LAW360

Portfolio Media. Inc. | 860 Broadway, 6th Floor | New York, NY 10003 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Why Cost-Benefit Analysis In Enviro Law Is Superior

Law360, New York (June 12, 2013) -- For at least the past five presidential administrations, federal regulations have been required to undergo a cost-benefit analysis to assess their efficiency and determine whether there are any better alternatives. The basic idea is that decisions are assessed by quantifying and weighing both the costs and benefits of implementing a particular regulation. This concept has basic origins in the tort common law, has been implemented frequently in federal laws and regulations and has been written about favorably by the federal courts.

However, not everyone believes that cost-benefit analysis should be used in implementing environmental policy.

Recently, President Obama's first U.S. Environmental Protection Agency policy chief, Lisa Heinzerling, wrote a critique of the Obama administration's rule-making efforts at federal agencies, including the EPA, because of what she deemed excessive control by Obama's Office of Management and Budget in "continu[ing] and deepen[ing] a longstanding practice of White House control over EPA rules, with cost-benefit analysis as the guiding framework."[1] She decried that the OMB's review, "under a cost-benefit rubric," of "all agency rules that it deems 'major' under executive orders mandating this review."[2]

Heinzerling, who wrote a book with economist Frank Ackerman in 2005 criticizing the use of cost-benefit analyses in environmental rule-makings[3], opined that the OMB was exercising too much control over the rule-making process with too little transparency and called for "relaxing the cost-benefit stranglehold on regulatory policy."[4]

This debate raises the question whether there is wisdom or waste in utilizing cost-benefit analyses to make environmental law and policy.

The History and Current Prevalence of Cost-Benefit Analysis

Cost-benefit analysis has long been used in many areas of the law, including to address environmental issues. It is generally used in the tort common law's definitions of negligence and nuisance. It was also expressly written into certain federal environmental statutes.

The Toxic Substances Control Act of 1976 requires the EPA to consider “the benefits of each substance or mixture for various uses and availability of substitutes for such uses” and “the reasonably ascertainable economic consequences of the rule, after consideration of the effect on the national economy, small business, technological innovation, the environment, and public health.”[5]

In addition, the 1996 Safe Drinking Water Act Amendments require that when promulgating a national drinking water standard under the act, the EPA must publish a determination “as to whether the benefits of the maximum contaminant level justify, or do not justify, the costs.”[6]

Similarly, every U.S. president since President Reagan has directed federal agencies to perform economic analyses of major regulations to determine whether its benefits are likely to exceed its costs and to assess whether there are more effective or less costly alternatives. President Reagan’s 1981 Executive Order 12291 directed, “Regulatory action shall not be undertaken unless the potential benefits to society from the regulation outweigh the potential costs to society.”

President George H.W. Bush continued to use Executive Order 12291, and President Clinton signed Executive Order 12866, which likewise required agencies to consider all significant costs and benefits, including ones that cannot be quantified, and alternatives that maximize net benefits or minimize net costs.

President Clinton’s order required agencies to show that benefits “justify” the costs, whereas President Reagan’s order directed that the benefits “outweigh” the costs. Thus, the requirements that agencies quantify as many costs and benefits as possible and examine potential alternatives have remained essentially the same over the years.

President Obama’s Executive Order 13563 further required that cost-benefit analysis be undertaken in the regulatory context and commanded each agency to “propose or adopt a regulation only upon a reasoned determination that its benefits justify its costs (recognizing that some benefits and costs are difficult to quantify)” and that each agency use the best available techniques to “quantify anticipated present and future benefits and costs as accurately as possible.”

The federal judiciary has also favorably weighed in on the use of cost-benefit analysis, including the United States Supreme Court. Most recently, in Entergy Corp. v. Riverkeeper Inc., the Supreme Court held that the EPA had properly relied upon cost-benefit analysis in implementing regulations under the Clean Water Act.[7]

The case involved “cooling water intake structures” at power plants that threatened the environment by squashing against intake screens or suctioning into the cooling system aquatic organisms from the water sources tapped to cool the plants. The Clean Water Act mandated that any cooling water intake structures “reflect the best technology available for minimizing adverse environmental impact.”[8]

The EPA expressly declined to mandate closed-cycle cooling systems for existing facilities (as it had done for new facilities) in part because the cost to render existing facilities closed-cycle compliant would be

nine times the estimated cost of compliance with the performance standards and because other technologies could approach the performance of closed-cycle operation.[9]

In a 6-3 decision written by Justice Scalia, the Supreme Court reversed the Second Circuit's decision holding that the EPA was not permitted to use cost-benefit analysis in determining the content of regulations promulgated under § 1326(b) of the Clean Water Act. The Supreme Court noted that the Second Circuit interpreted the relevant statute to mandate the best technology available that can "be reasonably borne by the industry" but noted that "whether it is 'reasonable' to bear a particular cost may well depend on the resulting benefits."[10]

The Supreme Court also noted that the respondents conceded that the statute's language was "plainly not so constricted as to require EPA to require industry petitioners to spend billions to save one more fish or plankton," which thus conceded the principle that it was permissible to at least conduct some cost-benefit analysis.[11]

Justice Breyer's concurrence (who himself wrote a book in 1993 arguing that health, safety and environmental regulation too often produce tiny benefits at a very great cost[12]) agreed that the statute authorized the EPA to compare costs and benefits but argued that the law was meant to restrict, though not forbid, the use of cost-benefit analysis.[13]

To forbid cost-benefit analysis would bring "irrational results," especially "in an age of limited resources available to deal with grave environmental problems, where too much wasteful expenditure devoted to one problem may well mean considerably fewer resources available to deal effectively with other (perhaps more serious) problems."[14]

The dissent, written by Justice Stevens, argued that the statute prohibited the use of cost-benefit analysis and stated its concern that usually, a regulation's financial costs are often more obvious and easier to quantify than its environmental benefits and that cost-benefit analysis often, if not always, yields a result that does not maximize environmental protection.[15]

Contrary Arguments to Cost-Benefit Analysis

Despite its widespread use, cost-benefit analysis has its critics who contend that there are problems with how it quantifies and weighs the costs versus benefits.

In a prior article from 2002, Heinzerling criticized the translation of lives, health and the natural environment into monetary terms and the discounting of harms to human health and the environment that are expected to occur in the future.[16] She stated that these features of cost-benefit analysis make it "a terrible way to make decisions about environmental protection."[17]

Other arguments against cost-benefit analysis include that it fails to adequately address cumulative impacts to the environment.[18]

An alternative principle, generally favored by opponents of cost-benefit analysis and largely embraced in Europe, is the precautionary principle, which represents the idea that regulation is required even in the face of a lack of information or scientific uncertainty where there is a sufficient environmental or other risk.[19]

Why Cost-Benefit Analysis Is Superior

One of the current and most outspoken proponents of the use of cost-benefit analysis is Cass Sunstein, President Obama's former head of the Office of Information and Regulatory Affairs (OIRA), which is within OMB. Sunstein has written often on the subject of cost-benefit analysis and alternative approaches.

Sunstein identifies what he contends are serious problems with the precautionary principle, including, "How much precaution is the right level of precaution? Are costs relevant to the answer? In any case human beings face a number of risks, not simply one, and any effort to reduce one risk might well increase another risk. Is it possible, even in principle, to take precautions against all risks, rather than a subset? If all risks cannot be reduced at once, how should regulators set priorities?"[20]

According to Sunstein and others who share his view, it is these issues that make cost-benefit analysis a superior way to determine effective regulation. Although not perfect, cost-benefit analysis seeks to best quantify the costs and benefits of a given action or regulation and then use that information to make the most efficient and best decision.

As Sunstein says, "Without some sense of both costs and benefits — both nonmonetized and monetized — regulators will be making a stab in the dark. Human beings have a great deal of difficulty assessing risks, making them prone to both hysteria and neglect; CBA does not supply definite answers, but it can help to establish which risks are serious and which are not. By contrast, the Precautionary Principle approaches incoherence. Because risks are on all sides of social situations, and because regulation itself increases risks of various sorts, the principle condemns the very steps it seems to require."[21]

Judge Richard Posner has also written extensively on the use of cost-benefit analysis, describing it as "an indispensable step in rational decision making in this and other areas of government regulation."[22] Posner rejects the precautionary principle as a reasonable approach but notes that once it is sensibly tempered, it turns into cost-benefit analysis plus risk aversion, that is, a form of cost-benefit analysis that creates a margin of safety to protect against those dangers that produce special concern.

Thus, the precautionary principle simply proposes an overabundance of caution where benefits and risks are uncertain, whereas cost-benefit analysis provides the larger framework to attempt to assess these risks and implement the most efficient and effective regulation based on current knowledge.

Side Effects of Institutionalized Cost-Benefit Analysis

While the widespread use of cost-benefit analysis in regulatory rule-making is often hailed by business and industry as the best and most efficient way for the federal government to implement regulation, it is not without its potentially unexpected side effects. With government agencies such as the EPA focused more on obtaining the best benefits in light of costs, that mindset also affects how they prioritize and conduct enforcement actions.

Recent statistics show that the EPA has been bringing fewer enforcement actions but yet has recovered record amounts in civil penalties.[23] This may be due to a conscious shift by the EPA to pursue larger, more complex cases that produce bigger fines.

An assistant administrator at the EPA's Office of Enforcement and Compliance Assurance explained: "We want our agents to be focusing on investigating the most important cases and the most significant crimes to have the maximum deterrent effect."[24]

Budget cuts have also likely played a factor in forcing the agency to prioritize. Consequently, if a federal agency targets a company for an enforcement action, it may be because the agency believes it can obtain large penalties.

Conclusion

Although cost-benefit analysis has its critics, it can be an effective strategy for federal agencies to develop and implement environmental regulations that impose reasonable costs in exchange for more valuable benefits to society.

However, the same goals are a warning sign for any company or individual that is the subject of an enforcement action. If a federal agency is spending its limited resources to investigate or prosecute a claim, then it is reasonable to expect that it is doing so with an expectation that the result will justify the effort.

On the whole, cost-benefit analysis remains the best method for efficiently implementing environmental policy and absolutely should continue to be utilized by government regulators.

--By Jeffrey Dintzer and David Edsall Jr., Gibson Dunn & Crutcher LLP

Jeffrey Dintzer is a partner, and David Edsall is an associate in the firm's Los Angeles office.

The opinions expressed are those of the author and do not necessarily reflect the views of the firm, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] Lisa Heinzerling, Who Will Run the EPA?, 30 Yale J. on Reg. 39 (2013).

[2] Id.

[3] Frank Ackerman & Lisa Heinzerling, Priceless: On Knowing the Price of Everything and the Value of Nothing (2005).

[4] Heinzerling, supra note 1, at 43.

[5] Toxic Substances Control Act of 1976, 15 U.S.C. § 2605(c).

[6] Safe Drinking Water Act Amendments of 1996, 42 U.S.C. § 300g-1(b)(4)(C).

[7] Entergy Corp. v. Riverkeeper, Inc., 556 U.S. 208 (2009).

[8] Id. at 213.

[9] Id. at 215-16.

[10] Id. at 225-26.

[11] Id. at 226.

[12] Stephen Breyer, Breaking the Vicious Circle: Toward Effective Risk Regulation (1993).

[13] Entergy Corp., supra note 8 at 230.

[14] Id. at 232-33.

[15] Id. at 237.

[16] Lisa Heinzerling & Frank Ackerman, Pricing the Priceless: Cost-Benefit Analysis in Environmental Protection, 150 U. Pa. L. Rev. 1553, 1583 (2002).

[17] Id.

[18] Joseph H. Guth, Cumulative Impacts: Death-Knell for Cost-Benefit Analysis in Environmental Decisions, Barry Law Review, Vol. 11 (2008).

[19] Cass R. Sunstein, Cost-Benefit Analysis and the Environment, 115 Ethics 351 (2005).

[20] Id. at 354.

[21] Id. at 354-55.

[22] Richard A. Posner, Catastrophe: Risk and Response, 139 (2005).

[23] John McArdle, EPA: Enforcement Targets ‘Larger, More Complex’ Violations, but Case Numbers Fall, National Water Resources Association (December 19, 2012), http://www.nwra.org/content/articles/epa-enforcement-targets-larger-more-complex-violat/.

[24] Id.

All Content © 2003-2013, Portfolio Media, Inc.