
PERSPECTIVES

ENVIRONMENTAL SELF- DISCLOSURE AS A TRANSACTIONAL RISK MANAGEMENT TOOL:

How EPA, DOJ, and State Audit Policies
Shape Environmental Liability in M&A
Transactions



Our perspectives feature the viewpoints of our subject matter experts on current topics and emerging trends.

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Legal advisors, corporate executives, and other corporate leadership should read this article to learn more about:

- How environmental self-disclosure is a valuation tool, not just a compliance exercise.
- How timing and voluntariness drive outcomes.
- Why coordinated EPA and DOJ strategy is essential.
- How post-acquisition “new owner” protections can materially reduce buyer risk.
- How state audit privilege laws can define deal risk.
- Why insurance does not replace disclosure strategy.

Executive Summary

Environmental self-disclosure has become a strategic transactional tool that directly influences valuation, risk allocation, and deal certainty in mergers and acquisitions involving regulated assets. This article explains how buyers and sellers can use the EPA Audit Policy, DOJ’s March 23, 2026 Corporate Enforcement and Voluntary Self Disclosure Policy, and varying state audit privilege laws to transform latent environmental noncompliance into manageable, quantifiable risk. By coordinating civil and criminal disclosure strategy, carefully managing timing and voluntariness during diligence and integration, and understanding the limits of representations and warranties insurance, deal teams can mitigate enforcement exposure, structure indemnities more precisely, and reduce post-closing uncertainty without undermining transaction objectives.

EXPERT VOICES

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John leverages his background as an environmental attorney and regulatory compliance expert to explain how environmental self-disclosure can be strategically used in M&As to convert latent noncompliance into quantified, deal-manageable risk. He focuses on coordinating EPA, DOJ, and state audit policies to protect valuation, limit enforcement exposure, and increase deal certainty.

Introduction

Environmental self-disclosure is often discussed in terms of regulatory compliance or enforcement. In modern transactions, however, it has evolved into a sophisticated risk management mechanism that can meaningfully influence valuation, indemnity structures, escrow sizing, post-closing integration strategies, and even a buyer’s willingness to close. In mergers, acquisitions, divestitures, and financing involving regulated assets, environmental noncompliance is rarely clear-cut. Buyers frequently inherit latent exposure through expired permits, undocumented releases, monitoring or reporting failures, and historical operational practices that no longer align with current regulatory expectations. How these issues are identified, evaluated, and disclosed—and to whom—determines whether they remain manageable business risks or escalate into material enforcement actions.

At the federal level, the U.S. Environmental Protection Agency’s *Incentives for Self-Policing: Discovery, Disclosure, Correction and Prevention of Violations (“EPA Audit Policy”)* provides the primary pathway for mitigating penalties and restraining criminal referrals.¹ Complementing that regime, the Department of Justice’s Environmental Crimes Section issued its own revised Corporate Enforcement and Voluntary

Self-Disclosure Policy on March 23, 2026, which governs potential criminal exposure arising from corporate actions, including violations discovered during diligence or in post-closing.^{2,3}

This article explains how these policy frameworks operate specifically in the context of mergers and acquisitions, highlights the decision points that most materially influence deal outcomes, and provides examples of state-level distinctions that can create or destroy value depending on whether they are properly understood and navigated.

The EPA Audit Policy in M&A: Turning Discovered Violations into Deal Certainty

EPA's civil penalty model ordinarily includes two components: gravity-based penalties, which reflect the seriousness of the violation, and economic benefit penalties, designed to recover any financial advantage gained through noncompliance.⁴ Under the Audit Policy, companies may obtain a complete waiver of gravity-based penalties if they meet all nine eligibility conditions.⁵ Even when a violation is not uncovered through a formal environmental audit, EPA can still waive up to 75% of gravity-based penalties.⁶ Although EPA generally reserves the right to recover economic benefit penalties, the Agency may waive them when the economic benefit is insignificant.⁷

In an M&A context, this penalty-mitigation framework directly influences how parties negotiate indemnity caps, survival periods,

purchase-price adjustments, escrow sizing, and post-closing remediation budgets. When violations can be disclosed and resolved under the Audit Policy, either before closing or during early post-closing integration, buyers are often able to transform open-ended environmental exposure into bounded, quantifiable risk—something far easier to account for in valuation models and liability allocations.

The Nine Conditions Through a Deal Lens: Timing, Independence, and Control

Among the nine eligibility conditions in the Audit Policy, three are especially significant in transactions: voluntariness, timing, and independence from government action. The timing element is often the most consequential. EPA requires companies to disclose violations within twenty-one days of discovery,⁸ a clock that frequently begins running during environmental due diligence. Discovery may occur during pre-closing site assessments, post-closing compliance audits, or operational integration activities, but care should be taken to meet the requirements for systematic discovery to preserve the maximum forgiveness. Deal teams should assume that once a violation is sufficiently understood to be recognized as such, the disclosure clock has already begun, regardless of whether the transaction has closed.

Maintaining independence from government action is equally important. To preserve

¹ USEPA, *Incentives for Self Policing (Audit Policy)*, 65 Fed. Reg. 19618 (2000).

² USDOJ, *Corporate Enforcement and Voluntary Self-Disclosure Policy* (2026).

³ USEPA, *State Audit Privilege and Immunity Laws* (https://19january2021snapshot.epa.gov/compliance/state-audit-privilege-and-immunity-laws-self-disclosure-laws-and-policies_.html).

⁴ EPA Civil Penalty Policy, EPA General Enforcement Policy #GM 22.

⁵ Audit Policy, 65 Fed. Reg. at 19621-23.

⁶ Id.

⁷ Id.

⁸ Audit Policy, Condition 2.

eligibility under the Audit Policy, disclosure must occur before the company becomes aware of government inspections, citizen suits, whistleblower complaints, or information requests.⁹ In transactions involving distressed assets or facilities already on regulatory radar, this requirement may necessitate accelerated post-closing audits to protect eligibility.

Criminal Exposure in Transactions: Coordinating EPA and DOJ Strategy

Environmental criminal exposure is among the most disruptive risks in transactional practice, particularly for private equity sponsors, lenders, and public companies. EPA’s Audit Policy states that the Agency will generally refrain from recommending criminal prosecution where violations are voluntarily discovered, disclosed, and corrected in good faith.¹⁰ Although DOJ is not bound by EPA’s position, this significantly reduces referral risk.

DOJ’s own Corporate Enforcement and Voluntary Self-Disclosure Policy, issued on March 23, 2026, provides additional clarity. Under that policy, DOJ will not seek a guilty plea where a company voluntarily self-discloses, fully cooperates, and appropriately remediates the misconduct, absent aggravating factors.¹¹ Notably, the DOJ policy expressly extends its benefits only if the company had no preexisting obligation to disclose the misconduct to the DOJ and the disclosure occurs prior to an imminent threat of disclosure or government investigation.¹² For this reason, M&A counsel must intentionally coordinate their EPA and DOJ strategies. Disclosing to EPA without considering

DOJ implications may leave criminal exposure unresolved, while approaching DOJ alone may undermine civil side penalty mitigation.

New Owner and Post-Acquisition Audits: Federal “Clean Slate” Mechanisms

Recognizing that strict enforcement against inherited violations could discourage remediation, EPA developed the Interim Approach to Applying the Audit Policy to New Owners, which provides enhanced penalty mitigation for violations discovered after acquisition, offers flexibility in disclosure timing, and acknowledges that buyers may have had limited access to the facility before closing.¹³ These features make the policy particularly valuable in carveouts, distressed transactions, cross-border acquisitions, and deals involving legacy industrial operations.

State Audit Privilege and Immunity Laws: Deal-Defining Differences

State law often determines whether environmental audit findings remain confidential diligence materials or become discoverable evidence. For example, Texas’s Environmental, Health, and Safety Audit Privilege Act is considered one of the strongest frameworks in the country. It provides evidentiary privilege for environmental audit reports, immunity from administrative and civil penalties for disclosed

⁹ Audit Policy, Condition 3-4.

¹⁰ 65 Fed. Reg. at 19620.

¹¹ DOJ CEVSD Policy, Appendix B.

¹² Id.

¹³ 73 Fed. Reg. 44991-45006.

violations, and special protections for new owners and acquisition-driven audits.¹⁴

Colorado's regime provides both privilege and penalty immunity but preserves the state's inspection and injunctive authority, making it favorable for buyers who conduct timely correction but less forgiving of delays.¹⁵ Ohio's statute (Ohio Rev. Code §3745.71-2) provides civil penalty immunity—excluding economic benefit recovery—while requiring highly structured and formalized disclosure.¹⁶

By contrast, Illinois repealed its audit-privilege law in 2005, leaving audit findings unprotected by statute and shifting transactional protection to traditional privilege doctrines such as the attorney-client privilege and work product immunity.¹⁷

RWI as a Complement to Environmental Self-Disclosure

Representations and Warranties Insurance (RWI) has become standard in deals involving regulated assets, but it functions primarily as coverage for breaches of representation—not for regulatory liability itself. RWI coverage generally applies only if the seller makes an environmental representation, that representation is breached, and the breach results in a covered loss as defined by the policy. Most RWI policies exclude known environmental conditions, matters disclosed in schedules, issues subject to specific indemnities, and often fines and penalties.

These exclusions create a direct interface with self-disclosure policy. Once a violation is disclosed to regulators, it becomes a “known issue” and is generally excluded from RWI

coverage. Conversely, withholding disclosure may preserve theoretical insurance coverage but also increase regulatory enforcement risk and compromise the benefits available under EPA and DOJ policies. In practice, RWI is designed to cover unknown historical risks—not known noncompliance that buyers intend to correct after closing.

RWI is therefore most effective when paired with regulatory mitigation strategies, contractual risk allocation, and—where appropriate—Pollution Legal Liability (PLL) insurance. Carriers place significant weight on the quality of environmental due diligence, including the robustness of Phase I environmental site assessments, compliance audits, and environmental management system reviews. In recent years, the RWI market has tightened around PFAS, emerging contaminants, and high-risk industrial sectors, making supplemental PLL policies more common in transactions involving significant environmental exposure.

Privilege Management in Deals

Federal law does not recognize a general environmental audit privilege, and EPA has repeatedly clarified that the Audit Policy does not create evidentiary protections. Disclosure of privileged state audit materials to federal regulators may also waive privilege under state law, and several states have narrowed their privilege statutes in response to EPA concerns. For this reason, deal teams frequently conduct audits under counsel's direction, segregate legal analysis from factual findings, label privileged materials appropriately, and carefully sequence state and federal disclosures to minimize the risk of waiving protections.

¹⁴ Texas Health & Safety Code Title 13, Chapter 1101.

¹⁵ Colorado Dept. of Public Health & Environment Policy Number EP-02 (2023).

¹⁶ Ohio Rev. Code § 3745.71-2.

¹⁷ Ill. Comp. Stat. Ann. § 415-5/52.2 (repealed Aug. 12, 2005).

Conclusion

Environmental risk in transactions is rarely eliminated; instead, it is apportioned, priced, and strategically managed. Effective transactional practice requires integrating disclosure planning directly into diligence, coordinating EPA and DOJ engagement at the outset, leveraging state privilege regimes where available, assuming disclosure decisions cannot be undone, and ensuring that environmental audits are treated not merely as engineering exercises but as legal tools. Mastery of these federal and state policies has become essential to delivering deal certainty in regulated industries.

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