the rules trying to accomplish?

- Goals of the efficiency rules:
 - “Maximum improvement in efficiency that is *technologically feasible* and *economically justified*” for specific “covered products”
 - “*Significant conservation of energy*”
- More specifically:
 - Reduce pollution
 - Save money for energy users
 - Encourage innovation
- Every rule must pass a cost/benefit test
 - Cost to manufacturer/benefit to consumer
 - Target payback period: three years or less

Program Is Now Mature

- Original basis for the rules: Energy Policy and Conservation Act of 1975
- The law has been amended several times, most recently by the Energy Independence and Security Act (EISA) of 2007
 - EISA requires the DOE to review its efficiency standards for each covered product at least once every six years
- Increased attention to enforcement since 2010
- Sharp increase in penalties starting in 2015
 - Penalties increase annually with inflation

Certification: The backbone of DOE's enforcement program



Certification

- DOE: “The Department’s certification requirements are the foundation of DOE’s compliance and enforcement framework.”
- All basic models must be certified *prior to distribution and annually thereafter*
- The certification report includes a compliance statement **signed by a company official** that guarantees the compliance of the covered product
- Other certifications required:
 - **Discontinuance** - Do not discontinue a model number until all units are sold
 - **Certification to a new standard** - Whenever DOE updates efficiency standards
 - **Recertification** - Recertification is required if a model is re-rated to claim new efficiency or if testing no longer supports the certified rating

Certification

- Certification reports may be submitted by a **manufacturer or importer**
- DOE does not require annual re-testing of efficiency, but . . .
 - The burden of continued accuracy is on manufacturers and importers
 - When you change a basic model designation, testing is required
 - This can have significant **enforcement benefits**
- Certification testing can be performed and results submitted by third party tester, but . . .
 - The manufacturer or importer is responsible for the accuracy of the certification

Certification by Basic Model

- Manufacturers certify by basic model numbers
 - All units within a basic model must have “essentially identical” energy use characteristics
 - DOE recommends certifying as basic models only units that have “superficial differences,” such as product finishes
- Compliance risk: if some units in a basic model fail under the enforcement testing protocol, DOE will deem **all units in the basic model non-compliant**
 - Enforcement actions often cover multiple basic models
 - For some products, larger groupings are permitted for certification
 - This reduces testing burdens, but **increases penalty risks**

Certification Testing

- Each product has its own sampling procedures for certification testing
 - Test and certify by basic model
 - Designed to avoid testing every individual unit
- To certify compliance, a manufacturer must test
 - A random selection of units
 - A statistically significant sample of units taken from a production line
- Note: sampling plans for **certification testing** and **enforcement testing** are different

Recordkeeping Requirements

- *Maintain records of all testing* conducted to satisfy regulations
 - If you do extra testing, save those records
- Required test records must be available for DOE review
- Retain records for two years *after model discontinuance*



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Violations and
penalties – Where
the rubber
meets the road



Violations Come in Many Varieties

- Four broad classes of violation of DOE rules
 - Violate **efficiency standard**, which can include a **design standard** – by the manufacturer, importer or private labeler
 - Violate **certification/testing** requirements
 - Fail to cooperate in an **enforcement investigation**
 - Fail to label as required
- Almost all enforcement cases involve:
 - failure to certify, or
 - violation of an efficiency standard (much greater penalty exposure)
- Customers are not subject to compliance obligations; assemblers may be
- Knowing false statements on a certification report can give rise to criminal liability
 - Not aware of any cases, but it can affect employee behavior

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Certification Violations



What constitutes a certification violation?

- Failure to file or **failure to correctly certify**
 - New product certifications
 - Annual certifications
 - Certification to new efficiency standard
 - Discontinuance certifications – when you stop selling a product
 - Recertification for product changes that affect efficiency
- **Failure to properly test** products prior to certifying them
- A certification violation can occur **even if the product complies** with the applicable efficiency standard

DOE routinely pursues certification violations

- Many are easy to identify: “Is a product number in our database?”
- Penalties for certification violations can be \$468 per unit,* but
 - DOE policy statement says certification penalties are usually limited to 25% of the maximum, but most cases don’t fit that formula
 - **Recent practice: flat \$8,000** if settled within 30 days for first time violations
 - \$16,000 if settled within 60 days
 - \$24,000 if there is also a testing violation
 - Higher penalties possible for failure to respond and for repeat violations
 - DOE will generally not assess **separate** penalties for certification and efficiency violations affecting the same basic model

*2020 level; adjusted annually for inflation.

Recent Cases

- Three Square Market, Inc., failed to certify nine models of commercial refrigeration equipment
 - In 2019, settled within 30 days for \$8,000
- Leer, Inc. manufactures and distributes walk-in cooler and freezer panels
 - In 2018, agreed to pay \$24,000 for failing to test and certify a walk-in freezer panel model
- Legacy Company manufactures and distributes commercial refrigeration equipment
 - In 2017, agreed to pay \$16,000 failing to certify two models of commercial refrigeration equipment
 - Settled more than 30 days after the Notice of Non-Compliance

Not every case fits the template

- YMGI: \$31,400 violation (\$157/unit sold)
 - Sold 200 air conditioners in U.S. without testing or certification
 - No finding that YMGI failed to meet the efficiency standard
- PQL Lighting imports and distributes lighting
 - In 2013, agreed to pay \$8,000 and to certify in within 60 days
 - DOE brought a further enforcement action in 2015. Imposed a \$12,500 penalty and ordered that all covered products be certified
 - Given the multiple violations, this was notably lenient treatment

Efficiency standards
violations:
Where the serious
risk lies

What constitutes an efficiency standards violation?

- Violation of efficiency standard occurs if there is a “knowing distribution in commerce” of a product that does not meet the efficiency standard
- “Knowing” includes:
 - Actual knowledge
 - Presumed knowledge if obtainable by “the exercise of due care”
- “Due care” is *not a high standard*
 - DOE assumes that, if a company pays reasonable attention, it will know whether it is in compliance
 - DOE presumes knowledge

How does DOE find violations?

- **DOE testing**
 - DOE has historically tested multiple samples before finding a violation
 - DOE proposal: also rely on third party tests or a single test if noncompliance gap is large (at least 25%)
 - DOE is proposing variations for certain products
- Some industries participate in voluntary compliance monitoring
 - Results are reported to DOE
- **Competitors** see violations and report them
 - DOE has an anonymous hotline for reporting
- **Employees** report violations or ask troubling questions
- Company **self-reports**



What happens if DOE learns of a standards violation?

- DOE requires immediate cessation of distribution of non-compliant models and cancellation of model numbers
 - DOE is proposing to specify a separate violation for distribution after finding of non-compliance
- DOE issues a Notice of Non-Compliance Determination
 - DOE is proposing to issue letter of intent and allow petition for reexamination before issuing Notice of Noncompliance Determination
- DOE and company negotiate a settlement in most cases
 - The penalty discount for settling (typically 50percent or more) is hard to resist unless there is a strong defense, which is unusual
- *DOE does not want to litigate these cases*
 - DOE is planning to build out administrative law judge review process

Consequences of a Violation

- Penalties for violation can be **\$468 for each non-compliant unit** of a basic model*
 - Failure of some units under the enforcement testing protocol can result in DOE assessing penalties for the entire basic model – a big multiplier effect
- DOE requires **notification of customers** who received or may have received non-compliant products
 - DOE is proposing to eliminate the customer notification requirement
 - ***Recalls not required***
 - **Non-compliant products can be exported**
- If a certification or testing violation occurs along with an efficiency standards violation, DOE typically only pursues the efficiency violation

* 2020 level; adjusted annually for inflation

How does DOE determine the penalty amount?

- Did the company self-report?
- What was the degree of non-compliance?
- How many models were affected?
- How long did the violation continue?
- What corrective actions did the company take on its own?
- What is the nature of the product, e.g., light bulb vs. industrial motors?
- Does the company have a history of violations?
- Is the company financially distressed?
- Has the company **failed to cooperate**?

Recent DOE standards enforcement cases and results

DOE Penalty Approach for Standards Violations

- Since 2015, efficiency enforcement violations have been among the **most costly federal regulatory violations**
 - DOE knows this
 - It is a conscious choice, reflecting its relatively modest enforcement capabilities
- Settlements are typically for ~50 percent of the maximum
 - For mass produced products, this can be very expensive
- Self-reported violations are the exception

Quantifying the non-compliance risk

- Whirlpool distributed 26,649 units of a non-compliant refrigerator freezer basic model
- DOE discovered it through compliance testing
- Whirlpool had no knowledge of the non-compliance and cooperated in the investigation
- The model fell short of the standard by 8% -- a significant amount
- DOE assessed **\$200/unit** for a total penalty of **\$5.3 million**

Other Penalties

- Beverage Air Corporation (2019) distributed 28 non-compliant commercial freezers; paid \$7252 (**\$259/unit**)
- Guangdong Chigo Air-Conditioning (2107) distributed 3,677 non-compliant split-system central air conditioner; paid \$735,400 (**\$200/unit**)
- Big Beam Emergency Systems (2016) paid \$6,500 for 38 units or **\$172/unit**
- Friedrich Air Conditioning Co. (2015) paid almost \$1.5 million on 8,000 non-compliant units -- **\$187/unit**; **payments stretched out** over two years
- LG Electronics (2014) distributed 7,000 + non-compliant room air conditioners; paid > \$1.4 million -- **\$200/unit**
- **Compare** GD Midea Air Conditioning (2014) paid \$416,800 for almost 15,000 non-compliant units that were on average 4% below the required efficiency (**~\$28/unit**)
 - Affiliates had other violations during the same period; **would not be this low today**
- You should assume the starting point is **\$200/unit to settle**

The value of self-reporting a violation?

- Very few self-reports are made, but . . .
- Others can report your violations
- DOE treats **self-reporting much more leniently**
 - A company that finds a violation of its own and wishes to self-report should not delay; a competitor or anonymous source may get there first



Self-reporting examples

LG Electronics

- Sold 14,900 non-complaint dehumidifiers
- Maximum penalty: >\$6.5 million
- Proposed penalty: ~ \$6.5 million
- Final penalty: \$56,600
- Most units were retrieved after import but before sale to customers
 - \$3.80 per unit sold

Cooper Power Systems

- Sold 229 non-complaint distribution transformers
- Maximum penalty: >\$5 million
- Proposed penalty: ~ \$1.2 million
- Final penalty: \$17,175
- Modest total penalty likely impacted discussion of any per unit penalty reductions
 - \$75 per unit sold

More self-reporting examples

ABB Inc.

- Sold 5,738 non-compliant
- Maximum penalty: >\$2.4 million
- Proposed penalty: \$2.4 million
- Final penalty: \$86,300
 - \$15 per unit sold

Lennox International

- Sold 3,137 non-compliant AC units
- Maximum penalty: \$627,400
- Proposed penalty: \$627,400
- Final penalty: \$51,960
 - \$16/unit

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Compliance and enforcement strategies



First Line of Defense: Find and Fix

- Every company will have a different procedure for raising compliance questions, but here, the golden rule is **when in doubt, ask**
 - “I didn’t know it was a violation” is not a defense
 - Remember: knowledge is presumed if obtainable in the exercise of due care
 - “I didn’t want to slow down production; the customer was waiting” is not a defense
 - The cost of being directed to stop shipments and inform customers of the violation is much higher



If you think you have a problem . . .

- **Make sure you have the right answer** before you make a record of your conclusion
 - You may not be right, and your written record (including emails and texts) may be used as evidence against the company
- Examine DOE's rulemaking record for guidance
- When there are gray areas, you can ask DOE, but be careful
 - These are the same people who **initiate enforcement actions**
 - You may not get a conclusive response unless DOE publishes a response to a FAQ
 - Far safer to ask an internal or outside expert
- If you cannot comply, consider a request for a **temporary exception** – before new standard takes effect
- Waivers of test procedures are also available, **provided the product meets efficiency standards**

Enforcement Strategies

- For **certification violations**, usually not much to argue about
 - To keep the penalty low, **settle quickly**
 - You also need to **certify quickly**, which will likely require testing
- For **efficiency standards violations**, there is some **room to negotiate**
 - If you discover a significant non-compliance:
 - Take prompt measures to halt distribution; penalties are per unit shipped
 - Consider a self-report to DOE – you must be first in the door to get credit for self-reporting
 - Marshal your facts; understand what went wrong; understand scope of exposure
 - How many basic models; how many units; how far over the efficiency standard?

Potential Strategies for Defense

- Look for enforcement **testing errors** – they do happen
 - Ask for the full testing reports, including pictures
 - Is the Lab DOE chose following test procedure protocol to the letter?
- Consider age and **condition issues** of the units DOE tested
 - Are they representative of what you shipped in commerce?
 - DOE is proposing to evaluate condition before testing
- Produce evidence of **internal compliance testing** – must be more than the minimum testing required
- Consider whether the **number of noncompliant units** is overstated
 - Did some units go to Canada or Mexico? They should be left out.
 - Are some units sitting in a warehouse, not distributed to customers?

Enforcement Discretion

- By statute, DOE can never impose a lower efficiency standard than one it has previously adopted: the “anti-backsliding” rule, but . . .
 - Sometimes DOE makes a mistake in a rulemaking that no one catches until it is too late
 - Sometimes a scenario arises that DOE did not consider in its rulemaking, producing unintended consequences.
- DOE can issue a statement indicating that it will exercise its discretion to not bring enforcement actions that would result in an unintended result
- If the circumstances warrant, consider making a request for a **statement of enforcement discretion**

Risk Reduction Strategies

- *Change basic model numbers frequently* to limit the potential number of non-compliant units
- Do lots of **testing** – save the records
- With third-party manufacturers
 - Use **contract terms to shift liability** for any failure to meet DOE standards
 - Consider independent testing in the country of origin
- Keep open lines of **communication with the employees** who must certify compliance
 - Solving problems internally is easier and cheaper
 - Employees can be the source of information that leads to enforcement cases
- Get smart upfront: participate in standards-setting rulemakings

A graphic on the left side of the slide. It features a white, angular, 3D-style frame that is open on the right side. Inside the frame, a set of keys is hanging from a metal ring attached to a door handle on a wooden door. The background behind the keys is a blurred green, suggesting foliage. A solid green triangle is positioned at the bottom left corner of the frame.

Key takeaways

What should you remember?


- The regulations are complex
- Mistakes *will happen*, and they can be *costly*
- DOE has limited resources to look for violations, but others in the industry may report your noncompliance
- DOE wants its compliance orders to send a message
- *Self-reporting* has generally been rewarded with low penalties
- There is some limited *room to negotiate* penalties and other terms
- Sometimes DOE is wrong
- DOE does not want to litigate

What's coming?

Uncertainty

- Change in head of enforcement
 - Will it lead to more aggressive or less aggressive enforcement
 - Will it lead to a lower penalty structure?
- Potential change in Administration
 - Last change led to a delay in bringing new cases, but no change in penalty levels



An aerial photograph of a crowded beach. The top left shows the ocean with waves washing onto the shore. The rest of the image is filled with a dense array of colorful beach umbrellas in various colors including green, yellow, red, blue, orange, and pink. Many of the umbrellas have geometric patterns. Interspersed among the umbrellas are numerous lounge chairs, some striped and some solid-colored. A few people can be seen walking on the sand. A large green semi-transparent box is overlaid on the top right portion of the image, containing white text.

Thank you for your attention
I look forward to your questions

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