Sierra Club v. Costle

Regulatory Oversight Wins in Court

Michael Sohn and Robert Litan

While the Supreme Court's decision in *Cotton Dust* has dominated recent regulatory news, a lower court's decision in *Sierra Club* v. *Costle*, issued several weeks earlier, is likely to have a far larger impact on executive branch and congressional efforts to reform the regulatory process.

Sierra Club involved the Environmental Protection Agency's "scrubber" regulation, which requires that coal- or oil-fired electric utilities install controls to reduce emissions by the same percentage, with little regard to the "cleanness" or "dirtiness" of the fuels being used. The court upheld the substance of that regulation and, at the same time, resolved procedural questions of equal, if not greater, importance. EPA's scrubber rule was issued in July 1979, after more than two years of study and consultation involving not only the agency, but also officials from the Department of Energy, the Department of Interior, and the White House. There were also consultations, after the comment period had closed, between EPA and various interest group representatives, as well as then-majority leader Senator Robert Byrd (Democrat, West Virginia) and the President himself. In a thoughtful and articulate opinion by Judge Patricia Wald, the U.S. Court of Appeals for the District of Columbia Circuit addressed the Sierra Club's challenge to the legitimacy of those post–comment period meetings. Not only did it reject that challenge, but it gave a ringing endorsement to the efforts of the President and his advisers to monitor and provide input to the decisions made by the "single mission" regulatory agencies.

Because of the issues involved and the thorough treatment given them by the court, *Sierra Club* v. *Costle* has important implications for the regulatory oversight procedures recently established by the Reagan administration. The opinion provides timely judicial support for the concept of Office of Management and Budget (OMB) oversight of executive branch regulatory agencies under Executive Order 12291. It also contains observations about the informal rulemaking process in general that deserve to be explored by all those interested in how regulations are developed.

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The Issues: Who Should Pay to "Clean" the Air?

In the long history of the rulemaking at issue in *Sierra Club* and of the statute that it implemented, a classic question recurs: who shall pay to clean the air?

The national commitment to the goal of clean air was made in 1970 when Congress amended the Clean Air Act to require that EPA set national ambient air quality standards for major pollutants to "protect the public health," and that the states enforce the standards by setting limitations on emissions. However, while mandating the goal of clean air—which was to be attained regardless of costs—Congress also displayed sensitivity to the distributional question of who would bear those costs. The members recognized that national health-based standards could have major effects in limiting economic growth in states where ambient air quality was poor. They recognized, too, that the system would permit states having relatively cleaner air to attract industry from other states by setting less stringent emission limits.

To mitigate these distributional concerns, Congress included in the 1970 amendments a requirement that EPA set uniform performance standards for all major *new* sources of emissions across the country, but left the politically tougher problem of emissions from *existing* sources to the states. The standards were to reflect what the best system of adequately demonstrated technology could achieve. In December 1971, EPA implemented these instructions by issuing its new source performance standard (NSPS) for large fossil-fired electricity generating plants, a major source of sulfur dioxide (SO_2) emissions. The standard limited SO_2 emissions from these plants to 1.2 pounds per million British thermal units (MBtus) of heat content of the fuel. This 1971 standard—which Congress required of EPA in order to solve one set of distributional concerns—soon created an entirely different distributional problem.

The predominant fossil fuel used in generating plants was then, and still is, coal. And, in general, coal from the eastern states (notably West Virginia) and many midwestern states as well, has a much higher sulfur content, and therefore produces greater amounts of SO_2, than coal mined in the West. At the time, two technologies were available for controlling SO_2 emissions from coal-fired plants: physical "washing" of the coal before it is burned and the more expensive process of fluegas desulfurization ("scrubbing"), an embryonic system for removing sulfur from the gas emitted as the coal is burned. It did not take utility managements long, however, to discover a third and simpler way. Because the 1971 NSPS was a standard of performance, measured in terms of SO_2 emissions from a smokestack, it could be met simply by burning low-sulfur western coal, thus avoiding the cost of installing pollution control technology. This, of course, created a new interstate rivalry, with the eastern coal states (primarily West Virginia) complaining that they were losing coal-related sales and jobs to the West.

Congress addressed this new distributional problem in the 1977 amendments to the Clean Air Act by instructing EPA to supplement its emissions ceiling for power plants with a percentage reduction requirement. The exact numerical percentage was left for EPA to fill in; but, as "guidance," Congress directed that it be based on the

> best technological system of continued emission reduction which (*taking into consideration the cost of achieving such emission reduction, and any nonair quality health and environmental impact and energy requirements*) the Administrator determines has been adequately demonstrated [section 111(a), emphasis added].

This provision was the product of an alliance between eastern coal supporters, who argued that their states should not bear the primary burden for "paying for clean air," and environmental groups, who wanted low-sulfur coal to be "scrubbed" to provide cleaner air even where the use of that coal brought emissions below the 1971 performance standard. In any event, the distributional issue was not yet fully resolved since the amendments directed EPA to fill in the exact percentage, taking cost and other factors into account.

The agency addressed these matters in a proposal issued in September 1978. That proposal retained the 1971 ceiling of 1.2 lb./MBtu SO_2, but added a requirement that 85 percent of the potential uncontrolled sulfur emissions from coal (measured over twenty-four hours) would have to be removed. (This requirement

would not apply, however, if SO_2 emissions were below 0.2 lb./MBtu.) Also, in response to pressure primarily from Department of Energy officials and White House economists—who were concerned that a uniform across-the-board percentage (or "full scrubbing") requirement would not be cost-effective—EPA's proposal asked for comment on "sliding scale" alternatives. Under a sliding scale, the percentage of uncontrolled sulfur that would have to be removed would decline with the sulfur content of the coal used.

EPA's proposal generated enormous interest—reflected in roughly 1,400 public comments, 50 agency meetings and substantive telephone conversations with the public, and 120 studies submitted to the public docket. The proposal also was important enough to merit a lengthy economic analysis from the Regulatory Analysis Review Group (RARG), President Carter's interagency group that watched over executive branch regulatory activities. RARG's primary concern was that by focusing on the *means* for reducing emissions rather than on the *level* of emissions, EPA's full scrubbing requirement would impose unnecessary costs on utilities without achieving corresponding environmental benefits. Ironically, RARG pointed out, the proposed rule would exacerbate the SO_2 problem in some areas, because the expense of installing scrubbers in new generating plants would discourage utilities from replacing their older and "dirtier" plants with newer and "cleaner" plants.

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RARG's analysis, as well as the comments and advice that came from other quarters, was greatly facilitated by EPA's use of a relatively sophisticated economic model capable of projecting under a wide range of assumptions the economic, energy, and emissions impacts (nationally and regionally) of alternative regulatory approaches through the year 1995. The model was also put to great use by a variety of groups after the public comment period closed on January 15, 1979. Over the next weeks, EPA officials discussed their findings with officials of other executive branch agencies and the White House. The pace of such meetings picked up in the spring. On April 5, EPA officials met with representatives from the National Coal Association (NCA), the Environmental Defense Fund, and others to discuss NCA's claim that large coal reserves, mainly in the East, could be rendered valueless if EPA decided to lower the emissions ceiling in addition to requiring a percentage reduction. On April 23, EPA Administrator Douglas Costle met with NCA representatives, Senator Byrd, and presidential adviser Stuart Eizenstat. Six days later President Carter and his advisers met with EPA officials. Finally, on May 2, EPA officials met again with Senator Byrd and representatives of the NCA. Summaries of all these meetings —except the one with the President—and of other staff-level briefings that occurred during the same period were placed in EPA's rulemaking record.

The final rule, published in the *Federal Register* on June 11, 1979, retreated from full scrubbing—but just barely. Specifically, it adopted a percentage reduction requirement for SO_2 of 90 percent averaged over a thirty-day period (equal to the proposed 85 percent averaged over twenty-four hours) if emissions remain above 0.6 lb./MBtu, and of 70 percent if emissions fall below 0.6 lb./MBtu. The 70 percent figure for lower-sulfur coals was settled on late in the rulemaking to encourage the development and use of "dry scrubbing"—a cheaper approach than "wet scrubbing," but one that had not yet been able to achieve 90 percent removal.

EPA's decision was challenged from all sides. Environmental groups claimed, among other things, that the agency had unlawfully abandoned full scrubbing and that EPA's extensive contacts with outside parties, other government officials, and legislators and their staffs ("ex parte contacts") were unlawful. A number of electric utilities challenged the 90 percent removal requirement as too stringent. Other utilities and the National Coal Association also intervened to support different parts of the rule.

The Court Decision

The D.C. circuit court upheld EPA's final rule in a 253-page opinion issued on April 29. The court's substantive holdings involved both legal and factual issues. First, the opinion construed section 111(a) broadly as permitting EPA to issue a variable percentage reduction requirement. The Sierra Club had argued that the section's legislative history required EPA to set a uniform reduction requirement for all types of coal. The court rejected that argument, relying heavily on statutory language that expressly directed EPA to take such factors as cost and energy requirements into account in setting the standard.

Second, the opinion rejected the Sierra Club's contention that, primarily because of the unreliability of EPA's model, the variable percentage requirement was unsupported by evidence in the record. Although the court recognized that the model was "at best imperfect and subject to manipulation," it refused to agree that, *as a matter of law,* EPA had erred in relying on it to make projections as far as fifteen years into the future. Indeed, the court observed that "computer modeling is a useful and often essential tool for performing the Herculean labors Congress imposed on the EPA in the Clean Air Act." In reaching this conclusion it emphasized that EPA had invited the public to comment on the model and its underlying assumptions, had involved other government agencies and White House economists in the modeling effort, and had admitted the model's limitations:

> The safety valves in the use of such sophisticated methodology are the requirement of public exposure of the assumptions and data incorporated into the analysis and the acceptance and consideration of public comments, the admission of uncertainties where they exist, and the insistence that ultimate responsibility for the policy decision remains with the agency rather than the computer.

Third, the court examined utility industry claims that the 90 percent reduction requirement was not adequately substantiated. In a remarkably detailed thirty-page discussion, Judge Wald waded through a series of statistical and technological arguments and counterarguments concerning the peak performance and reliability of scrubbing systems (by themselves or together with coal washing) before ultimately rejecting the industry contention that the 90 percent standard could not be met.

The procedural challenges to EPA's final rule fared even worse. The court rejected the claims that meetings between EPA decision makers and other government officials following the close of the public comment period were legally impermissible or that a notation of such meetings must always be placed in the rulemaking docket. It left for another day the question whether a rulemaking would be subject to judicial reversal when executive branch officials outside an agency serve as "conduits" for conveying the "off-the-record" views of private parties to agency decision makers, stating that the record did not support the claim that unrecorded conduit communications had occurred.

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Implications for Executive Order 12291

The *Sierra Club* decision has obvious application to President Reagan's effort to centralize control over executive branch regulatory activities. The centerpiece of this effort, Executive Order 12291 of February 1981, grants OMB unprecedented powers over the development of new agency regulations. Most significantly, the order gives OMB the authority to "pre-clear" both major regulatory proposals and final decisions. It also upgrades President Carter's "regulatory analysis" provisions to a formal cost-benefit requirement—that is, agencies must demonstrate, to the extent permitted by law, that the potential benefits of their proposals outweigh the potential costs.

To some extent, the Reagan executive order can be viewed as institutionalizing, for *every* major executive branch rulemaking, the procedure actually followed in EPA's rulemaking on new source performance standards. Thus, just as White House economists and other executive branch officials met with EPA

officials before, during, and after the public comment period to discuss the issues present in the scrubber rulemaking, the Reagan order contemplates the involvement of OMB economists at all of these stages—but on a *routine* rather than ad hoc basis.

There are, however, important differences between the scrubber proceeding and the new Reagan procedures. In the former, EPA voluntarily received advice from officials outside the agency; the new executive order mandates that EPA receive such advice and empowers OMB to hold up the issuance of regulatory proposals and final decisions until the consultation process has been completed. Moreover, it is not yet clear how the Reagan administration plans to deal with the "conduit" problem, on which the court did not rule in its scrubber decision. And finally, the executive order imposes upon the agencies a cost-benefit analysis obligation that was not at issue in *Sierra Club*.

Morton Rosenberg of the Library of Congress recently cited these differences, among others, as reasons to be concerned that the new executive order is legally vulnerable. In a lengthy and well-documented report, he argues that the concentration of such power within OMB *may* displace "the discretionary authority of agency decisionmakers." In addition, he points out that the institutionalization of a review process in OMB heightens the risk that personnel from outside the agency could become "conduits" for off-the-record information, thereby depriving outside parties of their right to respond and hindering judicial review of agency decisions.

While not precisely addressing these issues, the *Sierra Club* opinion sheds some light on all of them:

(1) White House Oversight. The decision's clearest message concerns the role of executive branch officials outside the rulemaking agency in the rulemaking process. The court found such involvement to be legally permissible and in fact conducive to sounder policy judgments:

> The authority of the President to control and supervise executive policymaking is derived from the Constitution; the desirability of such control is demonstrable from the practical realities of administrative rulemaking. Regulations such as those involved here demand a careful weighing of cost, environmental, and energy considerations. They also have implications for national economic policy. *Our form of government simply could not function effectively or rationally if key executive policymakers were isolated from each other and from the Chief Executive. Single mission agencies do not always have the answers to complex regulatory problems. An overworked administrator exposed on a 24-hour basis to a dedicated but zealous staff needs to know the arguments and ideas of policymakers in other agencies as well as in the White House* [emphasis added].

Implicitly recognizing the essentially legislative or "policymaking" character of the informal rulemaking proceeding that was before her, Judge Wald concluded that, in the absence of a congressional direction to the contrary, courts should not erect barriers to frank input at the decision-making stage from all parties in the executive branch who may have something to contribute.

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The scrubber rulemaking is a clear example of how informal rulemakings are suffused with issues of an intensely political character. The battle lines on the scrubber issue were drawn in Congress, first, between high-growth and low-growth states and, later, between eastern and western coal-producing states. The 1977 amendments passed the latter controversy on to EPA to resolve. Once there, the computers whirred and the analysts analyzed, but in the end the most important question the agency had to decide was political: who should foot the bill for cleaner air—consumers or stockholders, in the East or in the West—and how large should that bill be?

The D.C. circuit court properly recognizes an important distinction between formal rulemakings and adjudications on the one hand and informal rulemakings on the other. Whereas the former typically involve highly particu-

larized issues and a limited number of private parties, the latter typically present broad policy issues involving many individuals and groups, are highly "political" in nature, and require the agency decision maker not only to reach findings of fact, but also to choose among competing interest groups and values. Thus the informal rulemaking is seen as representing a delegation of an essentially legislative function—"filling in the blanks" left in a statute because Congress either did not have time to do so or chose to pass the issue to the agency in order not to risk a consensus in favor of legislation. It is this view of informal rulemaking that prompted the court to adopt a political or legislative, rather than a judicial, model for judging the propriety of agency informal rulemaking procedures:

> Under our system of government, the very legitimacy of general policymaking performed by unelected administrators depends in no small part upon the openness, accessibility, and amenability of these officials to the needs and ideas of the public from whom their ultimate authority derives, and upon whom their commands must fall. As judges we are insulated from these pressures because of the nature of the judicial process in which we participate; but we must refrain from the easy temptation to look askance at all face-to-face lobbying efforts, regardless of the forum in which they occur, merely because we see them as inappropriate in the judicial context.

Having decided that the agency decision maker should not be isolated from others in the executive branch as he or she struggles to reach a sound policy conclusion, the court then all but closed the door to a judicially imposed requirement that the substance of these intragovernmental "policy sessions" be disclosed. While the undocketed meeting primarily at issue in *Sierra Club* involved a presidential meeting, the broad language of the opinion would certainly appear to cover all White House contacts with executive branch agencies. Thus, so long as agencies do not attempt to base their decisions on off-the-record information derived during such meetings, the courts can perform their reviewing function and, in the court's words, do not need to "know the details of every White House contact," including a presidential one. The courts will ascertain whether the agency decision has the requisite factual support in the record, but will not impose requirements designed to preclude the possibility that "undisclosed Presidential prodding" led to a result that is factually based on the record, but different from what the agency head would otherwise have chosen. As the court states, "we do not believe that Congress intended that the courts convert informal rulemakings into a rarefied technocratic process, unaffected by political considerations or the presence of Presidential power."

What, then, of the distinction between Executive Order 12291 and the EPA process approved in *Sierra Club*—the fact the order mandates extra-agency consultation and authorizes OMB to delay issuance of a rule until the process has been completed? It seems to us doubtful that the D.C. court would consider this a distinction with a difference. When it approved "the presence of a Presidential power," surely it was not so naive as to imply that this presence was to be felt only when the agency itself so desired. Similarly, when it decried the "isolation" of "single-mission agencies" that a nonconsultation rule would produce, it could not have meant to imply that self-imposed isolation would be satisfactory. In short, it seems most likely that the court would view the executive order's requirement of extra-agency consultation, and its adoption of procedures to ensure it, to be within the President's powers of managing the administration of the government.

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Of course, *Sierra Club* did not address a situation where the President, or an OMB director acting pursuant to an executive order, *instructs* an executive branch agency to reach a decision that it would not otherwise have taken, especially where, as in the typical regulatory statute, the agency is vested with the decision-

making authority by Congress. Such a case would test the outer reaches of the President's powers under Article II to "see that the laws are faithfully executed." Yet as a practical matter, such cases may never arise. An agency head is unlikely to risk presidential displeasure by openly bucking a "strongly expressed presidential preference"—or even one from OMB, provided it is supported by the President. Moreover, the judicial reticence to explore the contents of intra-executive branch deliberations exhibited in *Sierra Club* makes it unlikely that the "hard cases" will ever see the light of day.

(2) The "Conduit" Problem. In contrast to its forthrightness in resolving many uncertainties about the legal status of contacts between White House and agency officials, *Sierra Club* refers to, but then skirts, the important "conduit" problem. In particular, the opinion contains themes from two opposing views of informal rulemaking, views drawn from the legislative and judicial contexts, respectively, that leave some doubt as to how the conduit problem will eventually be resolved. Thus, the court notes that while informal rulemaking has an essentially legislative or policy-making character which may justify or even require the accessibility of agency decision makers, we should not lose sight of the fact that it is *not* legislation pure and simple and that lines must be drawn which do not apply when Congress itself is at work.

Informal rulemaking is a method by which Congress delegates the task of solving complex and often technical problems to "experts" rather than deciding them itself. Even in informal rulemaking, Congress has somewhat formalized the methods by which the expert decision maker acquires information, by requiring agencies to provide notice of proposed rulemakings and opportunities for the public to comment on the proposals. Increasingly, in fact, Congress has required the use of additional fact-gathering procedures, including oral hearings, rebuttals, and limited cross-examination. Both the Administrative Procedure Act and these so-called hybrid procedures are designed to ensure that affected persons have a reasonable and fair opportunity to participate in the process and that courts have an adequate basis for reviewing the agency's faithfulness to its statutory mandate. Those related notions—the right to participate and the need for an adequate record—have implications that are foreign to a purely "legislative" or "political" model of rulemaking. For example, if one were to judge informal rulemaking procedures solely by legislative norms, there would not be the concern, expressed recently by the Administrative Conference of the United States, that agencies avoid

> *any possibility* that intragovernmental communications from outside the rulemaking agency might serve as undisclosed or inadvertent conduits for new material factual information, and with providing adequate opportunities for other participants to respond to material factual information that is introduced [ACUS Preamble to Recommendation 80-6].

On June 13, 1981, OMB Director David Stockman sent a memo to executive branch agency heads stating that OMB's procedures "will be consistent with the holding and policies discussed in *Sierra Club*," and that where OMB "receives or develops" factual material that it believes should be considered by a rulemaking agency, it will identify such material as appropriate for inclusion in the rulemaking record. These instructions are far from crystal clear, however. It may often be difficult to distinguish between factual and policy communications from outsiders. Moreover, it is not certain that this new practice applies to oral as well as written communications.

Administration officials would do well to note Judge Wald's reference to the advice that the Department of Justice gave to officials of the Council of Economic Advisers (CEA) during the Department of Interior's strip-mining rulemaking: "summarize and place in rulemaking records a compilation of *all* written and oral comments they receive relevant to particular proceedings" (emphasis added). Indeed, it was largely because CEA and Interior followed this advice that the D.C. district court rebuffed a procedural challenge to the strip-mining rules in 1979 (*In re Permanent Surface Mining Regulation Litigation*). In an article relied on heavily by the *Sierra Club* court, Dean Paul Verkuil of Tulane Law School suggested that the courts should adopt the Justice Department's recommendations to CEA (*Columbia Law Review*, June 1980). The court did not need to address

this question on the facts before it, because there was no reason to believe that the recommendation had not been followed in the scrubber proceeding or that unrecorded conduit communications had even taken place.

The ambiguities in OMB's June 13 memorandum concerning the definition of factual information and the coverage of oral conversations clearly increase the risk that, in the future, a court will be faced with a case in which unrecorded conduit communications did occur and no policy was in place to record them. From a purely legal perspective, OMB could avoid this risk by automatically passing on to the agency *any* written materials it receives and by logging and docketing all conversations with outside parties. Beyond the legal issue posed by the conduit problem, administration officials might be well advised, as a political matter, to do their own "cost-benefit analysis" in this sensitive area. They might find that the political benefits in terms of perceived fairness of the decision-making process outweigh the administrative costs of dictating and docketing summaries of meetings with nongovernmental officials on subjects of announced rulemakings.

(3) Cost-Benefit Analysis. The third major feature of the executive order that was not part of the process approved by the court in *Sierra Club* is the requirement that agencies conduct "regulatory impact analyses" identifying costs, benefits, and alternatives to their proposals. These analyses in effect form the agenda for consultation with OMB—and OMB has authority to require an agency to extend or supplement its analysis.

In *Sierra Club*, EPA conducted its own regulatory impact analysis; but the fact is that it was not instructed by the President or by OMB as to whether and how to do so. The issue presented by the executive order is whether the President has the power to direct, not the agency's decision, but the manner in which that decision is to be considered.

The answer, of course, is surely not, if that manner includes consideration of factors which the applicable statute forbids, or the ignoring of factors which the applicable statute requires. But the executive order takes account of this limitation by specifying that its requirements do not apply where statutes provide otherwise. The question, therefore, comes down to this: where the agency's statute neither explicitly requires nor explicitly forbids cost-benefit analysis, can the President require it? *Sierra Club* does not address this issue, but the answer would appear to be yes. The cost-benefit requirements of the new executive order do not mandate any particular result. Rather, they specify an analytical *process* to be employed in making regulatory decisions. And, as long as cost-benefit analysis is not precluded by applicable statute, mandating that process would appear to be well within the President's Article II power to supervise and guide his appointees in the execution of laws adopted by Congress.

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Effects of Pending Legislation

The *Sierra Club* case is certain to be of continuing importance for implementation of the President's regulatory reform program, whether or not pending regulatory reform bills are adopted. In their present form, the two principal proposals (S. 1080 and H.R. 746) would solve two of the three problems unaddressed by *Sierra Club*: they would specifically require cost-benefit analysis by law, and they would give the President (or OMB) a role in overseeing the manner in which it is conducted. They leave unaddressed, however, the third uncertainty—the problem of conduit contacts.

Finally, and most important, the bills also leave unaddressed the basic and most significant issue raised in *Sierra Club*: whether the President and his designees are permitted to have some influence not merely upon the process, but upon the very substance of agency decisions. In this regard, the *Sierra Club* case remains an important victory for advocates of a stronger presidential role in the rulemaking process—but only in one battle, and in a war that is sure to continue. ■