

Congress of the United States
U.S. House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-6515

To: Members, Committee on Small Business
From: Committee Staff
Date: July 28, 2014
Re: Hearing: "Regulatory Overreach: Is EPA Meeting Its Small Business Obligations?"

On Wednesday, July 30, 2014, at 1:00 pm in Room 2360 of the Rayburn House Office Building, the Committee on Small Business will meet for the purpose of examining whether the Environmental Protection Agency (EPA) is complying with the Regulatory Flexibility Act (RFA).¹ This year, the EPA has proposed rules to reduce greenhouse gas (GHG) emissions from power plants pursuant to the President's Climate Action Plan² and recently issued a proposed rule that would change the scope of waters subject to regulation under the Clean Water Act.

I. Environmental Statutes Administered by EPA

The EPA administers several environmental statutes including the Clean Air Act and the Clean Water Act (collectively, the "Acts"). Before discussing the regulatory proposals and the EPA's compliance with the RFA, a brief overview of the relevant provisions of the Acts is necessary.

A. The Clean Air Act (CAA)³

In 1970, Congress enacted the CAA "to protect and enhance the quality of the Nation's air resources."⁴ The Act regulates both stationary and mobile sources of air pollution through a complex interrelated series of actions by EPA and the states.⁵

Title I provides the basic framework for the regulation of air pollutants in the United States.⁶ The EPA is authorized to establish emissions limitations, what are known as "new source performance standards" (NSPSs), for new, modified and reconstructed "stationary sources" (buildings, structures, facilities or installations) that in the EPA Administrator's judgment cause or contribute significantly to air pollution.⁷

¹ 5 U.S.C. §§ 601-12.

² EXECUTIVE OFFICE OF THE PRESIDENT, THE WHITE HOUSE, THE PRESIDENT'S CLIMATE ACTION PLAN 6 (2013) [hereinafter Climate Action Plan], available at <http://www.whitehouse.gov/share/climate-action-plan>. The President also issued a memorandum to the EPA Administrator that laid out a specific rulemaking time table. Memorandum of June 25, 2013, Power Sector Carbon Pollution Standards, 78 Fed. Reg. 39,535 (July 1, 2013).

³ 42 U.S.C. §§ 7401-7671q.

⁴ 42 U.S.C. § 7401(b)(1).

⁵ K. BRICKLEY, ENVIRONMENTAL CRIME 146 (2008).

⁶ The CAA has six titles but for purposes of this memo only Title I, and in particular § 111, is relevant to the establishment of GHG emission standards for power plants.

⁷ 42 U.S.C. § 7411(b). The EPA may distinguish among classes, types and sizes of sources. *Id.* It has set NSPSs for over 70 categories and subcategories of sources including: petroleum refineries; new residential wood heaters; and municipal solid waste landfills. See 40 C.F.R. Pt. 60. A standard of performance is the "best system of emission reduction" that has been "adequately demonstrated" and is "achievable," taking into account the economic costs, any nonair quality health and environmental impacts, and energy requirements. 42 U.S.C. § 7411(a)(1).

Performance standards for existing sources also may be established. However, EPA does not directly establish standards for existing sources; instead, the EPA is authorized to establish a “procedure” (commonly referred to as “emission guidelines”) for states to develop state plans to set performance standards for existing sources.⁸

B. The Clean Water Act (CWA)⁹

The objective of the CWA is to “restore and maintain the chemical, physical and biological integrity of the Nation’s waters”¹⁰ and is accomplished by eliminating “the discharge of pollutants into the navigable waters.”¹¹ Thus, the regulatory paradigm of the CWA rests on the definition of navigable waters. “Navigable waters” are defined under the CWA as “the waters of the United States, including the territorial seas.”¹² Once a body of water has been determined to be a water of the United States, the permitting requirements of the CWA are triggered; pollutants¹³ and dredged and fill materials¹⁴ cannot be discharged without a permit. While the CWA is generally administered by the EPA,¹⁵ the EPA and United States Army Corps of Engineers (Corps) jointly administer and enforce the Section 404 Program.¹⁶

II. EPA Rulemakings in 2014

A. Proposed Rules – Power Plants

The EPA has issued proposed rules to curb GHG emissions, specifically carbon dioxide (CO₂), from power plants as directed by the President in his Climate Action Plan.¹⁷ On January 8, 2014, the proposed rule for new power plants (as a NSPS) was published in the Federal Register, which would establish separate CO₂ emission standards for new coal- and natural gas-fired power plants.¹⁸ The standard for coal plants is based on partial implementation of carbon capture and storage (CCS) technology.¹⁹ While a discussion of CCS is beyond the scope of this memorandum, concerns have been raised that CCS has not

⁸ *Id.* at § 7411(d).

⁹ 33 U.S.C. §§ 1251-1387.

¹⁰ *Id.* at § 1251(a).

¹¹ *Id.* at § 1251(a)(1).

¹² *Id.* at § 1362(7). A brief overview of the two most recent Supreme Court decisions that have dealt with the scope of CWA jurisdiction can be found in the Committee on Small Business’s May 29, 2014 hearing memorandum, available at http://smallbusiness.house.gov/uploadedfiles/5-29-2014_revised_hearing_memo.pdf.

¹³ *Id.* at §§ 1311(a), 1342. Pollutants from point sources may not be discharged into a water of the United States unless the discharger has a permit issued pursuant to § 402 of the CWA (colloquially known as the “Section 402 Program”). *Id.* at § 1362(12). “Pollutant” includes sewage, garbage, chemical wastes, biological materials, discarded equipment, sand, cellar dirt and rock. *Id.* at § 1362(6). “Point source” is defined to mean “any discernible, confined and discrete conveyance” and includes pipes and ditches. *Id.* at § 1362(14).

¹⁴ *Id.* at §§ 1311(a), 1344. The permit program for dredged or fill activities is referred to as the “Section 404 Program.” “Dredged material” is material that is dredged or excavated; “fill material” is material that is placed in a “water of the United States” including dirt, rock, soil and clay. 33 C.F.R. § 323.2(c), (e).

¹⁵ *Id.* at § 1251(d).

¹⁶ *Id.* at § 1344. States may operate their own Section 402 and 404 permit programs. *Id.* at §§ 1342(b), 1344(g).

¹⁷ Until recently, EPA did not believe that it had the authority to regulate GHGs under the CAA. However, that changed with the Supreme Court’s decision in *Massachusetts v. EPA*, 549 U.S. 497 (2007). A brief explanation of the Court’s decision and the EPA’s subsequent actions can be found in the Committee on Small Business’s July 15, 2013 hearing memo, available at <http://smallbusiness.house.gov/calendar/eventsingle.aspx?EventID=340255>.

¹⁸ Standards of Performance for Greenhouse Gas Emissions From New Stationary Sources: Electric Utility Generating Units, 79 Fed. Reg. 1430 (Jan. 8, 2014) [hereinafter New Power Plant Rule]. Power plants are referred to as “electric utility generating units” by the EPA. This memorandum will adopt the more colloquial terminology.

¹⁹ *Id.* CCS is technology that involves capturing, compressing, transporting and storing CO₂ in deep underground rock formations. <http://www.globalccsinstitute.com/content/what-ccs>.

been adequately demonstrated nor can it be installed at a reasonable cost.²⁰ Since the proposed CO₂ emission limits cannot be achieved by coal-fired power plants without CCS, critics charge that the New Power Plant Rule effectively bans construction of new coal-fired power plants.²¹ Yet, the EPA projects that the rule will result in no costs or benefits because it expects that companies will build new power plants that comply with the proposed rule's requirements even in the absence of the proposal.²²

On June 18, 2014, the EPA proposed a rule to establish CO₂ emission guidelines for existing power plants.²³ The EPA proposes state-specific emission rate-based CO₂ goals and guidelines for states to follow in developing plans for EPA's approval to achieve the goals.²⁴ The goals were determined by using four measures that are referred to as "building blocks." The building blocks are: 1) making coal-fired power plants more efficient; 2) shifting power generation to natural gas-fired power plants; 3) increasing the power generated by nuclear power plants and renewable facilities; and 4) using demand-side energy efficiency efforts to reduce electricity usage.²⁵ States are expected to use a combination of the building blocks to achieve their CO₂ goals.²⁶ The EPA estimates that the annual compliance costs for the Existing Power Plant Rule will be between \$5.4 to \$7.4 billion in 2020 and \$7.3 to \$8.8 billion in 2030.²⁷ Electricity costs are projected to increase by 6 to 7 percent in 2020 and 3 percent in 2030.²⁸

B. Proposed Rule – Definition of "Waters of the United States"

The EPA and Corps (collectively, the "agencies") have proposed a rule that would revise the definition of "waters of the United States" for all sections of the CWA.²⁹ While the WOTUS Rule retains some of the existing regulation's structure, it asserts categorical jurisdiction over waters that previously were subject to case-by-case determinations and defines certain terms for the first time. For example, the agencies are asserting jurisdiction over "adjacent waters" for the first time and "tributary," "neighboring" (a term used in the definition of "adjacent"), and "significant nexus" are defined for the first time. Under the WOTUS

²⁰ Henry Fountain, *Corralling Carbon Before It Belches From Stack*, N.Y. TIMES, July 22, 2014, at A1. Retrofitting one existing coal-fired power plant in Saskatchewan with CCS will cost \$1.2 billion and the cost building a new power plant in Kemper County, Mississippi with CCS has swelled to \$5.5 billion. *Id.*

²¹ Andrea Vittorio, *EPA's Carbon Limits for New Power Plants Must Be 'Grounded in Reality,' Industry Says*, BLOOMBERG BNA, May 13, 2014, available at <http://www.bna.com/epas-carbon-limits-n17179890410/>.

²² EPA, REGULATORY IMPACT ANALYSIS FOR THE PROPOSED STANDARDS OF PERFORMANCE FOR GREENHOUSE GAS EMISSIONS FOR NEW STATIONARY SOURCES: ELECTRIC UTILITY GENERATING UNITS 5-54 (2013).

²³ Carbon Pollution Emission Guidelines for Existing Stationary Sources: Electric Utility Generating Units, 79 Fed. Reg. 34,830 (June 18, 2014) [hereinafter Existing Power Plant Rule]. Simultaneously, the EPA issued a proposed rule for modified and reconstructed power plants. Carbon Pollution Standards for Modified and Reconstructed Stationary Sources: Electric Utility Generating Units, 79 Fed. Reg. 34,960 (June 18, 2014).

²⁴ Existing Power Plant Rule, 79 Fed. Reg. at 34,833. If a state does not submit a plan or the plan is not approved by the EPA, the EPA will develop a federal plan for the state. *Id.* at 34,951; see 42 U.S.C. § 7411(d)(2) (authorizing the EPA to develop a plan if a state does not).

²⁵ Questions have been raised concerning the legality of the proposed rule, including whether the EPA's statutory authority allows it to base its "best system of emission reduction" on CO₂ reductions that would occur at sources outside of the regulated sources. GRANT Y. NAKAYAMA, JEFFREY BOSSERT CLARK AND ILANA SALTZBART, KIRKLAND & ELLIS LLP, *EPA'S CONTINUED REGULATORY BARRAGE ON FOSSIL FUEL-FIRED ELECTRIC GENERATION 3-4* (2014), available at http://www.kirkland.com/siteFiles/Publications/Alert_06102014.pdf.

²⁶ Existing Power Plant Rule, 79 Fed. Reg. at 34,859.

²⁷ EPA, REGULATORY IMPACT ANALYSIS FOR THE PROPOSED CARBON POLLUTION GUIDELINES FOR EXISTING POWER PLANTS AND EMISSION STANDARDS FOR MODIFIED AND RECONSTRUCTED POWER PLANTS ES-7 (2014).

²⁸ *Id.* at ES-24.

²⁹ Definition of "Waters of the United States" Under the Clean Water Act, 79 Fed. Reg. 22,188 (Apr. 21, 2014) [hereinafter WOTUS Rule]. A more detailed description of the WOTUS Rule and its potential effects on small businesses can be found in the Committee on Small Business's May 29, 2014 hearing memorandum, available at http://smallbusiness.house.gov/uploadedfiles/5-29-2014_revised_hearing_memo.pdf.

Rule, the following categories of water fall within the parameters of the CWA: 1) traditional navigable waters; 2) interstate waters and wetlands; 3) the territorial seas; 4) impoundments of the first three categories and tributaries; 5) tributaries of the first four categories; and 6) waters and wetlands adjacent to the first five categories.³⁰ “Other waters” (those not set out in the aforementioned six categories) may be found subject to regulation under the CWA on a case-by-case basis if either alone, or in combination with “other similarly situated waters” in the same region, they have a “significant nexus” to traditional navigable waters, interstate waters or the territorial seas.³¹ The EPA estimates that the WOTUS Rule will annually cost between \$133 and \$231 million.³²

In developing a proposed rule, EPA is required to follow certain procedures to ascertain the consequences of its proposal. One of those procedural requirements involves analysis of economic impacts on small entities. Had the EPA complied with these requirements for both the power plants rules and the WOTUS Rule, it might have uncovered information about small entity impacts and flaws with the proposals.

III. Regulatory Flexibility Act

The RFA applies to all rules, both proposed and final, for which the EPA must conduct notice and comment rulemaking as required by § 553 of the Administrative Procedure Act or any other law. Under the RFA, all agencies are required to assess the economic consequences of their rules on small businesses, small governmental jurisdiction and small non-profits (collectively, “small entities”). Before the agency issues a proposed rule, it must conduct a threshold analysis of the economic impact of the proposed rule. If the agency determines that the proposed rule will have a “significant economic impact on a substantial number of small entities,” it must prepare an “initial regulatory flexibility analysis” (IRFA).³³ If the agency determines the proposed rule will not have a “significant economic impact on a substantial number of small entities,” the agency head may certify to such a conclusion and need not prepare an IRFA.³⁴ The certification statement must include a “factual basis for the certification.”³⁵

The RFA also requires agencies to conduct outreach to small entities when a rule will have a “significant economic impact on a substantial number of small entities.”³⁶ Further, the EPA has an additional outreach obligation for any proposed rule that requires preparation of an IRFA. Pursuant to § 609(b) of

³⁰ *Id.* at 22,198-99.

³¹ *Id.* at 22,262-63. The WOTUS Rule retains exclusions for waste treatment systems and prior converted croplands and proposes to exclude specific waters from the definition including: ditches that are excavated wholly in uplands, drain only uplands and have less than perennial flow; ditches that do not contribute flow to a traditional navigable water, interstate water, territorial sea or impoundment; artificial irrigated areas that would revert to upland if irrigation ceased; artificial lakes or ponds created on dry land and used exclusively for stock watering, irrigation, settling basins or rice growing; artificial reflecting or swimming pools created on dry land; small ornamental waters created on dry land; water-filled depressions created incidental to construction activity; groundwater; and gullies, rills and non-wetlands swales. *Id.* at 22,263.

³² UNITED STATES ENVIRONMENTAL PROTECTION AGENCY AND UNITED STATES ARMY CORPS OF ENGINEERS, ECONOMIC ANALYSIS OF PROPOSED REVISED DEFINITION OF WATERS OF THE UNITED STATES 33 (2014).

³³ 5 U.S.C. §§ 603, 605(b). An IRFA must describe the small entities that will be affected, the impact of the proposed rule on small entities, the compliance burdens imposed and any significant alternatives that could minimize any significant economic impacts. *Id.* at § 603(a)-(c).

³⁴ *Id.* at § 605(b). A certification at the proposed rule stage does not mean the agency may certify at the final rule stage. If sufficient information is submitted to the agency during the comment period that shows there is a significant economic impact on a substantial number of small entities, then the agency must prepare a final regulatory flexibility analysis.

³⁵ *Id.*

³⁶ *Id.* at § 609(a).

the RFA, EPA must convene a small business advocacy review (SBAR) panel³⁷ before the rule is proposed to receive input from small entities representatives (SERs).³⁸

In addition to the obligations of the RFA, EPA must comply with the requirements of Executive Order (E.O.) 12,866. E.O. 12,866 requires EPA to estimate the benefits and costs of its rules and tailor them to impose the least burden on small businesses.³⁹

In recent years, small businesses and the SBA Office of Advocacy, the independent executive branch office that monitors agency RFA compliance, have raised concerns that the EPA is not fulfilling its RFA obligations. Unfortunately, the EPA's recently proposed rules continue to raise concerns about the agency's commitment to fulfilling its obligations under the RFA.

IV. EPA's Compliance with the RFA

The EPA's work to create carbon standards for power plants began well before the President's Climate Action Plan was issued in 2013. In 2011, the EPA convened a SBAR panel on the power plant rules.⁴⁰ At the time, the SBA Office of Advocacy raised concerns that the panel had been convened prematurely because EPA was not prepared to discuss its regulatory approach or alternatives to reduce burdens on affected small entities.⁴¹ However, the EPA proceeded to meet with small entities in the context of the panel only to cease work shortly thereafter.⁴² It can reasonably be concluded that EPA expected the power plant rules to have a significant economic impact on a substantial number of small entities since that is the trigger for convening a SBAR panel.

Nevertheless, the EPA has certified both the New Power Plant Rule and the Existing Power Plant Rule as ones that will not have a significant economic impact on a substantial number of small entities.⁴³ In the New Power Plant Rule RFA certification, the EPA states that the rule will result in no economic impacts because it projects that no new coal-fired power plants without CCS will be built.⁴⁴ The EPA certified the Existing Power Plant Rule because the states, not power plants, will be directly regulated under the rule.⁴⁵

³⁷ The panel is comprised of a representative of the EPA, a representative of the Office of the Chief Counsel for Advocacy of the United States Small Business Administration (SBA Office of Advocacy) and a representative from the Office of Information and Regulatory Affairs (OIRA) at the Office of Management and Budget (OMB). *Id.*

³⁸ *Id.* at § 609(b)-(d). The panel provides SERs with a draft of the proposed rule as well as any analysis of small entity impacts and regulatory alternatives, and collects advice and recommendations from the SERs. The panel then must report on the SERs' comments and its findings. The report is made part of the rulemaking record. *Id.*

³⁹ 3 C.F.R. 638 (1993), *reprinted in* 58 Fed. Reg. 51,735 (Oct. 4, 1993).

⁴⁰ SBA OFFICE OF ADVOCACY, REPORT ON THE REGULATORY FLEXIBILITY ACT FY 2012, at 25 (2013) [hereinafter RFA FY 2012 Annual Report], *available at* http://www.sba.gov/sites/default/files/files/FIN_12regflx.pdf. On March 4, 2011, the EPA formally notified SBA Office of Advocacy that it was going to convene a SBAR panel on the power plant rules and SBA Office of Advocacy acknowledged the notification by letter. Letter from Winslow Sargeant, Chief Counsel for Advocacy, SBA to Alexander Cristofaro, Small Business Advocacy Chair, EPA (Mar. 16, 2011), *available at* http://www.sba.gov/sites/default/files/advocacy/epa11_0316.pdf.

⁴¹ Letter from Winslow Sargeant, Chief Counsel for Advocacy, SBA to Lisa Jackson, Administrator, EPA and Cass Sunstein, Administrator, OIRA, OMB 1 (June 13, 2011), *available at* <http://www.sba.gov/content/letter-dated-06132011-environmental-protection-agency-1>.

⁴² RFA FY 2012 Annual Report, *supra* note 40, at 25.

⁴³ New Power Plant Rule, 79 Fed. Reg. at 1500; Existing Power Plant Rule, 79 Fed. Reg. at 34,947.

⁴⁴ *Id.* This projection rests on the existing and expected market conditions – highly competitive natural gas prices, lower electricity demand, and increases in renewable energy supply. 79 Fed. Reg. at 1442. Should any of the market conditions change, EPA's projection may be incorrect.

⁴⁵ A series of cases decided in the United States Court of Appeals for the District of Columbia have held that the RFA does not require an agency to assess the impacts of its rules on small entities that it is not directly regulating. *See American Trucking Ass'n v. EPA*, 175 F.3d 1027, 1043-45 (D.C. Cir. 1999) (certification of ozone national

However, if the EPA has to promulgate a plan for a state that fails to submit a satisfactory plan, the EPA must comply with the RFA because it would be directly regulating the power plants.

Despite certifying both rules, the EPA acknowledges that there has been significant interest from small entities (public power utilities and rural electric cooperatives) that will be affected by the rules. This should not be surprising since it is entirely foreseeable that small power plants will be affected by both rules. If a small entity wants to build a new coal-fired power plant in the future, it will have to incur the costs and burden associated with implementing CCS. Existing small power plants will also be affected by emissions limitations implemented by the states as part of their plans to achieve the CO₂ goals the EPA is proposing. In addition, it is entirely foreseeable that small businesses could be affected by higher electricity costs or reliability issues. The impacts of rate increases may be particularly acute for energy intensive small businesses such as manufacturers. Even though such indirect impacts need not be examined under the RFA, they should have been assessed pursuant to E.O. 12,866.

The EPA and Corps certified that the WOTUS Rule would not have a “significant economic impact on a substantial number of small entities.” However, the agencies failed to provide any factual basis for the certification,⁴⁶ as required by the RFA, despite the potential consequences for small businesses.⁴⁷ On May 29, 2014, the Committee held a hearing on the WOTUS Rule at which testimony was received from representatives of three small businesses (a home builder, a farmer and a stone and gravel company executive).⁴⁸ All three small businesses raised concerns that the EPA did not convene a SBAR panel and did not assess the rule’s effects on small businesses. In addition, they stated that the economic analysis the EPA had done severely underestimated the costs businesses will incur to comply with the rule.

The EPA claims that the WOTUS Rule will provide clarity to regulated entities.⁴⁹ However, the small businesses testified that the rule is confusing and will create more not less confusion about whether a certain body of water is jurisdictional. This completely undermines EPA’s major rationale for promulgating the rule.

V. Conclusion

The EPA is not fully complying with the letter or spirit of the RFA. The RFA embodies a set of common-sense rulemaking requirements that ensure that agencies engage with small businesses early in the rulemaking process and identify more cost-effective and less burdensome ways to achieve their regulatory objectives. The EPA’s indifference to the law unfortunately demonstrates its lack of concern about the real-world consequences of its actions for American small businesses. This irrational approach to rulemaking may result in litigation that could delay implementation of its rules thereby undermining the EPA’s regulatory objectives.

ambient air quality standards proper because small entities not directly regulated)), *aff’d in part and rev’d in part on other grounds sub nom.*, *Whitman v. American Trucking Ass’ns*, 531 U.S. 457 (2001). This year, the House passed the Regulatory Flexibility Improvements Act of 2013 (H.R. 2542), as Title III of the Achieving Less Excess in Regulation and Requiring Transparency Act of 2014 (H.R. 2804), which would strengthen the RFA. The bill clarifies that “economic impact” means any direct economic effect and any indirect economic effect on small entities (including compliance costs and effects on revenue) which is reasonably foreseeable.

⁴⁶ WOTUS Rule, 79 Fed. Reg. at 22,220.

⁴⁷ A discussion of the flaws with the WOTUS Rule and its direct consequences for a variety of small businesses can be found in the Committee on Small Business’s May 29, 2014 hearing memorandum, *available at* http://smallbusiness.house.gov/uploadedfiles/5-29-2014_revised_hearing_memo.pdf.

⁴⁸ *Will EPA’s ‘Waters of the United States’ Rule Drown Small Businesses?: Hearing Before the H. Comm. on Small Business*, 113th Cong. (2014).

⁴⁹ WOTUS Rule, 79 Fed. Reg. at 22,188.