

THE ENVIRONMENT AND THE FEDERAL SECURITIES LAWS†

RAYMOND L. FRIEDLOB*

JAMES W. SANDERSON**

Congress embarked on a significant course in 1969 with the enactment of the National Environmental Policy Act (NEPA).¹ The Act was an attempt to impress upon federal departments and agencies and the country an awareness of and a concern for the preservation and enhancement of the environment. It was, more importantly, an effort to make an impression upon and guide the agency decision-making process. In declaring the purpose of this legislation, Congress promulgated a national policy to "encourage productive and enjoyable harmony between man and his environment . . ."² The Act created the Council on Environmental Quality within the Executive Office of the President and charged it to carry out the purposes of the Act. Section 102 establishes new mandates with which all federal agencies must now comply, and contains perhaps the most well-known requirement, that of directing the preparation of an environmental impact statement (EIS) by federal agencies on "major federal actions significantly affecting the quality of the human environment . . ."³

The subject of this article is the environment and the federal securities laws, more particularly, Release No. 5386,⁴ which contains the Securities and Exchange Commission's (SEC's) environmental reporting and disclosure policies prompted by section 103 of NEPA. Section 103 requires federal agencies to review their current regulations and procedures with a view to amending them in order to respond to this new mandate.⁵ The SEC's response to NEPA

† The views expressed herein are those of the authors. They do not represent the views of the Environmental Protection Agency.

* A.B., University of Colorado, 1966; J.D., University of Denver, 1969; LL.M. (Taxation), New York University, 1970; Partner, Brenman, Sobol & Baum, Denver, Colorado; Member, Colorado bar.

** A.B., University of Nebraska, 1966; J.D., University of Denver, 1969; postgraduate work, taxation, Georgetown University, 1971-72; Assistant Regional Counsel for the Environmental Protection Agency; Member, Colorado bar.

¹ 42 U.S.C. §§ 4321-47 (1970).

² 42 U.S.C. § 4321 (1970).

³ 42 U.S.C. § 4332(2)(C) (1970).

⁴ SEC Securities Act Release No. 5386 (April 20, 1973), reprinted in [1973 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 79,342.

⁵ See 42 U.S.C. § 4333 (1970), which provides:

All agencies of the Federal Government shall review their present statutory authority, administrative regulations, and current policies and procedures for the purpose of determining whether there are any deficiencies or inconsistencies therein

involves insisting upon regular reporting regarding the business cost effects of compliance with environmental laws, including an estimation of cost effects based on compliance with current and proposed laws, and reporting of judicial and administrative proceedings.

An understanding of the scheme of environmental regulation is a necessary precedent to an understanding of the interaction between the federal securities laws and major environmental laws. While the following description of environmental regulation may appear elementary to those seasoned in environmental law practice, it is the authors' opinion that many in securities practice can benefit from exposure to the major pieces of environmental legislation. Following this description of the framework of the environmental laws, the SEC's reaction to the NEPA mandate will be analyzed. Since disclosure of administrative and judicial proceedings under the environmental laws is now required, the article will proceed to a description of the nature of such proceedings. There will then be an examination of major areas of environmental disclosure in the context of specific industry groupings. Finally, the article will briefly explore the impact of the energy crisis in the environmental/securities area.

I. THE FRAMEWORK OF ENVIRONMENTAL REGULATION

The field of environmental regulation is an ever-expanding one. The Environmental Protection Agency (EPA) was created on December 2, 1970,⁶ from parts of fifteen other federal agencies. It became an independent regulatory agency whose sole mission was the protection and enhancement of the environment. In addition to NEPA, it administers six basic regulatory statutes, all of which have been enacted or expanded since 1970.⁷ Promulgation of regulations, enforcement actions and litigation are only now commencing in many of these areas. To provide the reader with guidance in determining proper disclosures with respect to securities law compliance, it may be helpful to provide a brief summary of the basic approaches taken by the various statutes.

which prohibit full compliance with the purposes and provisions of this chapter and shall propose to the President not later than July 1, 1971, such measures as may be necessary to bring their authority and policies into conformity with the intent, purposes, and procedures set forth in this chapter.

⁶ Reorganization Plan 3 of 1970 (effective Dec. 2, 1970), 35 Fed. Reg. 15,623 (1970). See 40 C.F.R. §§ 1.1 et seq. (1973) for statement of organization and general information.

⁷ Clean Air Act of 1970, 42 U.S.C. §§ 1857 et seq. (1970); Federal Water Pollution Control Act Amendments of 1972, 33 U.S.C. §§ 1251 et seq. (Supp. II 1972); Noise Control Act of 1972, 42 U.S.C. §§ 4901 et seq. (Supp. II 1972); Federal Environmental Pesticide Control Act, 7 U.S.C. §§ 135 et seq. (Supp. II 1972); Solid Waste Disposal Act, 42 U.S.C. §§ 3251 et seq. (1970); Marine Protection, Research, and Sanctuaries Act of 1972, 33 U.S.C. §§ 1401 et seq. (Supp. II 1972).

NEPA has been mentioned in the opening section of this article. The private sector, however, is most often affected by NEPA through the delay caused by the thorough compliance with the statute which requires complete study of: the environmental impact; adverse environmental effects and alternatives to the proposed action; the relationship between long and short-term uses; and the irreversible commitments of resources caused by the project.⁸ The impact of NEPA often develops when a private businessman, contractor or developer is dependent upon the commencement of a federal project. For example, a highway contractor, who is awaiting authorization to proceed with construction, may find a delay caused by litigation as to the sufficiency of such an environmental impact statement relative to the placement and/or scope of the highway project.

The Environmental Impact Statement (EIS) procedures dictated by NEPA are not unlike the federal securities law disclosure concepts in that both require total disclosure of all pertinent information to aid in the decision-making process. A rapidly developing facet of the EIS process has recently included a thorough examination of the so-called secondary impacts of a project, such as stimulated growth and congestion. This factor is exemplified in the environmental review conducted by the National Park Service relative to a proposed extension of the airport runway at Jackson Hole, Wyoming. A lengthened runway would generate regular commercial jet service, increased aircraft noise, more tourists, stimulate the vacation home industry, lead to increased congestion and contribute to long-term deterioration of the quality of life in the surrounding area. All are secondary effects of any airport improvement.⁹

Key elements of the Federal Water Pollution Control Act Amendments of 1972¹⁰ include new standards for pollution abatement, higher federal funding for construction of municipal treatment facilities, expanded pollution-control planning, a new permit system for dischargers into the nation's waters, provision for public participation and citizen lawsuits, and new enforcement procedures accompanied by stiff penalties for non-compliance.

The legislation abandoned the old concept of sole reliance upon water-use classifications and introduced a set of effluent standards and mandatory dates for achieving such standards. The first phase

⁸ See 42 U.S.C. § 4332(2)(C) (1970).

⁹ See Department of Interior, Draft Environmental Statement No. 73-46, Actions Under Consideration Jackson Hole Airport, Grand Teton National Park, Wyo. (July 25, 1973), prepared by Grand Teton National Park, Midwestern Region, National Park Service, Department of Interior.

¹⁰ 33 U.S.C. §§ 1251 et seq. (Supp. II 1972).

of the water cleanup has the target date of July 1, 1977. By that date, every industrial plant must install "the best practicable control technology currently available"¹¹ The EPA has regulations in effect under the Marine Protection, Research, and Sanctuaries Act of 1972 which control ocean dumping¹² and is developing regulations to control toxic wastes, oil and other hazardous materials. New facilities will be required to install the "best available demonstrated control technology" as defined on an industry-by-industry basis.¹³ The second phase of purifying the nation's waters will require all discharging industries to install, by 1983, the "best available technology"¹⁴ to treat their wastes. Further, the law sets as a goal, though not as a requirement, the complete elimination of harmful discharges by 1985.¹⁵

The regulatory framework for the water area centers on a permit system which requires that industry must obtain a permit for each facility in order to discharge into the nation's waters.¹⁶ The permit will specify abatement programs with deadlines for completion of each phase of the program; the conditions of the permit will be available to the public. Additionally, industry must file regular reports with respect to discharges.¹⁷ The broad rights of citizen lawsuits directed against dischargers violating the abatement requirement¹⁸ will undoubtedly assist the EPA in its enforcement duties. Violators are subject to civil penalties of up to \$10,000 a day, and willful or negligent violators are subject to criminal fines of up to \$25,000 a day, plus one year imprisonment.¹⁹ Permits should all be issued by December 31, 1974. Therefore, industries are only now learning the cost of their share of the cleanup.

The Clean Air Act Amendments of 1970²⁰ essentially contain the first substantive attempt to improve the quality of the nation's air. Ambient air quality standards²¹ for major pollutants were established at (1) levels to protect health (the primary standard), and (2)

¹¹ 33 U.S.C. § 1311(b)(1)(A)(i) (Supp. II 1972).

¹² 40 C.F.R. §§ 220.1 et seq. (1973). The Act is codified at 33 U.S.C. §§ 1401 et seq. (Supp. II 1972).

¹³ 33 U.S.C. § 1316 (Supp. II 1972). See Arnold, *Effluent Limitations and NPDES: Federal and State Implementation of the Federal Water Pollution Control Act Amendments of 1972*, 15 B.C. Ind. & Com. L. Rev. 767, 771 (1974), where the author notes that the EPA has often failed to develop industry-by-industry guidelines in this area, but rather has issued permits on a case-by-case basis.

¹⁴ 33 U.S.C. § 1311(b)(2)(A)(i) (Supp. II 1972).

¹⁵ 33 U.S.C. § 1251(a)(1) (Supp. II 1972).

¹⁶ 33 U.S.C. § 1342 (Supp. II 1972). See generally Arnold, *supra* note 13.

¹⁷ 33 U.S.C. § 1342(b)(2)(B) (Supp. II 1972).

¹⁸ 33 U.S.C. § 1365 (Supp. II 1972).

¹⁹ 33 U.S.C. §§ 1319(c), (d) (Supp. II 1972).

²⁰ 42 U.S.C. §§ 1857 et seq. (1970).

²¹ 42 U.S.C. § 1857c-4 (1970).

levels to protect the public welfare (the secondary standard).²² Through the mechanism of a State Implementation Plan (SIP),²³ a program is established to lower the level of pollutants in order to reach the health standard by May 31, 1975. Secondary standards are to be met within a "reasonable time," which is defined for each pollutant.²⁴ Up to two additional years may be allowed to achieve the primary standard where strict statutory prerequisites are met.²⁵ Thus, in currently polluted areas, most stationary sources of pollutants will be required to abate their emissions by mid-1975.

Section 111 of the Clean Air Act imposes strict emission limitation requirements on new air pollution sources. In essence, new sources are required to remove air pollutants from their discharges by installing adequately demonstrated technology, as defined by categories in the standards of performance established by regulation.²⁶ Section 112 of the Clean Air Act provides for national emission standards for hazardous air pollutants. Sources of hazardous air pollutants²⁷ are to come into strict compliance with the provisions of this section and are monitored by the EPA during the pre-construction period.

In order to control automobile-related pollutants,²⁸ the Act places standards upon new car manufacturers²⁹ and authorizes "land-use and transportation controls."³⁰ The states and the EPA have developed transportation control plans, pursuant to this mandate, in 38 metropolitan areas. These plans consist of installing pollution control devices on existing automobiles and strategies designed to limit the number of vehicle miles of travel in the region. In

²² Promulgated standards are set forth at 40 C.F.R. §§ 50.1 et seq. (1973). The secondary standard is to prevent other types of harmful effects, such as to animals, plants and property.

²³ See 42 U.S.C. § 1857c-5 (1970); 40 C.F.R. §§ 52.01 et seq. (1973).

²⁴ 42 U.S.C. § 1857c-5 (1970).

²⁵ 42 U.S.C. § 1857c-5(e) (1970).

²⁶ 42 U.S.C. § 1857c-6 (1970); 40 C.F.R. §§ 60.1 et seq. (1973). Five categories have been promulgated: fossil-fired steam generators (primarily power plants), incinerators, portland cement plants, nitric acid plants and sulphuric acid plants. In addition, finalized standards of performance were recently announced for seven additional categories: petroleum liquid storage facilities, secondary lead smelters, secondary brass and bronze ingot plants, iron and steel smelters, sewage treatment plants, asphalt concrete plants and petroleum refineries. Proposed Regs., 38 Fed. Reg. 15,406 (1973). See also 39 Fed. Reg.—(March 1974) for promulgation.

²⁷ 42 U.S.C. 1857c-7 (1970); 40 C.F.R. §§ 61.01 et seq. (1973). Four categories have been promulgated: asbestos, beryllium, beryllium rocket motor firing, and mercury.

²⁸ Carbon monoxide, photochemical oxidants, hydrocarbons and nitrogen dioxide. 40 C.F.R. §§ 50.8-.11 (1973).

²⁹ 42 U.S.C. § 1857f-1 (1970).

³⁰ 42 U.S.C. § 1857c-5(a)(2)(B) (1970). For extensive commentary on the transportation controls provisions, see Bracken, *Transportation Controls Under the Clean Air Act: A Legal Analysis*, 15 B.C. Ind. & Com. L. Rev. 749 (1974); Comment, *The Clean Air Amendments of 1970: Better Automotive Ideas from Congress*, 12 B.C. Ind. & Com. L. Rev. 571 (1971).

addition, the EPA has proposed regulations to control indirect sources of air pollution.³¹ These indirect source regulations and vehicle miles of travel reduction measures are forms of land-use control, which can limit the size or prevent construction of facilities that generate traffic.³² In the future, certain large facilities may require modification or, in severely polluted areas, even be prohibited. This regulation is directed to those facilities which, because of their nature, will generate a certain amount of traffic, the pollution from which will, as a result, prevent the attainment or maintenance of an air quality standard.

The U.S. District Court for the District of Columbia in *Sierra Club v. Ruckelshaus*³³ has ordered the EPA to develop regulations to prevent the significant deterioration of air quality in those areas which now do not exceed either the "primary or secondary" standards. These regulations³⁴ should be promulgated in 1974 and potentially could limit or channel growth in those areas which currently have clean air.³⁵

Violators of the Clean Air Act are subject to civil action, including injunctive measures and criminal penalties of not more than \$25,000 per day or more than one year imprisonment. Section 304 of the Clean Air Act provides for citizen lawsuits.³⁶

The Noise Control Act of 1972³⁷ brought the federal government into the field of limiting noise that affects public health or welfare. Noise emission standards for manufacturers of certain categories of equipment are to be developed.³⁸

The Solid Waste Disposal Act, as amended,³⁹ displays the federal concern for this problem. To date, however, the problem is primarily one of local concern with the federal government supplying support for research, resource recovery and recycling. Federal grants are available for planning and for construction of new facilities.

³¹ 38 Fed. Reg. 29,893 (1973). See also Proposed Indirect Source Regulation: A Partial Integration of Land Use and Air Quality Planning, 3 E.L.R. 10,178 (1973). It is anticipated at the time of writing that promulgation will occur in February 1974. Congress may modify the statute somewhat in this area. See 119 Cong. Rec. S23,845 (daily ed. Dec. 21, 1973).

³² Such facilities would include, for example, highways and roads, parking facilities, shopping centers, recreational centers and amusement parks, sports stadiums and airports.

³³ 344 F. Supp. 253 (D.D.C.), aff'd, 4 E.R.C. [Env. Rptr. Cases] 1815 (D.C. Cir. 1972), aff'd by an equally divided court sub nom. *Fri v. Sierra Club*, 412 U.S. 541 (1973).

³⁴ Proposed EPA Regs., 38 Fed. Reg. 18,986 (1973).

³⁵ Congressional committees have announced that hearings will be conducted during 1974 to review possible Clean Air Act modifications. Clarification of this issue may result.

³⁶ 42 U.S.C. §§ 1857c-8, 1857h-2 (1970).

³⁷ 42 U.S.C. §§ 4901 et seq. (Supp. II 1972).

³⁸ 42 U.S.C. § 4905 (Supp. II 1972).

³⁹ 42 U.S.C. §§ 3251 et seq. (1970).

The Federal Environmental Pesticide Control Act of 1972⁴⁰ requires registration of pesticides⁴¹ and prohibits the use of any registered pesticide in a manner inconsistent with the labeled instructions.⁴² Beginning in October, 1974, pesticides will be classified for "general" or "restricted" use.⁴³ Those with a "restricted" classification may be used only by or under the supervision of certified applicators or under such other conditions as the EPA may prescribe. The EPA is empowered to stop the sale of a pesticide for violations of the registration, or if the registration of the pesticide terminates.⁴⁴ The EPA is also empowered to seize the product for non-registration or mislabeling.⁴⁵ Civil penalties for violations range from \$1,000 to \$5,000.⁴⁶ Willful violations are subject to not more than a \$25,000 fine and up to one year imprisonment.⁴⁷

This article does not pretend to be exhaustive of the subject of state environmental regulations. However, most states have corresponding statutes in the area of air and water pollution. Many states have some type of NEPA review embodied in state law.⁴⁸ The California, Montana, Washington and Puerto Rico statutes even apply to certain private actions.⁴⁹ In addition, states are moving rapidly into the area of land-use control with statutes designed to protect and preserve coastlines and natural formations. It is probable that Congress will enact a federal land-use act and that federal monies will then be available to assist development of state land-use regulatory programs which embrace certain broad federal guidelines. In fact, some state environmental laws are quite restrictive and far harsher than federal laws, both in fact and practice.⁵⁰

⁴⁰ 7 U.S.C. §§ 135 et seq. (Supp. II 1972).

⁴¹ 7 U.S.C. § 136a (Supp. II 1972); 40 C.F.R. § 162.10 (1973).

⁴² 7 U.S.C. § 136j(a)(2)(G) (Supp. II 1972).

⁴³ 7 U.S.C. § 136 (Supp. II 1972). See especially Note following 7 U.S.C.A. § 136 (Supp. 1973).

⁴⁴ 7 U.S.C. § 136k(a) (Supp. II 1972).

⁴⁵ 7 U.S.C. § 136k(b) (Supp. II 1972).

⁴⁶ 7 U.S.C. § 136l(a) (Supp. II 1972).

⁴⁷ 7 U.S.C. § 136l(b) (Supp. II 1972).

⁴⁸ Compare, e.g., Cal. Pub. Res. Code, §§ 21,000 et seq. (Supp. 1973), with Mass. Gen. Laws Ann. ch. 30, §§ 61, 62 (Supp. 1973), and N.Y. ECL § 3-0301.2C (1973).

⁴⁹ The California Environmental Quality Act of 1970, Cal. Pub. Res. Code, §§ 21,000 et seq. (Supp. 1973), was interpreted in the case of *Friends of Mammoth v. Mono County*, 8 Cal. 3d 247, 502 P.2d 1049, 104 Cal. Rptr. 761 (1972), wherein the California Supreme Court held that the statute applied to private developers and required state and local agencies to file an environmental impact statement before acting on a private action. In this case, the local governmental body was required to file an environmental impact statement prior to acting on a private developer's permit application for the construction of a housing development. *Accord*, *Eastlake Community Council v. Roanoke Associates, Inc.*, 82 Wash. 2d 475, 315 P.2d 36 (1973) (en banc).

⁵⁰ See, e.g., Wyo. Stat. §§ 35-502.1 et seq. (Cum. Supp. 1973).

It should be noted also that there are non-statutory sources of environmental law, both at the state and federal level. See, e.g., Note, 15 B.C. Ind. & Com. L. Rev. 795 (1974);

Thus, an independent search to determine the effects of applicable state law may be appropriate.

II. SEC POLICIES AND THE NEPA MANDATE

As a result of the mandate of the National Environmental Policy Act of 1969, the SEC was charged with the duty of improving and coordinating its plans, functions, programs and resources in order to fulfill the environmental goals enumerated thereby. However, while the Commission was reviewing its policies and goals with respect to NEPA, it was being pressed by environmental groups to require environmental disclosure in reports filed with the Commission. The environmentalists also petitioned for required SEC rule-making activity under Rule 4 of the Commission's Rules of Practice. The Commission's general investigation disclosed no serious securities violations with respect to a need for expanded environmental disclosure. As a result, suit was filed, pursuant to section 9(a) of the Securities Act of 1933, in the Court of Appeals for the District of Columbia, wherein direct review of a Commission order was sought. The court indicated from the bench that no reviewable "order" existed within the confines of the Securities Act of 1933, but that a district court case would lie pursuant to NEPA. This litigation is still pending against the SEC in this regard.⁵¹

Subsequently, as the first step in conforming policies and regulations to the mandates of NEPA, the Commission issued Securities Act Release No. 5170.⁵² The Release called attention to environmental significance with respect to the disclosure requirements al-

Comment, *The Aftermath of the Clean Air Amendments of 1970: The Federal Courts and Air Pollution*, 14 B.C. Ind. & Com. L. Rev. 724, 755-61 (1973); Note, 14 B.C. Ind. & Com. L. Rev. 767, 770 (1973).

⁵¹ *Natural Resources Defense Council, Inc. v. SEC*, [1972-1973 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 93,784 (D.C. Cir. 1973). Following the court of appeals' advice that a suit would lie under NEPA, action was commenced to compel the SEC to act under Rule 4 of the SEC's Rules of Practice and engage in rule making activity in accordance with NRDC's petition. The NRDC petition required certain modes of interpretation of SEC rules wherein companies would be required to disclose the types of emission control equipment as well as any engineering data in connection therewith. The SEC countered that the point was moot inasmuch as rule making had then been completed. The district court case was stayed, [1972-1973 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 93,805 (D.D.C. 1973), while the NRDC proceeded to challenge the rules again before the court of appeals. The court of appeals, however, stayed that action, Civil No. 73-1591 (D.C. Cir. 1973), pending the determination as to the same point by the United States Supreme Court arising under the Securities Exchange Act of 1934. *PBW Stock Exchange, Inc. v. SEC*, 485 F.2d 718 (3d Cir. 1973), petition for cert. filed, 42 U.S.L.W. 3434 (U.S. Jan. 21, 1974) (No. 73-1134). As a sequel to this game of "round robin," it is anticipated that the district court which has jurisdiction will address the substantive issues inasmuch as additional action is contemplated by NRDC under the Administrative Procedure Act.

⁵² SEC Securities Act Release No. 5170 (July 19, 1971), reprinted in [1970-1971 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 78,150.

ready contained in the Commission's forms and rules under the Securities Act of 1933 and the Securities Exchange Act of 1934. The Release noted that, in describing a company's business on Commission forms or in response to Commission rules, full disclosure would be required

when compliance with statutory requirements with respect to environmental quality e.g., various air, water, and other anti-pollution laws, may necessitate significant capital outlays, may materially affect the earning power of the business, or cause material changes in registrant's business done or intended to be done.⁵³

Additionally, the Release announced the Commission's view that material legal proceedings under federal, state or local statutes regulating the discharge of material into the environment, or otherwise specifically relating to the protection of the environment, would have to be disclosed.⁵⁴ Further, if such litigation was pending or known to be contemplated and the disclosures were omitted from any required document on the ground of immateriality, the Commission stated that it would be the practice of the Division of Corporation Finance to request as supplemental information: (1) a description of the omitted information, and (2) a statement of the reasons for the omission.⁵⁵

After approximately six months of review of disclosures by companies, pursuant to Securities Act Release No. 5170, the Commission determined that additional action was necessary. In Securities Act Release No. 5235,⁵⁶ the Commission sought public comment on its proposals to amend the registration and reporting forms to require material disclosures concerning the effect that compliance with environmental laws and regulations would have upon the capital expenditures, earnings and competitive position of an issuer of securities and its subsidiaries. Additionally, full disclosure was recommended with respect to pending or contemplated enforcement proceedings arising under environmental laws.

In response to public comment, on April 20, 1973, the Commission, in Securities Act Release No. 5386,⁵⁷ adopted amendments to its registration and reporting forms to require disclosures with respect to the effect upon the issuer's business of compliance with

⁵³ Id.

⁵⁴ Id.

⁵⁵ Id.

⁵⁶ SEC Securities Act Release No. 5235 (Feb. 16, 1972), reprinted in [1971-1972 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 78,524.

⁵⁷ SEC Securities Act Release No. 5386 (April 20, 1973), reprinted in [1973 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 79,342.

federal, state and local environmental laws. The registration forms amended under the Securities Act of 1933 were Forms S-1, S-7 and S-9. Under the Securities Exchange Act of 1934, the amendments pertained to Forms 10, 10-K and 8-K.

In an effort to "promote investor protection and at the same time promote the purposes of the National Environmental Policy Act," Release No. 5386 embodies a dual-pronged disclosure scheme regarding compliance cost effects on business, and the description of judicial and administrative proceedings.

The required description of business items, as amended, calls for information concerning business done and intended to be done, both during prior years and in future periods, and provides for disclosure of

"the material effects that compliance with Federal, state and local provisions 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."⁵⁸

According to the Commission's own statement in the introductory note, the business description items "emphasize the possible future effect of environmental statutes and regulations,"⁵⁹ but do not specify any minimum or maximum time period required in the description since "environmental compliance programs for different industries may involve substantially differing lead times."⁶⁰ Instead, the Release places the burden of the time-period decision on the shoulders of management to disclose if management has a reasonable basis to believe that future environmental compliance may have a material effect on such expenditures, earnings or competitive position. Further, management must segregate amounts, if there is a reasonable basis, for expenditures which are partly for the replacement, modification or addition of equipment or facilities and partly for the purpose of complying with environmental provisions.⁶¹

Contrary to the Commission's disclosure requirements with regard to other types of litigation, all administrative or judicial proceedings arising under the environmental laws are deemed by the release not to be considered as "ordinary, routine litigation incidental to the business," and must be disclosed whether or not the "10% economic materiality tests" apply.⁶²

⁵⁸ Id.

⁵⁹ Id.

⁶⁰ Id.

⁶¹ Id.

⁶² Id.

The Release centers around the question of materiality, which is common to many aspects of the federal securities laws, and seems to expand upon that concept in one instance. As a rule, the Commission defines materiality in the common law tradition as facts pertaining "to those matters as to which an average prudent investor ought reasonably to be informed before purchasing the security registered."⁶³ This definition of materiality has been most recently noted with approval in *Escott v. BarChris Construction Corp.*,⁶⁴ which defined a material fact as "a fact which if it had been correctly stated or disclosed would have deterred or tended to deter the average prudent investor from purchasing the securities in question."⁶⁵ Further, the mythical prudent investor would be concerned with facts which have an important bearing upon the nature or condition of the issuing corporation or its business. So, while in most contexts the Commission depends upon the common law judicial definitions of materiality, it has attempted in Release No. 5386, at least with respect to environmental legal proceedings, to impose a more stringent materiality test approaching materiality per se (i.e., all environmental legal proceedings and their factual basis must be disclosed, economic materiality notwithstanding).

III. ADMINISTRATIVE AND JUDICIAL PROCEEDINGS

Release No. 5386 requires a description of administrative and judicial proceedings arising under any federal, state or local provisions relating to the discharge of materials into the environment or otherwise relating to the protection of the environment. Since the description must include the factual basis of the proceedings and the relief sought, a brief review of the scheme and types of proceedings which usually arise is helpful. However, it should be noted that this is a new and rapidly developing area and the discussion herein is general since administrative procedures and enforcement methods are evolving.

The technique of controlling water and air pollution centers around permits and compliance schedules designed with the cooperation of government and industry. In the water area, a discharge permit will be required and a stipulated compliance schedule adhered to. In the air pollution area, emission limitations have been promulgated for existing sources. A compliance schedule, in step with EPA regulations, is required. With respect to new sources of air pollution, stricter requirements are mandated which encompass

⁶³ 1 L. Loss, Securities Regulation 305 (2d ed. 1969) (footnote omitted), quoting SEC Rule 405.

⁶⁴ 283 F. Supp. 643 (S.D.N.Y. 1968).

⁶⁵ Id. at 681.

stricter emission limitations contained in the new source performance standards. The permit system is also utilized by local governments for noise pollution and solid waste creation and management.

Enforcement procedures under the environmental laws are less formally defined than other administrative law areas. Currently, the EPA is still in the process of promulgating initial regulations. Federal enforcement procedures in the environmental area are somewhat simplified due to the fact that the Administrative Procedure Act is short-circuited in the environmental area in some instances.⁶⁶ By delegation, the ten Regional Administrators are responsible for much of the administrative procedure.

To date, formal adjudicatory hearings are more prevalent in connection with the water permit program,⁶⁷ and air enforcement cases are handled more often by less formal procedures. The EPA is authorized to pursue the injunctive route against polluters.⁶⁸ Additionally, certain newly promulgated (within 30 days) actions of the EPA may be directly challenged in the appropriate circuit court⁶⁹ and the enforcement orders issued administratively are under the jurisdiction of the federal district courts.⁷⁰ Criminal proceedings are handled through the appropriate United States attorney's office. The remedy of criminal and civil fines has also been provided.

In the environmental enforcement area, citizen suits are encouraged and provided for,⁷¹ and, of course, citizens and environmental pressure groups have sued under state and local statutes.

The disclosure which should be addressed to the citizen suits is a difficult question. The test of materiality per se would seem to indicate that all such suits must be disclosed and the factual basis explained. The existence of this type of test, with respect to citizen suits, should be examined closely by the SEC. There exists the potential for interference with the capital markets by rabid environmental pressure groups directed toward companies contemplating public financings, which could result in a new derivative suit remedy. The fact pattern most often is demonstrated in registration statements which are about to become effective when a party suddenly emerges threatening to file a significant lawsuit on the eve of

⁶⁶ For example, Congress believed the overriding need to achieve clean air outweighed a need for lengthy administrative proceedings and allowed the EPA to promulgate regulations under 42 U.S.C. § 1857c-5 (1970) after conducting an informational legislative-type hearing.

⁶⁷ An adjudicatory hearing may be requested by interested persons relative to the issuance or denial of a discharge permit. 40 C.F.R. § 125.34(c) (1973).

⁶⁸ 42 U.S.C. §§ 1857c-8(a), (b) (1970); 33 U.S.C. §§ 1319(b), 1342(h) (Supp. II 1972).

⁶⁹ 42 U.S.C. § 1857h-5(b)(1) (1970); 33 U.S.C. § 1369(b)(1) (Supp. II 1972).

⁷⁰ 42 U.S.C. § 1857c-8(a) (1970); 33 U.S.C. §§ 1319(a), 1342(h) (Supp. II 1972).

⁷¹ 42 U.S.C. § 1857h-2 (1970); 33 U.S.C. § 1365 (Supp. II 1972).

effectiveness.⁷² The results are most often very damaging to the issuer inasmuch as the normal method of public financing requires such a highly-coordinated effort. It is the authors' concern that, perhaps, some environmental groups would use this same sort of tactic against companies and create an "effective date blackmail" scheme in the environmental area. It is the authors' further opinion that, if the experience of the SEC discloses that this is or does become prevalent, the test be altered to prevent the practice.

IV. FRAMEWORK OF ENVIRONMENTAL DISCLOSURE

Securities Act Release No. 5386, due to the mandate of NEPA, requires disclosure of environmental matters by companies affected by SEC public disclosure requirements. In an effort to assist practitioners in their compliance with this release, the authors have attempted to delineate some major policy areas, on an industry basis, which are appropriate areas for disclosure. The balance of this article will concentrate on some major items of disclosure in the industry groupings of mining, land development, oil and gas, and manufacturing.

A. *Mining*

Environmental problems concerning mineral resources are presently receiving considerable attention on a nationwide scale. As a first proposition, it is important to note that, with respect to the exploration and development of mineral resources, the conflict between environmental protection and mineral development is a sharply-drawn issue. Consequently, it is incumbent upon the securities practitioner to make broad analytical inquiry into mining operations for disclosure purposes with respect to environmental matters.

The first and most pointed inquiry with respect to mining should presently be directed toward proposed legislation and its potential effect on the mining business of a company. This necessary inquiry must be made inasmuch as, beginning with the 92nd Congress, an exceptionally large number of legislative proposals have been introduced, including those dealing with surface mining restrictions, marine mineral exploration, mining law revisions, mineral research development, mineral recycling and other areas. Whereas details of proposed legislation are probably not necessary, a summary of the more important features is in order.⁷³

⁷² See, e.g., *American Thermal Resources, Inc. v. Milligan*, Civil No. C-26307 (Los Angeles County Super. Ct. 1972).

⁷³ The recent Prospectus of Ruby Mining Company (Reg. No. 2-47774, July 10, 1973)

The second major environmental inquiry with respect to mining is necessarily directed at disposal of waste products produced from mining operations and the costs of preventing them from being environmental hazards. The results of mining remain long after the activity because of the permanent and conspicuous nature of its wastes. Most prominent is the problem of mill tailings piles, which are the residue remaining after the commercial ore has been extracted. The tailings piles, depending upon their constitution, are subject to erosion during surface runoff events. In turn, the runoff carries the mineral-laden sediment into streams where subsequent leaching is most often a source of water quality degradation.⁷⁴ This type of discharge requires a waste-water discharge permit,⁷⁵ and proper disclosure of the effects of the discharge and economic costs of cleanup is mandatory. If the tailings are properly isolated from the local hydrology, then costs may be mitigated and this waste disposal problem is removed from the purview of the permit program.

Another major problem in the mining business, which is a necessary subject of disclosure, is the return of the ground rock into the mined space after milling. Due to the bulking effect which

disclosed the thrust of proposed legislation, under a caption entitled "Environmental Impact and Proposed Legislation," as follows:

The exploration operations, such as are contemplated by the Company are subject to State and Federal regulations regarding environmental considerations. The Company is not aware of any serious problems in this regard in connection with its proposed exploration. Should the Company discover an ore body which it believes to be commercial, an environmental impact study must be made which could adversely affect future mining operations.

Legislation has been introduced in Congress, which if passed, would materially change the Federal mining laws. The Company is unable to ascertain the effect upon its titles to its properties should this proposed legislation be enacted. Such legislation is designed in part to establish a nation-wide program to prevent adverse effects and permanent damage to the environment, land and water. The proposed legislation, if passed, would require the obtaining of permits to conduct surface exploration, surface mining and reclamation. The granting of mining permits would be conditioned upon an operator demonstrating that his mining plan would not endanger the environment and would restore the land to its former condition. To renew a permit, an operator must demonstrate compliance with the statute. Inspection of the mining and reclamation operations would be made by the regulatory authority prior to granting renewal to assure compliance. In addition, to obtain a permit, physical and financial responsibility would have to be shown, by insurance or otherwise, and a reclamation plan for the land covered would have to be submitted and approved. Failure to comply would subject an operator to possible civil and criminal penalties. Should the legislation pass, the Company could be required to expend funds to reclaim its properties from any damage to the property resulting from the proposed exploration.

⁷⁴ See Final Environmental Statement, Lead-Deadwood Sanitary District No. 1, South Dakota Project No. WPCSD-200 (March 1972), and the First Supplemental Environmental Statement thereto (Oct. 26, 1973), prepared pursuant to § 102(c) of the National Environmental Policy Act of 1969 by the EPA, Region VIII, Denver, Colo.

⁷⁵ 33 U.S.C. §§ 1342-45 (Supp. II 1972).

results during grinding of ore, all of the ground rock usually cannot be replaced in the mined spaces. The result is that the unreplaceable ground rock has historically been sluiced directly into the nearest stream with the resultant waste-water mixture "clogging" the stream. Disposal methods and cost should be disclosed. A discharge permit is required, and the cost of compliance therewith must be discussed.

Further analysis should focus upon and identify any damaging by-products of the production cycle produced and should analyze their effect on the environment. For example, in the case of production of geothermal energy, the brine produced and its potential for pollution of surface and/or groundwater bodies presents a unique problem.⁷⁶

Often, a by-product of mining is the discharge of toxic materials. This should be investigated and disclosed as a major environmental factor inasmuch as such discharge is potentially dangerous. As a result, it is more difficult and costly to abate and could result in a court imposed cessation of operation.⁷⁷ For example, the Homestake Mining Company (the largest domestic producer of gold) discharges cyanide into streams in the amount of 180 pounds per day, and discharges varying amounts of several other metals, including arsenic, iron, lead, zinc and selenium.⁷⁸ At a hearing conducted by the EPA on December 11, 1973, in Deadwood, South Dakota, pursuant to its NEPA review, it was revealed that the cost of treatment of these wastes has risen from the original estimate of \$3-\$4 million up to approximately \$13-\$14 million. As this example makes clear, it is incumbent to focus upon poisonous substances which are released into the environment, and to make adequate disclosure of the hazards and abatement costs in connection therewith.

Further inquiry should probably be made with respect to the creation of "environmental eyesores" by the mining industry. En-

⁷⁶ The Prospectus of American Thermal Resources, Inc. (Reg. No. 2-43076, April 12, 1972) describes the brine disposal problem and generation of unwanted by-products, which could potentially pollute, under the caption "Risk Factors," as follows:

Possible Environmental Control Costs. There is increasing national concern over the ecological impact of power generation. Certain geothermal steam wells have been known to produce noxious and poisonous substances, and it can be expected that development of this source of power will be subject to restrictions to protect the environment. Such restrictions may be costly and time consuming with respect to the development of any source of geothermal power. Should hot water be produced with the geothermal steam, the steam conditions may be too wet or too corrosive for an economic generation of electricity. Moreover, the water so produced may not be mixable with surface or ground bodies and may require disposal in deep wells required to be drilled for this purpose.

⁷⁷ See 42 U.S.C. § 1319 (Supp. II 1972), especially § 1319(b).

⁷⁸ See Final Environmental Statement, *supra* note 74, at 4.

vironmental eyesores are not necessarily, by their nature, pollutive of the air or water, but they are aesthetically displeasing. Inquiry should be made in this regard. However, disclosure should be tempered with the realities of alternatives available and whether land-use provisions apply.

The problem of air pollution in mining operations should be addressed, and the most prevalent form of pollution, especially in arid climates, is so-called "fugitive dust" created by earth-moving operations. A permit may be needed which imposes stringent and costly requirements for maintaining the ambient air quality standards for particulate discharge.⁷⁹

Strip mining, generally, is one of the most politically potent subjects related to the mining business. Potentially, the most significant environmental cost related to strip mining is reclamation. Therefore, reclamation costs must be quantified and the economics of a reclamation plan should be disclosed, along with the effects of such plan on the competitive position of the issuer. For example, due to terrain and climatic differences, two bodies of coal similar in composition may result in dissimilar profits because of a disproportionate reclamation burden.

Proposed legislation will probably establish the format for environmental disclosure required in surface mining operations. The legislation is expected to limit the amount of land which can be excavated at one time, and require combining the process of reclamation with the progress of mining operations. However, the extent of the proposed legislation is not known and some very restrictive measures have been advocated, among them a prohibition of "hanging" walls, which would greatly increase reclamation costs.⁸⁰ Therefore, such new requirements mandate comparative disclosures with respect to the increased cash flow needs for carrying on a reclamation project while mining. Additionally, costs of such steps as measures which must be taken to protect offsite areas from environmental degradation, stabilization and re-vegetation of refuse and waste piles, stabilization of access roads, natural drainage restoration, performance bonds, and topsoil preservation costs should be mentioned if their performance is required.⁸¹

B. *Land Development*

In terms of sheer numbers of inexperienced participants, the Gold Rush of 1849 was far less alluring than has been the land

⁷⁹ 42 U.S.C. § 1857c-5(a)(4) (1970). In most states, a permit to operate may be required under the state implementation plan.

⁸⁰ Smith, *Land Use and the Extractive Industries*, 3 *Colo. Law.* 17, 21 (1974).

⁸¹ See, e.g., Proposed Forest Service Regs. §§ 251.12, 252.1-17, 293.13-15, 38 Fed. Reg. 34,817 (1973).

development boom of the 1970's. In this respect, many land development projects, which are either publicly financed or financed through the utilization of the private offering exemption, have probably overlooked or failed to properly disclose many items in the project which could potentially have adverse environmental effects.

One of the basic inquiries is the effect of state, county and municipal statutes, ordinances or regulations which could frustrate development. Of course, land-use regulation varies greatly depending upon the location of the project, but, generally, such regulation provides for the assurance of an adequate domestic water supply, sewage drainage plans, the compatibility of topography with proposed uses and the total land-use plan. A general knowledge by the practitioner of the local land-use regulatory scheme is a prerequisite in structuring the disclosure. With respect to topography, inquiry should be made to determine the stability of the soil, whether the soil will support the structures planned and whether erosion problems exist. Adverse topographical or geological conditions should be the subject of disclosure inasmuch as fragile terrain may severely limit the carrying capacity of the land and, in turn, limit the amount of development. This disclosure should also be analyzed with respect to land adjacent to the proposed project. Such problems can also include a topographical condition wherein roads would possibly exceed maximum grade standards or there is a potential for earth slides, avalanches or earthquakes.

The availability of water resources is a necessary prerequisite to any land development. The efficiency, quantity, quality, location, dependability and extraction of water resources should be examined and discussed as they relate to the project and local land-use regulations.⁸² Any further inquiry should be directed to the manner in which the land will accommodate itself to the drainage and flood plain requirements imposed by state and local law. Thus, the extent of the nondevelopable land must be ascertained and disclosed.

The method of sewage treatment must be disclosed. Disclosure should relate to whether there is an association with an existing system or whether formation of a sanitary district and self-funded construction of a treatment plant is necessary.⁸³ Information should be disclosed with respect to any problems and additional costs associated with the formation of special water and sewer improvement districts, which could result in a heavy front-end burden and

⁸² See, e.g., Colo. Rev. Stat. Ann. § 106-2-34(e) (Cum. Supp. 1972).

⁸³ A municipal discharge permit will be required, which must be consistent with the state water planning process (the so-called "303(e)" planning process) required under the Federal Water Pollution Control Act Amendments of 1972, 33 U.S.C. § 1313(e) (Supp. II 1972). 40 C.F.R. §§ 130.1 et seq. (1973).

reduce profitability of the venture. In the past, land development plans utilizing septic tanks and leaching fields have been prevalent. However, increased density and/or subsurface conditions many times now render this method unacceptable if groundwater pollution is caused. Therefore, discussion of this potential problem may be necessary.⁸⁴

The problem of disclosure with respect to reductions in the aesthetic experiences or surroundings in land development presents a difficult problem. The parameters of disclosure with respect to aesthetic matters belie precise quantification. Suffice it to say that only the more notorious aesthetic reductions should be considered appropriate for disclosure.⁸⁵

Another area of environmental analysis with respect to land development is the potential adverse consequences to the project resulting from problems in obtaining necessary governmental action not directly associated with the development project itself, but vital to such development. An example of this would be a highway project to improve access to the area. Not only the specific and adjacent parcels of land must be analyzed with respect to environmental impact, but the entire area must be given scrutiny. Environmental impacts of this type occur more frequently in the recreational land development scheme (which, of late, is the subject of many public financing efforts), but can occur in any land development project.

Returning to the example of a paving project to increase accessibility, if federal monies are used, the project may be the subject of an environmental impact statement. The attendant intense recreational pressures resulting from the introduction of more users and visitors due to improvement of accessibility could cause significant

⁸⁴ The first developer in the area is generally allowed to utilize septic tanks. However, subsequent developers may be precluded by the local permitting body from the less costly avenue of sewage disposal because the carrying capacity of the soil in the drainage area may have been reached.

⁸⁵ An example of an area where aesthetic reduction disclosure could be required is in the case of cattle feeding. The existence of noxious odors and fugitive dust, if the operation is in an urbanized area or is proximate to an urban setting, should be appropriately disclosed. Recent cattle feeding prospectuses have (like most other prospectuses) included only general environmental disclosures. An example of this is the Prospectus of Chaparral Cattle Feeders (Oct. 1, 1973):

Cattle feedyard operations are potentially significant sources of environmental pollution. The states in which Partnerships may feed cattle, and in some cases subdivisions of such states, have enacted water and air pollution control statutes with which feedyards must comply in conducting their businesses. National and local governmental bodies are becoming increasingly concerned with environmental considerations, and it is possible that this concern will result in the imposition in the near future of controls which are more strict than those presently in effect. Compliance with any such controls may be expected to result in increases in the costs of feeding cattle.

adverse environmental impacts to the general area and, thus, frustrate the development. Impacts, such as noise and disturbances (for example, snowmobiles and off-the-road vehicles), fires, litter and encroachment on wild and natural areas, could cause sufficient negative environmental impacts to result in irreversible social and economic impacts to the general area. Thus, appropriate governmental agencies may not authorize needed favorable action. Industries participating in public financing efforts should be aware of these problems and disclose pertinent aspects thereof.

Development in urban areas will be influenced by the EPA's indirect source regulations.⁸⁶ Housing subdivisions, shopping centers and industrial facilities located in metropolitan areas (especially those areas with polluted air) must disclose costs of compliance, including air monitoring and traffic modeling,⁸⁷ as well as comment on the permit process (approval, denial or forced contraction of the proposed project). Inquiry should be directed to whether the proposed project is located within an area designated for potential air pollution problems.⁸⁸ Development within such areas will carry a heavier compliance burden.⁸⁹ Approximately 34 states have legal authority to regulate the placement and size of indirect sources of air pollution⁹⁰ and, in some instances, states are more stringent than the EPA in their approach.⁹¹

C. Oil and Gas

The necessity for more meaningful disclosures with respect to the environment in the oil and gas industry is obvious.⁹² There are three major areas within the industry, each requiring a different

⁸⁶ 38 Fed. Reg. 29,893 (1973).

⁸⁷ Through the use of computer models which contain base information regarding traffic density, it is possible to determine the effect a proposed development will have upon traffic load in a given area, and possible resultant auto-related air pollution increase.

⁸⁸ Air quality maintenance areas will be designated during 1974 by either the several states or the EPA. These are areas in which it is estimated that an air pollution problem will develop during the next decade. Land-use plans will be required to prevent the anticipated problem. 38 Fed. Reg. 15,834 (1973).

⁸⁹ Proposed developments must comply with the overall growth plan which is not required outside of designated areas.

⁹⁰ Those states which do not have such legal authority are: Alaska, Iowa, Kansas, Michigan, Mississippi, Missouri, Montana, New Jersey, North Dakota, Oklahoma, South Carolina, South Dakota, Tennessee, Texas, Utah and Wyoming.

⁹¹ Colo. Rev. Stat. Ann. §§ 66-31-3, -6, -11, -12, -13 (Perm. Cum. Supp. 1971); proposed amendments to Colo. Air Quality Control Reg. No. 7.

⁹² Generally, all that has been required is a bland statement of potential environmental problems. See, for example, the Offering Circular of Wulf Oil Corp. (Dec. 14, 1973), which disclosed: "It should be noted that compliance with statutory requirements respecting environmental quality may necessitate significant capital outlays which might materially affect the earning power of the Company, or may cause material changes in the Company's proposed business."

emphasis with respect to environmental disclosures. The three major areas are the extractive or explorative portion of the industry (discovery and recovery of petroleum), the refining portion (distillation of petroleum into marketable by-products), and the marketing function. Environmental disclosures with respect to the extractive and marketing phases will be treated here. The refining phase is more closely allied to manufacturing businesses, which are treated elsewhere in this article.

The most visible environmental problems created by the traditional explorative and extractive phase are oil spills, pipeline breaks and blowouts. Each occurrence is the object of great amounts of publicity if the event is slightly greater than infinitesimal in effect. However, inasmuch as spills, breaks and blowouts occur statistically in few cases when compared with the number of wells drilled and the extensive pipeline systems in the United States and internationally, disclosure of the propensity for spills, breaks and blowouts should probably be severely limited, unless certain geologic or topographical conditions significantly heighten the risk of these types of catastrophic occurrences.

The clearance of trails through forested areas for seismic exploration is a source of environmental concern and, therefore, should be the subject of disclosure. Such trails are normally cut in order to follow the underground geological formations that are the subject of the test and, as a result, there is no overriding concern for the surface and natural cover. With respect to such seismic trails, inquiry must be made concerning damage that cutting the trails may cause and reclamation of the trails, once cut. Normally, reclamation requirements include backgrading, reseeding and fertilizing. However, it is not without the realm of possibility to require the guarantee of a timber stand in some cases, which would negatively influence the profitability of the venture.

Groundwater pollution is another major problem in the explorative and extractive phase. Normally, cementing procedures and the use of a pipe which meets surface pipe requirements are mandated for the fresh water geological zone in petroleum recovery. The failure of such cementing procedures could cause groundwater pollution by the oil. If the geologic structure of the drilling site is such that there is a risk that cementing procedures may not prevent groundwater pollution, then such increased risk should be disclosed.

The aesthetic experience reduction problem is not a significant problem with respect to conventional drilling operations. However, there are two major areas of inquiry which should be made in that regard. First, if the site is proximate to an urban setting, disclosure

should be made with respect to the cost of the steps that may be taken to camouflage the operation once drilling is completed. The second area of inquiry is the cost which must be expended to reduce the noise level of the pumping operation.

If secondary recovery methods are proposed and involve the construction of a plant or similar hardware to implement the recovery system, the environmental impacts indigenous to the implementation of such secondary recovery system must be disclosed.

The area of offshore drilling poses special and different environmental problems. The technology to abate environmental hazards of such drilling and exploration is still being developed inasmuch as focus on offshore drilling and the resulting potential for environmental problems is relatively recent. Disclosure should probably center around the special problems and the technological answers which are being developed. An example of this would be the new emergency shut-off systems, which are being developed to prevent and contain blowouts in offshore drilling because the offshore blowout causes significant water pollution, endangers marine life and spreads rapidly as the result of currents.⁹³ Generally, the company should disclose whether or not it is using or will use the "best available technology" to counteract and diminish the hazards of offshore exploration and recovery. For example, new electronic probes are available to reduce coring and disturbance of marine life due to exploration activity.⁹⁴

Oil shale development poses perhaps the most complex and difficult environmental problems in the area of petroleum product extraction. The prototype oil shale leasing program is underway and, prior to widespread commercial oil shale development, more information should be available concerning the difficulty and costs of preventing significant environmental degradation. There will be significant water quality problems. For example, increasing salinity in the Colorado River Basin is already an international and interstate problem. The development of oil shale in the upper reaches of this basin will result in downstream salinity increases and resultant economic detriments as the result of the salt-concentrating effects of consumptively using surface water resources for oil shale operations. Added to this will be large increases in salinity attributable to the disposal of excess waters and from erosion of spent shale pile leachates.⁹⁵ This degradation in water quality in the Colorado River Basin will be contrary to the goals of the Federal Water Pollution

⁹³ 4 BNA Env. Rptr. 22-24 (1973).

⁹⁴ *Id.* at 23.

⁹⁵ This process is the percolation of runoff water through the spent shale pile.

Control Act Amendments of 1972. Furthermore, such an effect on water quality would be in conflict with the degradation conclusions and recommendations on salinity which were adopted at the Seventh Session of the Conference in the Matter of Pollution of Interstate Waters of the Colorado River and its Tributaries, held on April 27, 1972.⁹⁶ Other water quality problems could result from sedimentations, heavy metals, toxic materials, oil spills and municipal waste-water discharges.

Waste-water discharge permits⁹⁷ will be required from either the EPA or one of the states⁹⁸ in which oil shale developments are taking place. Permits will be required for discharges from spent shale piles, discharges from desalination plants and, possibly, for discharges from point sources of re-injection of excess waters from the process. Companies should report the costs attributable to compliance with required permit conditions and a discussion should also focus upon the salinity problem and the issuer's proposed plan for meeting this problem.

A significant amount of air quality deterioration will be associated with oil shale development. Oil shale leases from the federal government and requirements by the EPA under the Clean Air Act⁹⁹ may require substantial air monitoring to obtain pre-oil shale development statistics. Inquiry should be made to determine costs attendant to any monitoring requirements, and to any delay involved as a result thereof. In order to meet air quality emission standards, some combination of stack height, pretreatment or stack gas technology will be required to abate the effects of sulphur oxide pollutants. The EPA regulations to prevent the significant deterioration of air quality¹⁰⁰ and applicable state air pollution laws will mandate the costs in this area.

One of the most difficult problems associated with oil shale development will involve reclamation of vast amounts of spent shale to prevent wind and water erosion. Federal lease requirements call for re-vegetation of disturbed areas. However, re-vegetation expenses in excess of \$500,000 per lease may be deducted from the royalty payments under the lease terms.

With respect to the marketing phase of petroleum products, evaporative loss of hydrocarbons during the storage, transfer and

⁹⁶ Reconvened Seventh Session of the Conference in the Matter of Pollution of the Interstate Water of the Colorado River and its Tributaries—Colorado, New Mexico, Arizona, California, Nevada, Wyoming and Utah (Denver, Colo., April 26-27, 1972), published by the EPA, Region VIII, Denver, Colo.

⁹⁷ 33 U.S.C. § 1342 (Supp. II 1972).

⁹⁸ Those states currently are Colorado, Utah and Wyoming.

⁹⁹ 42 U.S.C. §§ 1857c-9(a)(1)(C), (D) (1970).

¹⁰⁰ Proposed EPA Reg., 38 Fed. Reg. 18,986 (1973).

marketing of petroleum products (principally gasoline) has contributed to the serious smog problems of the major U.S. cities.¹⁰¹ The end result of a chemical reaction between hydrocarbons and other elements in the atmosphere is the photochemical smog that causes injury to the eyes and respiratory system. The EPA has promulgated regulations to control this problem.¹⁰² The regulations call for vacuum-sealed storage facilities (both at large terminal sites and at the service station level) and the use of a vapor recovery system during gasoline transfer (*i.e.*, from storage tank to tank truck, from tank truck to service station tank and from service station to automobile). Some of the control equipment is still in the development stage and, as a result, the required installation timetable is staggered between mid-1974 and mid-1977. The compliance costs are substantial, running from \$2,000-\$5,000 per service station and \$10,000-\$15,000 per tank truck. Many cases are pending against the EPA which, in whole or in part, challenge these regulations.¹⁰³ The applicability of these regulations should be examined to determine costs of compliance and competitive impact.¹⁰⁴

D. *Manufacturing*

The breadth of this area precludes detailed discussion. Consequently, only broad areas of interest which apply to manufacturing processes will be explored. In addition to the costs related to abatement of air and water pollution attributable to the manufacturing process—which must, of course, be sought out and analyzed—the practitioner should determine the effect of environmental provisions on the product.

Production costs may have been added to assure that the product is in compliance with applicable standards and, if the costs associated therewith are quantifiable, they should be separately disclosed. Congressionally-mandated pollution control devices on automobiles have necessitated the addition of hundreds of dollars to the price of each automobile. Separate disclosure should be possible for costs attributable to lowering the noise level of construction equipment. A further instance is the example of the movement

¹⁰¹ This is a serious problem in the major metropolitan areas in California, Texas, New Jersey, Pennsylvania, Massachusetts, Colorado, the District of Columbia and Maryland.

¹⁰² See, e.g., 38 Fed. Reg. 30,821-24 (1973).

¹⁰³ Over 250 cases have been docketed against the EPA under 18 U.S.C. § 1857h-5 (1970), challenging the EPA-developed transportation control plans. Many of these cases involve the hydrocarbon recovery regulations. However, because briefs have not been filed, the essence of the dispute is not yet apparent.

¹⁰⁴ Companies whose major activities center in geographical areas subject to these regulations, such as California, will obviously fare adversely when compared to those whose marketing operations are centered primarily in rural and non-polluted metropolitan areas.

toward returnable glass soft drink containers,¹⁰⁵ which may dramatically affect those who now produce metal containers.

In addition to those engaged in the manufacture of pesticides, industries which rely on the use of pesticides, such as farming, should disclose any effects attributable to pesticide regulation. For example, inquiries should be made to determine if historically-used pesticides are still available or if an adequate substitute exists.

Most manufacturing concerns emit air and water pollution in varying degrees. Earlier sections with respect to air and water pollution abatement should be consulted for guidance in structuring proper disclosures. The location of the facility may be relevant. Greater degrees of air pollution control might be required in order to reach the ambient air quality standards for a facility located in a congested polluted area when compared to a facility located in a rural non-polluted setting. This may affect an issuer's competitive position.

The age and other physical characteristics should be examined. For example, in the smelting industry, older facilities are often more costly to retrofit with emission limitation equipment. Older facilities also tend to allow more fugitive emissions which are most difficult to capture and properly vent to an electrostatic precipitator and/or scrubbing device. Antiquated processes, by their very nature, may cause more pollution and are also, as a rule, more difficult to equip with emission capturing devices.

The comparative burden of pollution abatement impacts varies disproportionately from industry to industry. The cost of removing 90% of sulphur oxide gases from smelting operations is approximately \$.30-\$.40 per pound of product produced. The market price for refined copper is in the range of \$.70 per pound, while refined lead is marketed at approximately \$.20 per pound. Therefore, due to the price disparity, the pollution abatement costs in lead production may take a greater toll on profitability and available capital. Adequate analysis should reveal any competitive disadvantages and note any extraordinary pollution-related capital demands as well as the resulting effect on normal corporate activities. Therefore, perhaps a useful and needed analysis should be directed toward whether the issuer should consider a positive disclosure if normal corporate activities—for example, plant expansion or debt service—are materially affected. Disclosure guidelines using percentage tests for economic materiality would probably be appropriate in this area.

¹⁰⁵ Oregon Beverage Container Act, reproduced in [State Solid Waste-Land Use] BNA Env. Rptr. 1286:0201 (1973).

V. THE IMPACT OF THE ENERGY CRISIS

The current energy crisis has complicated certain aspects of life for all Americans. The securities law area is no exception. Changes are in the making for many environmental laws.¹⁰⁶ The SEC has announced that, as a result of the current energy crisis, publicly-held companies should make prompt and accurate disclosure of information concerning the effect of the energy shortage (both favorable and unfavorable) to security holders and the investing public, and of shortages of fuel or other types of energy and their impact on particular types of issuers.¹⁰⁷

A. Congressional Deliberations and the Administration Proposals

Since November 1973, Congress has been working on various proposals for an Energy Emergency Act (EEA)¹⁰⁸ in response to the energy crisis. The Act was passed by Congress, but in March 1974 it was vetoed, and the Senate failed to override the veto.¹⁰⁹ Since the veto, Congress has been working on compromises which would enact the substance of the EEA. In the midst of this congressional activity, the Administration, on March 22, 1974, submitted formal proposals for amendments to the Clean Air Act which resurrected several of the main-ideas of the EEA.¹¹⁰ Since these main provisions have now proven acceptable to both Congress and the Administration, their enactment in some form would appear likely.

These provisions relating to the Clean Air Act will be discussed in detail below along with the other provisions of the EEA. In addition to these provisions the following proposals were made. The Administration, without EPA concurrence, seeks two major changes. One would allow as a permanent strategy the use of Intermittent Control Systems which would allow use of curtailment of production in accordance with meteorological conditions in order to meet ambient air quality standards.¹¹¹ In addition, the proposals attempt to change the result of *Sierra Club v. Ruckelshaus*¹¹² by

¹⁰⁶ The President, in his energy message of Jan. 23, 1974, requested relaxation of certain environmental laws. 120 Cong. Rec. H151 (daily ed. Jan. 23, 1974).

¹⁰⁷ SEC News Digest 73-245 (Dec. 20, 1973).

¹⁰⁸ S. 2589, 93d Cong., 1st Sess. (1973).

¹⁰⁹ 120 Cong. Rec. H1243 (daily ed. Feb. 27, 1974) (bill sent to President); 120 Cong. Rec. S2926 (daily ed. Mar. 6, 1974) (Senate failed to override veto).

¹¹⁰ EPA Proposals for Amending the Clean Air Act, accompanying Address by Russell Train, EPA Administrator, in Washington, D.C., March 22, 1974 [hereinafter cited as Proposed Amendments].

¹¹¹ Id., Attachment C.

¹¹² 4 E.R.C. 1815 (D.C. Cir. 1972). See text at notes 33-35 supra.

revoking the authority of the EPA to promulgate standards designed to prevent air quality deterioration from levels exceeding minimum air quality requirements.¹¹³ With regard to air quality standards for auto-related pollutants, the EPA has requested authority to grant to severely polluted metropolitan areas deadline extensions beyond the 1977 statutory deadline. The Administration estimates that no more than one-half of the 38 metropolitan areas presently covered by EPA transportation control plans will be able to qualify for such deadline extensions.¹¹⁴ These three proposals are likely to come under congressional scrutiny in the coming months.

B. *The Original Energy Emergency Act*

In its form as originally passed, the Energy Emergency Act would have created a Federal Energy Administration (FEA) to administer the major programs covering the situation, such as fuel allocation and energy conservation measures.¹¹⁵ The law would have empowered the Administrator of the FEA to order major fuel-burning installations to switch to coal from natural gas and petroleum products after balancing the environmental effects of such conversional acts against the need to fulfill the purpose of the Act on a plant-by-plant basis.¹¹⁶

A new section is proposed to be added to the Clean Air Act which would allow the Administrator of the EPA to suspend, until November 1, 1974, emission limitations and compliance schedules contained in any federal, state or local law, regulation or requirement pertaining to fuel-burning sources.¹¹⁷ Further, during 1974, it has been announced that appropriate congressional committees will make a review to determine necessary modifications to federal environmental laws needed to respond to the fuel crisis over the long term. If a source switched permanently to coal from another fuel, the EEA would have provided that, where the installation of continuous emission limitation equipment was needed, the source, under statutory constraints, would have until January 1, 1979, to install such equipment and come into compliance.¹¹⁸

¹¹³ Proposed Amendments, *supra* note 110.

¹¹⁴ *Id.*, Attachment A, § 3. For the source of the EPA estimate, see Fact Sheet, Legislative Proposals to Amend the Clean Air Act of 1970, at 2 (EPA, March 22, 1974).

¹¹⁵ Immediately after the Presidential veto, the House passed a bill which would establish the Federal Energy Administration. See A Bill to Create a New Federal Energy Administration, H.R. 11793, 93d Cong., 2d Sess. (1974). See also 120 Cong. Rec. H1542-73 (daily ed. Mar. 7, 1974).

¹¹⁶ Section 106 of the conference version of S. 2589, 119 Cong. Rec. S23,823-24 (daily ed. Dec. 21, 1973).

¹¹⁷ Proposed § 119 of the Clean Air Act is contained in § 201 of S. 2589, 119 Cong. Rec. S23,829, S23,843 (daily ed. Dec. 21, 1973).

¹¹⁸ Proposed § 119(b) of the Clean Air Act is contained in § 201 of S. 2589, 119 Cong. Rec. S23,830-31, S23,845 (daily ed. Dec. 21, 1973).

The bill would also have suspended NEPA for one year as it applied to implementation of this Act. In other words, major short term actions taken under the EEA would have been exempt from section 102(c) of NEPA, which requires that an EIS precede major federal actions. However, prior to taking such action, pursuant to EEA, or, in any event, no later than 60 days after taking such action, the EEA would have mandated an environmental "assessment" equivalent to that required under section 102(c) "to the greatest extent practicable within this time constraint."¹¹⁹ The assessment would then have been available for a 30-day comment period and, "upon request," a public hearing would have been held to review environmental issues. But any action taken under this Act, the term of which would have extended beyond one year, would then be subject to the full provisions of NEPA.

When the Administrator of the FEA ordered a switching of fuels from natural gas to coal, this would have had a substantial impact upon fossil-fuel fired power plants. The result would have affected fuel costs and caused unexpected expenditures for tall stacks and/or stack gas cleaning devices required under the EPA-mandated installational guidelines. Filings and reports under the Public Utility Holding Company Act of 1935¹²⁰ would then have needed an extensive discussion of how these developments would affect the company.

It is premature to estimate the impact of the EEA, and the Administration proposals, in the securities/environmental area. At this time, no specific disclosure guidelines can be developed. However, the progress through Congress of the various proposals should be watched carefully, and their potential effect should be analyzed in connection with the exigencies of everyday business.

CONCLUSION

In connection with the authors' concern with respect to "effective date blackmail" suits, previously discussed, it is recommended that the SEC carefully regulate the breadth of environmental disclosure. Further, it is believed that the investor's decision should not be impaired by a deluge of extraneous technical and engineering information, emission data, specific technology planned for installation, and technology currently in use. The EPA already has authority to require this type of reporting, when relevant to its environmental mission.¹²¹ Over-zealousness on the part of the SEC in

¹¹⁹ Section 205(c) of S. 2589, 119 Cong. Rec. S23,831 (daily ed. Dec. 21, 1973).

¹²⁰ 15 U.S.C. §§ 79 to 79z-6 (1970).

¹²¹ See, e.g., 42 U.S.C. § 1857c-9 (1970).

requiring such technical reporting can only serve to dilute the significance of environmental disclosures generally, and cause a new genre of "boilerplate" language.

In summary, the SEC has indeed become a participant in the environmental movement, either wittingly or unwittingly, in that the environmental disclosure requirements may serve to discourage investment, not because of economics, but due to the political and social ramifications of the investment itself. More specifically, an investment decision adverse to a company can result in that the mythical investor "might not want to buy a polluter."