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In this Article David Spence and Lekha Gopalakrishnan propose a new understanding of regulatory bargaining. Economists and others have long argued that the American regulatory system is unnecessarily inefficient. Critics charge that the system is both substantively inefficient, in that it sometimes mandates the use of inefficient means for achieving a regulatory goal, and procedurally inefficient, in its over-reliance on rules. These arguments have led to a wave of regulatory reform experiments in the federal bureaucracy, many of which seek to promote positive-sum changes in regulatory policy through bargaining among private- and public-sector stakeholders. As several commentators have noted, most of these regulatory reforms have not met expectations in that bargaining participants often forgo positive-sum changes in the status quo. Those same commentators have offered a variety of explanations for these failures, most of which are either unpersuasive or incomplete. Spence and Gopalakrishnan propose an another explanation drawn from the standard bargaining literature in economics, one that seems to explain the trajectory of recent regulatory reforms. The authors argue that, in the context of political conflict over policy changes, participants in these bargaining processes view positive-sum policy changes in zero-sum terms. That is, they bargain strategically, using their power to veto these positive-sum changes to extract further policy concessions from other stakeholders. This revelation has important implications for the future of this kind of regulatory reform.

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INTRODUCTION

Why is regulation inefficient, and why do regulators forgo obvious opportunities to make it more efficient? This is a familiar lament, one that is heard beyond the confines of academic discourse. For ex-

ample, in a recent best seller,[1] Philip Howard explores the inability of policymakers to make "common sense" decisions. Howard places the blame for this phenomenon on "the law," particularly statutes and rules.[2] The evidence he offers in support of his argument is anecdotal, and many of his anecdotes describe the failure of governmental actors to take steps that would produce "positive-sum" changes—that is, changes that would help some without hurting others.[3] One such anecdote is the story of a proposed donation to New York City of portable public restroom kiosks, a proposal that seemed likely to offer a solution to a vexing public health problem. Though the proposed facilities were already road-tested in other large cities and would have cost the city nothing,[4] they were not wheelchair-accessible and would violate a city anti-discrimination ordinance.[5] Ultimately, opposition to the proposal led the city to refuse the donation.

Economists have long argued that statutes frequently require less-than-sensible approaches to policy problems.[6] This economic critique of regulation has been particularly unrelenting in the field of environmental regulation, where economists have criticized the barriers to efficient pollution control posed by enviroumental statutes and regulations. In recent years, arguments like these have spurred (i) calls for reform of environmental regulation by politicians,[7] (ii) a series of internal[8] and external[9] evaluations and reviews of govern-

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1. PHILIP K. HOWARD, THE DEATH OF COMMON SENSE: HOW LAW IS SUFFOCATING AMERICA (1994).

2. *Id.* at 177 ("Principles are like trees in open fields. We can know where we are and where to go. But the path we take is our own. What good is law today? We fight off rules like branches hitting us in the face, losing any sense of where we are supposed to be going and bleeding from illogical dictates that serve no one's purpose.").

3. For a more precise discussion of this concept, see the discussion of "Pareto optimality," *infra* note 12 and Section II.A.

4. The facilities would have been paid for by renting advertising space on the outside of each unit. *See* HOWARD, *supra* note 1, at 114.

5. Nor would provision of additional wheelchair-accessible facilities in buildings have overcome the legal or political hurdles, because they would not have been provided in the same location as the kiosks. *See id.* at 114-15.

6. *See* the discussion of this literature, *infra* notos 20-26 and accompanying text.

7. Indeed, regulatory reform legislation has occupied a place on the legislative agenda of late. *See, e.g., House GOP Pledges Progress on Reform, Says Help from EPA Would be "Welcome,"* 27 Envtl. Rep. (BNA) 1656 (1996) (discussing House Republicans' regulatory reform agenda); *Property Rights Measure Most Visible of Several Proposals to Curb Regulation*, 25 Envtl. Rep. (BNA) 2502 (1995) (discussing the Republicans' reform agenda generally); *Washington Clarifies Lender Liability*, 26 Envtl. Rep. (BNA) 235 (1995) (discussing legislation "already passed by the House as part of the 'Contract With America,' including regulatory reform with an emphasis on cost-benefit analysis").

8. The best known recent example is the so-called "Gore Report," or National Performance Review, which comprised a series of agency-specific reviews. *See generally* AL GORE, FROM RED TAPE TO RESULTS: CREATING A GOVERNMENT THAT WORKS BETTER AND COSTS LESS, REPORT OF

ment regulatory systems, and (iii) a wave of regulatory reform experiments at the Environmental Protection Agency ("EPA").[10] Indeed, it can be argued that the EPA has become the national focal point of modern regulatory reform, and that many of the EPA's reform experiments have been aimed at overcoming legal or statutory barriers to efficiency. However, regulatory reform is rapidly approaching a crossroads. After more than a half-decade of experiments, pilot projects, and "reinvention" efforts, the EPA seems uncertain where to go next. Many of its reinvention programs have stalled or have failed to meet expectations, and the Agency seems unable or unwilling to draw larger lessons from its successful experiments.[11] This Article represents an attempt to understand and explain why that is.

We argue that, in the context of regulatory reform, the problems that Philip Howard attributes to "the law" are at their core political. This is perhaps not surprising, since most regulatory law is the product of political processes. Section I outlines the efficiency critique of regulation, noting two varieties of inefficiency in regulation—substantive inefficiency and procedural inefficiency. Section II explores the economist's analytical framework for understanding and evaluating these regulatory reform efforts, with special emphasis on the concept of Pareto optimality[12] and the argument that all available positive-sum changes from the status quo will be achieved through bargaining. It then explores several recent regulatory reforms at the EPA that have attempted to facilitate the bargaining solution in practice, noting that the results to date have been disappointing.

THE NATIONAL PERFORMANCE REVIEW (Sept. 7, 1993). However, as we observe at note 15, *infra*, internal reviews of regulatory processes are nearly as old as government regulation itself. For a summary of those reviews, see *infra* notes 16-17 and accompanying text.

9. Perhaps the two most prominent examples are the National Academy of Public Administration's ("NAPA") recent reviews of EPA decisionmaking. *See* NAPA, SETTING PRIORITIES, GETTING RESULTS: A NEW DIRECTION FOR EPA (1995) [hereinafter NAPA SETTING PRIORITIES]; NAPA, RESOLVING THE PARADOX OF ENVIRONMENTAL PROTECTION: AN AGENDA FOR CONGRESS, THE EPA AND THE STATES (1997) [hereinafter NAPA, RESOLVING THE PARADOX].

10. The EPA's own reform efforts are numerous and varied. They can be tracked via the EPA's "reinvention" web page, *Reinventing Environmental Protection* (visited Jan. 21, 2000) <http://www.epa.gov/reinvent/>. We discuss EPA regulatory reinvention efforts, *infra* at Sections II.B.1-4.

11. For a detailed discussion of this issue, see *infra* Sections II.B.1-4.

12. A distribution of goods among members of a group is Pareto optimal when no other distribution (or trades) will make some subset of the group better off without making another subset worse off. A "Pareto superior" alternative to the status quo is one that would make someone in the group better off without hurting anyone in the group. In discussing proposed changes to any status quo, we will use the more conventional term "positive-sum" rather than "Pareto superior."

Section III reviews the developing critique of regulatory reform and proposes another, alternative answer to the question of why EPA reforms have not met their proponents' expectations.[13] This answer is suggested by Philip Howard's restroom kiosk example,[14] in which a group with political veto power perceived an essentially positive-sum proposal in zero-sum terms. We hypothesize that the same phenomenon is happening now at the EPA: that is, in the larger context of long term, repeated political conflict over environmental regulation, regulatory reforms that economists would view as positive-sum changes are viewed by important stakeholders in zero-sum terms. Those stakeholders, primarily environmental interests inside and outside of the EPA, veto proposed reforms that would neither harm nor benefit them, but would benefit their adversaries, primarily industry. We show that stakeholders exercise this veto power rationally, not only because they suspect that proposed reforms would harm their interests, but also because this approach maximizes their ability to extract further concessions from their adversaries in the future.

Section IV examines more closely the EPA's experience to date with its most celebrated regulatory reform initiative, Project XL, in an attempt to verify our hypothesis. We conclude that that experience indeed has been consistent with our analysis, in that certain environmental interests within the EPA have restructured the Project XL process so as to impede the approval of positive-sum changes to the status quo. Restructuring also has had exactly the effects desired by those interests: it has induced firms to offer greater increases in environmental benefits in order to obtain economic benefits that otherwise would have been vetoed.

Section V concludes with some thoughts on the implications of our analysis for the future of regulatory reform. We are cautiously optimistic about its potential for improving regulation in incremental but important ways, particularly if the rules governing the bargaining process can be changed to protect the integrity of bargaining outcomes against legal challenges.

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13. Sections II and III represent the further development and elaboration of ideas we presented in an earlier paper entitled *The New Political Economy of Regulation: Looking for Positive-Sum Change in a Zero-Sum World*, at the Wharton Impact Conference on Environmental Contracting, Philadelphia, PA. That earlier paper will appear in the published proceedings of that conference.

14. Howard attributed the kiosk plan's demise to the disabled lobby's perceived infringement of their "rights." *See* HOWARD, *supra* note 1, at 113-16.

I. THE VARIETIES OF REGULATORY INEFFICIENCY

While "regulatory reform" is not a new idea,[15] in the last three decades the call for regulatory reform has grown stronger, producing a succession of presidential reform initiatives. Beginning with the Carter Administration and culminating in the Reagan-Bush era, we have seen a groundswell of opposition to regulation as an impediment to economic growth, and a general trend toward increasingly centralized White House review of regulations,[16] culminating in the Bush Administration's Competitiveness Council, headed by Vice President Dan Quayle.[17] The combination of regulatory reform with regulatory relief during the Reagan-Bush years led to some confusion of these two analytically distinct notions. While the elevation of another Democrat to the presidency in 1992 brought a retreat from the regulatory relief efforts of the Reagan-Bush years, it did not slow the movement for regulatory reform. To the contrary, in some ways the Clinton Administration has stepped up the pace of regulatory reform.

The distinction between regulatory relief and regulatory reform is a distinction between ends and means—between simply reducing the regulatory burden on industry by lowering standards, and ad-

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15. Indeed, studies of regulations and regulatory agencies have filled scholarly journals for more than a century. For a discussion of the early scholarly debates over administrative reform, see MICHAEL W. SPICER, THE FOUNDERS THE CONSTITUTION AND PUBLIC ADMINISTRATION: A CONFLICT OF WORLD VIEWS 26-40 (1995). For a discussion of early reform debates within the federal government, see JOHN A. ROHR, TO RUN A CONSTITUTION: THE LEGITIMACY OF THE ADMINISTRATIVE STATE 55-167 (1986).

16. This trend is chronicled in RICHARD A. HARRIS & SIDNEY M. MILKIS, THE POLITICS OF REGULATORY CHANGE: A TALE OF TWO AGENCIES 3-139 (1996). *See also* David B. Spence, *Administrative Law and Agency Policymaking: Rethinking the Positive Theory of Political Control*, 14 YALE J. ON REG. 407, 416 (1997). Jimmy Carter attempted to address the problem of inefficient regulation by centralizing the regulatory process in the White House through the use of Office of Management and Budget ("OMB") oversight of executive branch rulemaking. Ronald Roagan took that centralization process one step further with his Executive Order No. 12291, under which the Reagan OMB actively sought to reduce the economic impacts of regulation on industry and to heighten the importance of cost-benefit considerations in the Agency policymaking process. For a scholarly analysis of the Reagan Administration regulatory review process, see Harold H. Bruff, *Presidential Management of Agency Rulemaking*, 57 GEO. WASH. L. REV. 533 (1989); Thomas O. McGarity, *Presidential Control of Regulatory Agency Decisionmaking*, 36 AM. U. L. REV. 443 (1987); Susan Rose-Ackerman, *Deregulation and Reregulation: Rhetoric and Reality*, 6 J.L. & POL. 287 (1989); Peter L. Strauss & Cass Sunstein, *The Role of the President and OMB in Informal Rulemaking*, 38 ADMIN. L. REV. 181 (1986); Peter P. Swire, *Incorporation of Independent Agencies into the Executive Branch*, 94 YALE L.J. 1766 (1985); W. Andrew Jack, Note, *Executive Orders 12,291 and 12,498: Usurpation of Legislative Power or Blueprint for Legislative Reform?*, 54 GEO. WASH. L. REV. 512 (1986).

17. The Council was roundly criticized for providing extra-legal opportunities for input to the regulatory process for industry, and Congress ultimately voted to remove the Council's funding. *See House Votes To Cut Funds Of Quayle Council*, 23 Envtl. Rep. (BNA) 776 (1992).

dressing the question of how best to achieve a given standard. Though some have pushed unsuccessfully for the former under the guise of the latter,[18] we are interested only in the latter here. The persistent and broad-based impulse toward regulatory reform has been fed not only by politicians and interest groups, but also by a scholarly critique of the regulatory system that has continued to develop alongside the political debate. That scholarly critique has coalesced along two distinguishable (but not always distinguished)[19] dimensions: one that focuses on the substantive efficiency of regulatory policies, and another that focuses on procedural efficiency, or rather the inefficiencies that stem from the process by which agencies make policy. The former critique is led by economists, the latter by public administration scholars, and both have allies among legal scholars.

The substantive efficiency critique of regulation is long-standing[20] and well-known, as is the economist's solution for inefficiency: namely, the replacement of regulatory mandates with market incentives. It says that regulation should be minimally prescriptive, leaving

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18. Indeed, Resources for the Future's Paul Portney has labeled these efforts "cartoon reform." *See* Paul R. Portney, *Cartoon Caricatures of Regulatory Reform*, RESOURCES, Fall 1995, at 21. We place the efforts of the Competitiveness Council and some parts of the 1994 House Republicans' environmental agenda in this category. It is worth noting that some critics of reform do not make this distinction and/or suspect that most regulatory reform is a disguised attempt at regulatory relief. *See, e.g.*, Amy Heinzerling, *Reductionist Regulatory Reform*, 8 FORDHAM ENVTL. J. 459, 460-61 (1997) (coupling the 1994 "Contract with America" with risk-based regulatory reform); Elizabeth Glass Geltman & Andrew E. Skroback, *Reinventing the EPA to Conform with the New American Environmentality*, 23 COLUMB. J. ENVTL. L. 1, 25-26 (1998) (describing 1994 House Republicans anti-environmental agenda). Of course, we acknowledge the existence of good faith arguments that regulatory standards (the ends of regulation) may be inefficiently stringent from a social welfare point of view. This argument is often associated with advocacy of risk analysis as a guide to spending on environmental protection. For a good summary of this large literature, see Frank Cross, *The Subtle Vices Behind Environmental Values*, 8 DUKE ENVTL. L. & POL'Y F. 151 (1997); Cass R. Sunstein, *A Note on "Voluntary" versus "Involuntary" Risks*, 8 DUKE ENVTL. L. & POL'Y F. 173 (1997). We do not address those arguments here; rather, we are concerned only with reform arguments aimed at the means of achieving regulatory goals.

19.The distinction we make here between substantive and procedural efficiency is particularly useful analytically in discussing the problems encountered by current regulatory reform initiatives. This should become evident as the argument unfolds here. There are reasons, however, why others may not make this same distinction. In particular, the two critiques overlap, especially in discussions of the design of regulatory instruments, where criticism of command and control regulation can be characterized as both a substantive and procedural critique. In addition, procedural inefficiencies beget substantive inefficiencies, blurring the distinction in that sense. *See infra* notes 27-34 and accompanying text.

20. *See generally* A.C. PIGOU, THE ECONOMICS OF WELFARE (1924). Most environmental economics texts contain good descriptions of Pigou's ideas. *See, e.g.*, WILLIAM J. BAUMOL & WALLACE E. OATES, ECONOMICS, ENVIRONMENTAL POLICY, AND THE QUALITY OF LIFE (1979); THOMAS H. TIETENBERG, ENVIRONMENTAL ECONOMICS AND POLICY (1998); R. KERRY TURNER & DAVID W. PEARCE, ECONOMICS OF NATURAL RESOURCES AND THE ENVIRONMENT (1990).

to regulated firms the task of determining the means of compliance with regulatory limits and goals. That preference for cost-efficiency has led to sustained criticism of so-called "command and control" environmental regulation, under which (i) all regulated firms must meet uniform, technology-based pollution control standards, and (ii) regulators often specify not only the firm's pollution control goal, but the means of achieving it as well.[21] That is, by specifying how individual firms must contribute to pollution control goals, we make pollution control unnecessarily costly. This is because command and control regulation ignores opportunities for two distinct benefits—gains from technological innovation and gains from trade.

First, leaving the means of pollution control to the discretion of the firm provides an incentive for firms to develop less costly control technologies. Conversely, specifying control technologies destroys that incentive.[22] EPA regulations are full of examples of prescriptions that force firms to use inefficient means to achieve a regulatory goal. Perhaps the most frequently-cited testimonial to that fact is the celebrated Yorktown Pollution Prevention Project, a multi-year collaborative effort between the Amoco Oil Company ("Amoco")[23] and the EPA that yielded an agreement to permit Amoco to reduce pollution from its Yorktown, Virginia refinery using more cost-effective approaches than those specified in EPA rules.[24]

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21. This literature is far too extensive to summarize here. For good summaries of the argument, see TIETENBERG, *supra* note 20, at 362-69; TURNER & PEARCE, *supra* note 20, at 84. There is also a sizeable body of literature criticizing reliance on uniform standards in the scholarly law journals, though much of that literature focuses on ambient air standards. *See, e.g.*, James E. Krier, *On the Topology of Uniform Environmental Standards in a Federal System—And Why It Matters*, 54 MD. L. REV. 1226 (1995); James E. Krier, *The Irrational National Air Quality Standards: Macro- and MicroMistakes*, 22 U.C.L.A. L. REV. 323 (1974).

22. While most federal air and water emissions standards are "technology-based," most of these standards do not legally require that firms actually use the technology on which the standard is based. *See, e.g.*, 40 C.F.R. § 60-63 (discussing criteria and standards under the Clean Air Act), 125, 129 (discussing criteria and standards under the Clean Water Act). Sometimes, however, permitting agencies do include such specifications in permits. Furthermore, firms may deem it in their best interests to use the technology in order to minimize the chances of harsh regulatory treatment in the event of a future problem. Finally, other parts of the federal environmental regulatory structure do specify in detail *how* firms must accomplish regulatory goals. See *infra* the discussion of the Amoco Yorktown facility, in the text accompanying note 24.

23. Amoco Corporation owned Amoco Oil Company, which owned the Yorktown facility. Recently, Amoco Corporation merged with British Petroleum to form BP Amoco. The facility is now known as the "BP Amoco Yorktown Refinery."

24. Edward Weber, who has studied the Yorktown Project, described how project participants identified the gains to be had from regulatory flexibility:

> [Stakeholders] discovered a number of instances in which regulations were poorly matched to the emissions profile of the facility. For example, in the particular case of benzene, . . . EPA rules issued in 1990 required Amoco to build a $31 million water-treatment system to capture benzene vapors emanating from wastewater. But data

Second, regulators can make pollution control less costly by allowing those firms that can reduce pollution more inexpensively to bear the lion's share of the control burden. Command and control regulation may specify that firms A and B must each reduce their pollution by 10 units. If firm A can reduce pollution at a fiat cost of $10 per unit of pollution while firm B's pollution reduction costs are $50 per unit, the firms provide 20 units of pollution reduction at a total cost of $600. However, if firm A provided all 20 units of pollution reduction, then the cost would be $200. A system of pollution taxes or marketable permits would allow firms to realize these gains,[25] and would provide a further incentive for firms to develop less costly pollution control methods.[26] Despite some incremental movement toward market-based approaches in the first three decades of modern American environmental regulation, we continue to rely mostly on command and control approaches. Hence, the calls continue for greater substantive efficiency in that regulatory regime.

The procedural efficiency critique is related to, but conceptually distinct from, the substantive efficiency critique. Since the inception of the modern environmental movement, the EPA has relied overwhelmingly on rulemaking to make and administer environmental policy, far more so than most other federal agencies.[27] Scholars trace that predilection to the political environment under which the Agency was created, noting that modern environmental laws were enacted at

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> gathered by the [project participants] showed "that EPA's basic assumptions in requiring such a system . . . were wrong for this refinery. . . ." At the same time, the project's monitoring efforts uncovered a far more serious, and unregulated, benzene problem at the refinery's loading docks. . . . Given the estimated $6 million capital construction cost of controlling barge-loading emissions, the refinery could have saved $25 million while concurrently cleaning up five times more pollution. . . .

EDWARD P. WEBER, PLURALISM BY THE RULES: CONFLICT AND COOPERATION IN ENVIRONMENTAL REGULATION 201 (1998). For another example of an inefficient mandate, see the discussion of the Merck facility, *infra*, note 59 and accompanying text.

25. Of course, under a marketable permit system, firm B would be willing to purchase 10 units of pollution reduction from firm A for some amount greater than or equal to $100. Likewise, at any tax rato greater than $20 per unit of pollution reduced, firm A will choose to reduce pollution by 20 units (or more) while firm B will choose te pay the pollution tax.

26. It is easy to see how, under either system, firms will try te devise less expensive pollution reduction methods to further reduce their own costs.

27. Some agencies eschew rules, preferring to make decisions on a case-by-case basis. Others adopt broad policies but choose not to promulgate them formally as rules. Of course, the Administrative Procedures Act requires that all "rules" be promulgated through APA rulemaking procedures. But as others have noted, many broad policies that appear to meet the definition of a "rule" under the APA are not formally memorialized as rules. For a discussion of these policymaking options, see Spence, *supra* note 16, at 428-30. In any case, the EPA's relative preference for rulemakings has been well chronicled. *See, e.g.*, CORNELIUS KERWIN, RULEMAKING: HOW GOVERNMENT AGENCIES WRITE LAW AND MAKE POLICY (1994).

a time of heightened concern over the problem of agency capture by industry.[28] After a long struggle with industry over the passage of environmental legislation, environmental interests did not want to see their victories undone by the Agency.[29] Consequently, the EPA was designed specifically to resist that kind of capture.[30] Even with its tamper-resistant design, however, EPA policymakers have remained acutely aware of the possibility that industry nevertheless might capture the Agency by persuading a sympathetic future President to appoint Agency leaders who might try to undermine the Agency's mission.[31] Rulemaking is a logical ex ante response to that risk. Memorializing policy choices in regulations makes it more costly for future agency policymakers to reverse those choices.[32] Indeed, agencies face the question of whether to memorialize policies in formally promulgated regulations both continually (when facing new policy choices) and continuously (with respect to each existing informal policy). In making such decisions, an agency balances the benefits of rulemaking against the transaction costs. Therefore, the probability that current policymakers will choose to formalize a policy in the form of a rule is partly a function of their assessment of future policymakers' hostility to the policy. Thus, the EPA's attachment to rulemaking is a testament to its (and its environmental constituents')[33] continuing concern over possible future capture by industry.[34]

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28. *See generally* THEODORE J. LOWI, THE END OF LIBERALISM (1979); MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION (1965); E.E. SCHATTSCHNEIDER, THE SEMISOVEREIGN PEOPLE: A REALIST'S VIEW OF DEMOCRACY IN AMERICA (1975); RICHARD B. STEWART, THE REFORMATION OF AMERICAN ADMINISTRATIVE LAW (1975).

29. Lawrence Susskind and Joshua Secunda contend that the EPA "was designed to carry out a *quasi-military* mission." Lawrence Susskind & Joshua Secunda, *The Risks and the Advantages of Agency Discretion: Evidence from EPA's Project XL*, 17 U.C.L.A. L. REV. 67, 68 (1998/99); *see also* ALFRED MARCUS, PROMISE AND PERFORMANCE: CHOOSING AND IMPLEMENTING AN ENVIRONMENTAL POLICY (1980).

30. Thus, the Agency's mission was defined clearly in pro-environmental terms in enabling legislation, in part to attract environmentally concerned professionals to the Agency, and also to facilitate legal challenges by environmental interest groups in the event the Agency swayed from this path in the future. *See* MARCUS, *supra* note 29.

31. For a discussion of the dynamics of this avenue of control, and its application to the appointment of a hostile EPA Administrator (Anne Burford) by Ronald Reagan, see Spence, *supra* note 16, at 430-32.

32. For an argument to this effect, see, e.g., Terry M. Moe, *The Politics of Structural Choice: Toward a Theory of Public Bureaucracy*, *in* ORGANIZATION THEORY: FROM CHESTER BARNARD TO THE PRESENT AND BEYOND 116-53 (Oliver Williamson ed., 1990) [hereinafter Moe, *Structural Choice*]; Terry M. Moe, *Political Institutions: The Neglected Side of the Story*, 6 J.L. ECON. & ORG. 213, 226 (Special Issue 1990). This does not mean, of course, that future agencies cannot reverse the policy, they can. That is what happened (and what the Supreme Court approved) in *Chevron U.S.A., Inc. v. Natural Resources Defense Council*, 467 U.S. 837, 866 (1984).

33. We should note that Congress often specifies that particular policies must be embodied in formally promulgated rules. This too can be explained as a precautionary device against

Of course, there are all sorts of other reasons to engage in rulemaking, not the least of which is the desire to strengthen the effect of favored policies by giving them the force of law. In addition, Kenneth Culp Davis has made the case for rulemaking as an objectively superior process, one that maximizes fairness, access, and certainty in administrative law.[35] However, scholars from a variety of disciplines have identified some of the drawbacks and unintended consequences of rulemaking as a policymaking device. One group of critics argues that overuse of rulemaking has slowed agency decisionmaking and has multiplied interest group opportunities to challenge agency decisions in court, causing an explosion of administrative litigation and a consequent reordering of administrative priorities. This, in turn, has made agencies gun-shy and has produced an "ossified" agency decisionmaking process that is less flexible, less rational, and less effective.[36] Another group of critics argues that rulemaking necessarily begets certain varieties of substantive inefficiencies because the task of writing an "optimally specific" rule is difficult, if not impossible.[37] Most of the time, one size does not fit all. For that reason,

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capture instigated by environmental interests and their congressional allies. *See* Moe, *Structural Choice*, *supra* note 32.

34. The term "capture" is beginning to fall inte disfavor, primarily because it is vague and because of its conspiratorial or pejorative connotations, which may not be appropriate. For a discussion of the varieties of capture, see David B. Spence, *Agency Discretion and the Dynamics of Procedural Reform*, 59 PUB. ADMIN. REV. 425, 426 (1999).

35. *See* KENNETH CULP DAVIS, DISCRETIONARY JUSTICE: A PRELIMINARY INQUIRY (1969).

36. This argument has sparked a lively debate. *See, e.g.*, SPICER, *supra* note 15, at 73-76; Robert A. Anthony & David A. Codevilla, *Pro-Ossification: A Harder Look at Agency Policy Statements*, 31 WAKE FOREST L. REV. 667, 676-80 (1996); *Bending the Rules: Flexible Regulation and Constraints on Agency Discretion*, Unpublished Paper, Florida State University School of Law, 1999 (on file with authors) (arguing, among other things, that agencies' ability to evade procedural mandates helps ameliorato the ossification problem); Jody Freeman, *Collaborative Governance in the Administrative State*, 45 U.C.L.A. L. REV. 1, 18 (1997) (arguing that "adversarialism . . . has contributed te a rigid rulemaking and implementation process that fails to encourage creativity, adaptation, and cooperation in solving regulatory problems"); Thomas O. McGarity, *A Cost-Benefit State*, 50 ADMIN. L. REV. 7, 26 (1998); Thomas O. McGarity, *Some Thoughts on Deossifying the Rulemaking Process*, 41 DUKE L.J. 1385 (1992); Thomas O. McGarity, *The Courts and the Ossification of Rulemaking: A Response to Professor Seidenfeld*, 75 TEX. L. REV. 525 (1997); Mark Seidenfeld, *Demystifying Deossification: Rethinking Recent Proposals to Modify Judicial Review of Notice and Comment Rulemaking*, 75 TEX. L. REV. 483 (1997); Richard J. Pierce, Jr., *Seven Ways to Deossify Agency Rulemaking*, 47 ADMIN. L. REV. 59, 82-86 (1995); Cass R. Sunstein, *Congress, Constitutional Moments, and the Cost-Benefit State*, 48 STAN. L. REV. 247 (1996) (advocating more adaptive rules).

37. *See* HOWARD, *supra* note 1, at 27 ("Once the idea is to cover every situation explicitly, the words of law expand like floodwaters that have broken through a dike. Rules elaborate on prior rules; detail breeds greater detail. There is no logical stopping point in the quest for certainty."); SPICER, *supra* note 15; Colin Diver, *The Optimal Precision of Administrative Rules*, 93 YALE L. J. 65, 76 (1983) ("The degree of precision appropriate to any particular rule depends

crafting a rule that simultaneously provides meaningful guidance to private sector actors and accommodates the myriad circumstances it will encounter over the course of its lifetime is a Herculean task, one that most rule writers fail. The attempt to accommodate specific situations (either at the drafting stage or in subsequent revisions) can make rules complicated and unwieldy, as the previously cited Yorktown Project illustrates.[38] It is this kind of problem that has led some scholars to propose that agencies rely minimally on rules and instead make rules on a case-by-case basis, the way common law "rules" emerge from a body of case law.[39] Others recommend ways to make rules more adaptable and accommodating, such as writing less specific rules, authorizing waivers, and the like.[40] Indeed, it is this need to make exceptions to rules that lies at the root of many of the EPA reform initiatives, a subject to which we turn now.

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on a series of variables peculiar to the rule's author, enforcer, and addressee. As a consequence, generalizations about optimal rule precision are inherently suspect."); Cass R. Sunstein, *Problems With Rules*, 83 CALIF. L. REV. 953, 1021 (1995) ("A system dedicated to the rule of law is committed to limiting official discretion, but it is not committed to the unrealistic goal of making every decision according to judgments fully specified in advance.").

38. *See supra* note 24 and accompanying text. For an exploration of this phenomenon in federal regulations, see HOWARD, *supra* note 1, at 17-18 (describing legal impediments to "sensible" mass transit policy in New York).

39. This is what Michael Spicer proposes. *See* SPICER, *supra* note 15. Likewise, Sunstein prescribes a system of "casuistry" and "privately adaptable rules . . . that allocate initial entitlements but do not specify end states." Sunstein, *supra* note 37, at 958. Freeman prescribes "provisional" rules that allow for adaptation of the rule to new, unforeseen circumstances. Freeman, *supra* note 36, at 22.

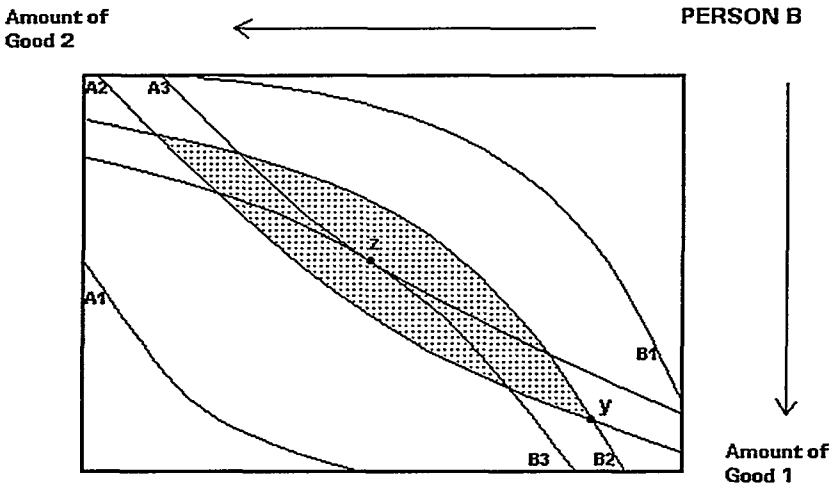
40. The delegation to an agency of the right to create regulations implies the right to waive regulations. *See* WAIT Radio v. F.C.C., 418 F.2d 1153, 1157 (D.C. Cir. 1969). Likewise, the U.S. Supreme Court has authorized the EPA to grant waivers, absent explicit statutory authority to do so, in at least one instance. *See* Chemical Mfrs. Ass'n v. N.R.D.C., 470 U.S. 116, 163-65 (1985) (upholding the EPA's variance program under the Clean Water Act as a reasonable way of ensuring that the Agency's "necessarily rough-hewn" rules do not impose a hardship on atypical firms). The Supreme Court's holding that an agency decision *not* to take enforcement action was unreviewable sparked a debate over the reviewability of waiver decisions. *See* Heckler v. Chaney, 470 U.S. 821, 828 (1985). For a good discussion of the legal authority for granting waivers to rules and the reviewability of waiver decisions, see generally Jim Rossi, *Waivers, Flexibility and Reviewability*, 72 CHI-KENT L. REV. 1359 (1997). *See also* Dennis D. Hirsch, *Bill and Al's XL-ent Adventure: An Analysis of the EPA's Legal Authority to Implement the Clinton Administration's Project XL*, 1998 U. ILL. L. REV. 129, 160-65 (1998) (arguing that the EPA has a broad implied waiver authority to make exceptions to regulatory requirements); Bradford C. Mank, *The Environmental Protection Agency's Project XL and Other Regulatory Reform Initiatives: The Need for Legislative Reauthorization*, 25 ECOLOGY L. Q. 1, 24-26, 31-34 (1998); Charles C. Caldart & Nicholas Ashford, *Negotiation as a Means of Developing and Implementing Environmental Policy*, 22-23 (1998) (unpublished working paper on file with author) (discussing the legal authority for waiving regulatory requirements in existing environmental statutes, and the EPA's reluctance to use its waiver authority).

II. THE BARGAINING SOLUTION IN THEORY AND PRACTICE

A. Bargaining Theory

Of course, microeconomics offers a familiar framework for analyzing and solving the inefficiency problems facing the regulatory system. It is a fundamental axiom of neoclassical microeconomics that, under certain conditions, a Pareto optimal distribution should be achieved through bargaining.[41] This notion is commonly illustrated through the use of a so-called "Edgeworth Box."[42]

FIGURE 1: The Standard Edgeworth Box Analysis



41. Indeed, this basic notion underlies the First Fundamental Theorem of welfare economics. Under the First Fundamental Theorem, if a perfectly competitive market exists, then the competitive market equilibrium is Pareto optimal. A perfectly competitive market economy exists when: (i) consumers maximize utility and consumer preferences are "convex" such that the marginal utility of a good decreases with increasing amounts of the good; (ii) consumer preferences satisfy nonsatiation, i.e., "more is better;" and (iii) there are no "market failures," that is, markets exist for all goods, there are no externalities, and increasing returns to scale (and natural monopolies) do not exist. *See, e.g.*, DAVID M. KREPS, A COURSE IN MICROECONOMIC THEORY 199-200 (1990). *See also* HAL R. VARIAN, INTERMEDIATE MICROECONOMICS: A MODERN APPROACH 51-52 (1990).

42. This device is named after Francis Ysidro Edgeworth, an English economist. The Edgeworth Box assumes a two person, two-good economy, and uses the microeconomic concept of "indifference curves" to illustrate why private bargaining among individuals should lead to a

Consider Figure 1, which depicts the standard Edgeworth Box bargaining process. Every point in the Box represents a potential division of the total amount of goods 1 and 2 between persons A and B. Assume that A's utility increases moving from indifference curve[43] A1 to A3, and that B's utility increases from B1 to B3.[44] It is easy to demonstrate that point *y* in Figure 1 is not Pareto optimal. Indeed, all the points in the shaded area represent distributions that are Pareto superior to *y* because the parties can move to higher indifference curves (and greater levels of utility or satisfaction) by voluntarily engaging in trades that take them into the shaded areas from these initial distribution points. Given an initial distribution at point *y*, trades that place the parties at point *z* will put each party on a higher indifference curve. Hence, point *z* is Pareto superior to point *y*. In fact, point *z* represents a Pareto optimal distribution because it, like all Pareto optimal distributions within the Edgeworth box, is at a point in which the indifference curves of A and B are tangent to one another.[45] At these points of tangency, any trade that moves one person to a higher indifference curve will move the other to a lower one. Hence, these points are Pareto optimal. In this way, bargaining over changes in the regulatory status quo might also produce Pareto improvements—positive-sum gains—in the regulatory process.

Pareto optimal distribution of goods in the usual case. For a straightforward and fairly thorough discussion of indifference curves, see VARIAN, supra note 41, at 33-52.

43. Of course, as the name implies, the indifference curve represents the various combinations of goods 1 and 2 between which person A is indifferent. In other words, at every point on indifference curve A1, person A has the same level of utility as she would at any other point on that curve. She is indifferent between the various combinations of goods represented by that curve. In this way, the shape of the curves shows A's marginal rate of substitution between the two goods, or the rate at which person A is willing to exchange amounts of good 1 for amounts of good 2, over a range of possible combinations. The marginal rate of substitution is actually the slope of the indifference curve.

44. Curves that are farther from the origin represent higher levels of utility. Thus, A would be happier with a distribution on curve A2 than curve A1. In the usual case, indifference curves look like those shown in Figure 1. That is, they are monotonic, with a decreasing slope as *x* (or the amount of good 1 in person A's bundle) increases. This means that over the range of choice examined, more of each good is better, implying a negative slope to the curve. *See* VARIAN, *supra* note 41, at 44-46. Hence, economists say that "well-behaved" indifference curves are convex to the origin. Convexity implies that the marginal rate of substitution for a good decreases over increasing amounts of that good. This assumes away the notion of satiation—i.e., that there are distributions of goods at which a person may not prefer more of a particular good. While the assumption of monotonicity assumes away the notion of satiation, the assumption of convexity reflects the decreasing marginal utility of a good at higher amounts of the good. This is, of course, true for many goods. *See id.*

45. This generalization holds true assuming well-behaved preferences for both parties.

B. Bargaining Experiments

The Clinton Administration gave voice to this prescription for regulatory inefficiency primarily through the Gore Report on "reinventing government," and through subsequent studies and initiatives to reinvent administration at the federal government level.[46] Like the scholarship that preceded them, these reports concluded that, as a product, environmental regulation was sometimes too prescriptive and too detailed, and that those detailed prescriptions sometimes foreclosed opportunities for more efficient and effective ways to achieve regulatory goals.[47] They urged the EPA to explore the further use of market incentives and risk-based decisionmaking, as well as opportunities for greater cooperation with states, local governments, citizens and industry.[48] For its part, the EPA undertook a series of regulatory initiatives designed to promote pollution reduction by industry[49] and to facilitate more cooperative approaches to regulation.[50] Among the latter were the four reforms described below, each of which: (i) embodies a more cooperative, less formal, and less adversarial approach to regulation as a means to achieve existing environmental goals more efficiently; (ii) seeks to enable regulators to take advantage of the specialized knowledge of industry in order to avoid regulatory

46. *See* GORE, *supra* note 8. The move to reinvent the EPA was also spurred on by a series of reports by the National Academy of Public Administration ("NAPA") that focused exclusively on reforming environmental regulation. *See* NAPA, SETTING PRIORITIES, *supra* note 9; NAPA, RESOLVING THE PARADOX, *supra* note 9.

47. *See, e.g.*, GORE, *supra* note 8, at 138-39 (specifically Recommendations EPA01, EPA02, and EPA04); NAPA, SETTING PRIORITIES, *supra* note 9, at 97-104.

48. *See* NAPA, SETTING PRIORITIES, *supra* note 9, at 100-104. Indeed, the Gore Report explicitly urged agencies to make more and better use of negotiated rulemaking and other consensus-based processes. *See* GORE, *supra* note 8, at 118-19.

49. For analyses of the EPA's voluntary programs, see generally Terry Davies & Jan Mazurek, Industry Incentives for Environmental Improvement: Evaluation of U.S. Federal Initiatives (1996) (on file with the Global Environmental Management Inst.); Michael Gearhart, *Case Studies in the Implementation of Voluntary Environmental Management System Standards*, Resenbaum News & Views *available at* <http://www.lawinfo.com/law/ca/environmentallaw/archives/news_v2n2.htm#Case_Studies> and <http://www.lawinfo.com/law/ca/environmentallaw/archives/Gearhart.htm>; Madhu Khanna & Lisa Damon, EPA's Voluntary 33/50 Program: Impact on Toxic Releases and Economic Performance of Firms, University of Illinois at Urbana-Champaign Environmental and Resource Economics Working Paper #8 (1997); James McCarthy, Voluntary Programs to Reduce Pollution, Congressional Research Service Report for Congress (1995).

50. The Administrative Procedures Act ("APA") authorizes the use of negotiated rulemaking. *See* 5 U.S.C. §§ 561-570 (1994). Shortly after the Gore Report, the President signed Executive Order 12,866, which directed executive branch agencies to explore the use of "consensual mechanisms for developing regulations" and to use negotiated rulemaking where possible. *See* Exec. Order No. 12866, 3 C.F.R. 638, 645 (1993).

inefficiencies; and (iii) has met with considerable resistance and criticism from opponents of reform.

1. Project XL

The Clinton Administration first announced the Project XL[51] program in March 1995.[52] The program was modeled after the Amoco/Yorktown example.[53] The EPA had high ambitions for Project XL, promising to implement fifty pilot projects by mid-1997.[54] Under the program, individual firms could propose changes in the environmental compliance activities at their facilities. The EPA initially established eight objectives that would guide their selection of projects for Project XL, representing a combination of environmental, cost-efficiency and other factors.[55] Despite high hopes that the program would provide an avenue for consensus-based, positive-sum change in environmental policy, the program experienced an early setback on September 5, 1996, when the sponsor of one of the program's most promising early proposals—the Minnesota-based 3M Company—notified the EPA that it was withdrawing from the Project XL process. As late as June 1996, the EPA, 3M, and the state had seemed close to an agreement on the project, and company representatives seemed confident that the 3M plant was in line to receive the first-ever multimedia permit.[56] One of the reasons cited for 3M's withdrawal was a dispute over whether 3M's proposal would satisfy the Agency's requirement that XL projects achieve superior environmental performance.[57]

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51. In an unfortunate attempt to force an acronym upon a catch-phrase, the "XL" stands for "eXcellence and Leadership."

52. *See* Regulatory Reinvention (XL) Pilot Projects, 60 Fed. Reg. 27,282 (1995).

53. *See supra* note 24 and accompanying text.

54. *See* Regulatory Reinvention (XL) Pilot Projects 60 Fed. Reg. 27,282.

55. Those eight criteria were: (1) superior environmental performance; (2) cost savings; (3) support of interested stakeholders, including local communities and governments; (4) testing of new and innovative processes that prevent the generation of pollution; (5) testing of new approaches that could be incorporated into other EPA programs; (6) technical and administrative feasibility; (7) making information about the project available to interested parties for evaluating success; and (8) ensuring compliance with Executive Order 12,898 on environmental justice. *See id.* at 27,287.

56. *See 3M decides to drop out of Project XL process after disagreement over performance guarantees*, 27 Envtl. Rep. (BNA) 1045, 1046 (1996); Christina M. Buelow, Barriers to Regulatory Reform as Experienced in the 3M Project XL Pilot 18-21 (May 1997) (unpublished Master's thesis, Duke University) (on file with authors); Alfred Marcus et al., A New Competence in Environmental Management: Lessons from Project XL in Minnesota, presented at the Wharton Impact Conference on Environmental Contracting, Philadelphia, PA (1999).

57. 3M proposed reductions in the allowable emission levels under its air permit, a benefit that participants in the bargaining process appeared to believe satisfied the criterion. Some at the EPA disagreed, however, apparently because 3M's actual emissions had been below even the

The 3M experience led the Agency to reevaluate the XL process. In early 1997 the EPA revised its decision criteria by stating that the Agency would emphasize three factors in deciding whether to approve an XL proposal in the future: (i) whether the proposal would achieve superior environmental performance (which the EPA also defined more precisely); (ii) whether the type of regulatory flexibility methods proposed were appropriate and might serve as a model for other projects; and (iii) whether the proposal contained adequate opportunities for involvement by stakeholders.[58] Since the 1997 notice, several high-profile companies have secured approval for their XL proposals. However, progress in the XL program has not kept pace with expectations. While the program has succeeded in identifying opportunities for positive-sum change,[59] it appears that only a subset of those opportunities are being realized. As of September 1999, the EPA had approved only 14 projects for implementation; in the same time period, three times as many projects had been rejected or the sponsoring companies had withdrawn the projects from consideration.[60] Perhaps more importantly, the program has been the object of some scorn within the Agency,[61] where its legality and wisdom have been questioned. Environmental interest groups[62] and commentators[63] have echoed these concerns, particularly the fear that XL

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reduced levels. *See* Buelow, *supra* note 56; Marcus, *supra* note 56. For further discussion of this issue, see Section IV, *infra*.

58. *See* Regulatery Reinvention (XL) Pilot Projects, Notice of Modifications to Project XL, 62 Fed. Reg. 19,872 (1997).

59. In addition to the 3M example, other XL proposals (such as the Berry and Intel projects) would involve emissions reductions coupled with increased compliance flexibility for industry. *See Project XL*, <http://yosemite.epa.gov/xl/xl_home.nsf/all/homepage>. For an in-depth study of the Intel proposal, see James Boyd, et al., Intel's XL Permit: A Framework for Evaluation (1998) (Resources for the Future Discussion Paper 98-11). The Merck XL project addressed a prototypical example of rule-based inefficiency. Under applicable ozone regulations, small changes in emissions of volatile organic chemicals ("VOCs") at the Merck facility would have triggered costly permitting requirements, even though the change would not increase ozone concentrations due to the unusual characteristics of the area (low levels of nitrogen oxides, a necessary precursor of ozone). *See* Hirsch, *supra* note 40, at 143-46.

60. *See Project XL*, <http://yosemite.epa.gov/xl/xl_home.nsf/all/homepage>.

61. An internal EPA newsletter quoted an unidentified EPA staffer as saying, "If it isn't illegal, it isn't XL." This quotation has been reproduced in a number of places. *See, e.g.*, Rena Steinzor, *Regulatory Reinvention and Project XL: Does the Emperor Have Any Clothes?*, 26 ENVTL. L. REP. 10527 (citing What's Up With Project XL — Week of 3/11/96, Project XL update).

62. *See* Cindy Skrzycki, *Critics See a Playground for Polluters in EPA's XL Plan*, THE WASH. POST, Jan. 24, 1997, at D1 ("Environmental and citizens' groups have their own names for what the Environmental Protection Agency's Project XL stands for: Instead of EXcellence and Leadership, they call it 'EXtra Leniency'.")

projects will bring environmental harm, and the concern that the projects often require variances or exemptions from legal requirements.[64] However, despite a recent groundswell of criticism, the program continues. Indeed, compared to many of the EPA's other reform initiatives, XL's future seems relatively secure.

2. Negotiated Rulemaking

Negotiated rulemaking can be conceived of as Project XL writ large, in that it employs the same goals and methods on a broader scale. While negotiated rulemaking takes place throughout the executive branch, nowhere has it been used as frequently and extensively as it has at the EPA.[65] In theory, negotiated rulemaking is designed to bring stakeholders into the regulation development process earlier, to promote the sharing of information and perspectives among stakeholders and the Agency, and thereby to produce better and less controversial rules.[66] Given the amount of resources that the EPA devotes to rulemaking and litigation in defense of its rules,[67] it is not surprising that the EPA has used negotiated rulemaking frequently. Indeed, if negotiated rulemaking can produce less controversial rules, there is good reason to expect that the EPA ought to use the process frequently. However, despite its eager embrace of negotiated rulemaking, the EPA's experiences with the process have met with a

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63. *See, e.g.*, William H. Miller, *Washington Wreck*, INDUSTRY WK., Aug. 18, 1997, at 116 (concluding that Project XL "has gotten off to a disappointing—some critics would say disastrous—start") For additional discussion of criticisms of the XL program, see *infra* Section III.

64. *See* Geltman & Skroback, *supra* note 18, at 33-34 (contending that Project XL operates "contrary to" the law); Mank, *supra* note 40, at 24-28, 70-88 (arguing that the XL program lacks the statutory authority to waive regulatory requirements, and urging legislative reform te authorize XL); Rena I. Steinzor, *Reinventing Environmental Regulation: The Dangerous Journey from Command to Self-Control*, 22 HARV. ENVTL. L. REV. 103, 134-36 (1998).

65. For a summary of the EPA and other agencies' use of negotiated rulemaking, see generally Cary Coglianese, *Assessing Consensus: The Promise and Performance of Negotiated Rulemaking*, 46 DUKE L.J. 1255, Appendices A & B (1997). For a summary of the EPA's negotiated rulemaking experience, see Laura Langbein & Cornelius Kerwin, Regulatory Negotiation Versus Conventional Rulemaking: Claims, Counter-claims, and Empirical Evidence, 6-11 (1998) (unpublished manuscript, George Washington University School of Public Affairs) (on file with authors).

66. Philip Harter is sometimes cited as the leading force behind the APA's endorsement of negotiated rulemaking. *See* Philip J. Harter, *Negotiating Regulations: A Cure for Malaise*, 71 GEO. L.J. 1 (1982) (summarizing his arguments in favor of negotiated rulemaking); *see also* Freeman, *supra* note 36, at 33-40.

67. For two good analyses of the litigation process that follows EPA rulemakings, see generally CARY COGLIANESE, CHALLENGING THE RULES: LITIGATION AND BARGAINING IN THE ADMINISTRATIVE PROCESS (Book Manuscript, Harvard University) (1995); ROSEMARY O'LEARY, ENVIRONMENTAL CHANGE: FEDERAL COURTS AND THE EPA (1993).

decidedly mixed reaction. Its critics contend that the process (i) has not produced better, more widely-accepted regulations; (ii) has not saved agency resources;[68] (iii) has not helped the Agency avoid litigation;[69] and (iv) represents an abdication of the Agency's decisionmaking responsibilities to private sector participants in the negotiation process.[70] Its defenders dispute these contentions,[71] and argue that negotiated rulemaking has produced some benefits that are difficult to quantify or measure.[72] Whatever the ultimate verdict, the process of negotiated rulemaking remains controversial, particularly among environmental groups.

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68. *See* Coglianese, *supra* note 65, at 1321 (arguing that there is little or no difference in the likelihood that a negotiated rule will be challenged in court compared with a traditionally promulgated rule, and that promulgating negotiated rules consumes no fewer resources than traditional notice and comment rulemaking); *see also* Steven J. Balla & John R. Wright, Consensual Rulemaking and the Time it Takes to Develop Rules, (paper presented at the Fifth Annual Conference on Public Management, College Station, TX (Dec. 3-4, 1999)) (unpublished, on file with authors) (finding that negotiated rulemaking processes have no discernible effect on the duration of rulemaking proceedings); Caldart & Ashford, *supra* note 40, at 10-11 (arguing that negotiated rulemaking has not delivered on its primary promised benefits of reduced rulemaking time and reduced litigation).

69. *See* Coglianese, *Assessing Consensus*, *supra* note 65, at 1321 (concluding that negotiated rulemaking "actually creates new sources of potential conflict in the regulatory process" by providing additional opportunities "to disrupt the consensus . . . .").

70. *See* William Funk, *Bargaining Toward the New Millenium: Regulatory Negotiation and the Subversion of the Public Interest*, 46 DUKE L.J. 1351, 1374-86 (1997). For a more detailed discussion of this issue, see *infra* Section IV.

71. Langbein and Kerwin offer a defense to many of these criticisms. Based on a survey of participants in negotiated rulemakings, they conclude that rules selected for negotiated rulemaking tend to be more complex and controversial to begin with, raising the question of whether comparisons like Coglianese's are fair. *See* Langbein & Kerwin, *supra* note 65, at 35. Coglianese disputes this conclusion. *See* Coglianese, *supra* note 65, at 1311-21. Langbein & Kerwin also find no support in their data for the notion that the EPA abrogates its decisionmaking authority in negotiated rulemakings. *See* Langbein and Kerwin, *supra* note 65, at 35-36.

72. Freeman, for example, argues that negotiated rulemaking cannot be judged fairly according to traditional regulatory goals, such as litigation avoidance. Rather, by allowing participants to "transcend[ ] the public-private divide," the process enables participants and policymakers to discover flexible solutions to problems that they would not have discovered otherwise. Freeman, *supra* note 36, at 33-54; *see also* Philip J. Harter, *Fear of Commitment: An Affliction of Adolescents*, 46 DUKE L. J. 1389, 1403 (1997) (arguing that the "rules that emerge through negotiated rulemaking reflect a shop-floor insight and expertise . . . [and they] take account of issues that would likely escape the attention of an agency in traditional rulemaking."); Langbein & Kerwin, *supra* note 65, at 35-36 (contending that the negotiated rulemaking process produces "better" rules irrespective of the probability of subsequent litigation, because participants are more satisfied with negotiated rules, and clarify more disputed issues in negotiated rulemakings).

3. The Common Sense Initiative

Another of the EPA's "flagship" reform initiatives, the Common Sense Initiative ("CSI"), was designed to bring together representatives of six environmentally significant industrial sectors of the economy: automobile manufacturing, computers and electronics, iron and steel, printing, metal finishing, and petroleum refining.[73] Representatives of individual firms within each sector meet regularly with EPA representatives and other interested stakeholders to explore opportunities to improve environmental regulation within each sector. More specifically, each group tries to identify opportunities for changing unnecessarily complex or inconsistent requirements within the existing regulatory structure. The hope is that by meeting face-to-face outside of the usual inspection and euforcement context, participants will be able to identify opportunities for positive-sum improvements in regulation.[74] In the words of the EPA, the CSI approach seeks to move regulation "from conflict to consensus, from piecemeal to holistic, and from inflexibility to innovation."[75]

Since the program was launched in 1994, sector representatives have met on a regular basis. Their initial proposals, called "projects" in CSI parlance, were modest. Most involved relatively small or incremental changes to the regulatory system, such as the iron and steel sector committee's proposal to develop a model community relations program for sector firms.[76] The program's modest achievements have provoked criticism from within and without,[77] and led to an EPA-

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73. The ongoing progress of the CSI groups is chronicled on the EPA's CSI Web Site. *See* EPA, *Common Sense Initiative* (visited Jan. 16, 2000) <http://www.epa.gov/commonsense/> (*CSI Web Site*).

74. *See CSI Web Site*, <http://www.epa.gov/commonsense/>.

75. *See CSI Web Site*, <http://www.epa.gov/commonsense/bckgrd.htm>.

76. *See CSI Web Site*, <http://www.epa.gov/commonsense/3table.htm> ("Community Involvement Project").

77. *See, e.g.*, Susan Bruninga, *Browner Touts Reinvention Progress, Says 50 XL Projects Expected by Late 1999*, 28 Envtl. Rep. (BNA) 2529-30 (1998) (chronicling some criticisms of the CSI program); Cheryl Hogue, *NAPA Panel Proposes New Law to Allow Rules Integration Under Existing Statute*, 28 Envtl. Rep. (BNA) 902, 903 (1997) (quoting the NAPA panel's assertion that CSI has failed to produce "a bold solution to an environmental problem that can capture the public's imagination or ignite industry's enthusiasm"); *The Federal-State Relationship: A Look Into EPA Regulatory Reinvention Efforts Before the Subcommittee on Oversight and Investigations of the House Comm. On Commerce*, 105th Cong. 34 (1997) (prepared statement of Russell J. Harding, Director, Michigan Department of Environmental Quality) (calling his state's experience with CSI "very disappointing," and attributing the program's failures to the EPA's "decision to base all actions and decisions on the concept of stakeholder consensus.") The General Accounting Office has also criticized CSI. *See* GENERAL ACCOUNTING OFFICE, PERFORMANCE AND ACCOUNTABILITY SERIES: MAJOR MANAGEMENT CHALLENGES AND PROGRAM RISKS—EPA (GAO/OCG-99-17) (Jan. 25, 1999); GENERAL ACCOUNTING OFFICE, ENVIRONMENTAL PROTECTION:

sponsored review of CSI in 1997.[78] Since that review, CSI committees have set their sights on more fundamental changes. The first sector-wide CSI agreement was reached among participants in the metal finishing sector group. The agreement commits members of the industry to a series of toxics-use reduction efforts and "beyond compliance" performance targets, in exchange for removal of certain specific regulatory barriers to efficient compliance.[79] Despite this change in focus within CSI, however, the program has not met its proponents' initially high expectations, and the EPA has decided to merge the program into another industrial sector-based regulatory program.[80]

4. The Environmental Leadership Program

Despite its promise, the Environmental Leadership Program ("ELP") has remained one of the EPA's lesser-known reform initiatives. The original aim of the ELP was to identify companies with particularly sophisticated and successful environmental management programs ("environmental leaders"), and to harness the knowledge that those firms could bring to the task of environmental compliance to benefit others. In 1994, the EPA invited proposals for pilot projects from environmental leaders in the private sector.[81] In 1995, the EPA selected twelve well-known, large companies with considerable environmental compliance experience for participation in the program.[82] As originally conceived, the program was to have had several phases, the first of which involved information sharing between teams of representatives from each company, representatives of the EPA, and, in some cases, other stakeholders. In this way, regulators could gain

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CHALLENGES FACING EPA'S EFFORTS TO REINVENT ENVIRONMENTAL REGULATION (GAO/RCED-97-155) (July 2, 1997). EPA Administrator Carol Browner defends CSI, but admits that CSI's lessons have not been integrated into the EPA's daily operations. *Browner Announces New Phase of CSI, Wants Thorough Use of Sector Approach*, 28 Envtl. Rep. (BNA) 2310, 2310 (1998).

78. *See* EPA, COMMON SENSE INITIATIVE UPDATE (Mar, 1997); *Common Sense Initiative Considers Involvement in Broader Environmental Issues*, 28 Envtl. Rep. (BNA) 2177 (Feb. 28, 1997).

79. *See CSI Web Site, supra* note 73, at <http://www.epa.gov/commonsense/CSIsect.html> ("Promoting Improved Performance Flexible Track Project (Metal Finishing 2000)").

80. The EPA is folding the work of CSI into something called the Standing Committee on Sectors of the National Advisory Council on Environmental Policy and Technology. *See* Susan Bruninga, *Multi-Stakeholder Process Applauded; Improvements Needed, CSI Council Told*, 29 Envtl. Rep. (BNA) 1702, 1702 (1999).

81. *See* Environmental Leadership Program: Update, 59 Fed. Reg. 4066 (January 28, 1994); Environmental Leadership Program: Request for Pilot Project Proposals, 59 Fed. Reg. 32,062 (June 21, 1994).

82. *See* EPA, *Environmental Leadership Program*, <http://es.epa.gov/elp/pilots.html> .

access to companies' expertise and companies could build trust with regulators.

The ELP pilot projects moved forward in 1995 and 1996. While the particular approaches of each individual project team varied, many spent their time conducting detailed environmental audits of the participating firms' facilities, and reviewing the firms' environmental management systems.[83] As a condition for this sharing of information, the EPA promised not to bring enforcement actions against the companies for violations identified during the course of these reviews, so long as the violations were corrected promptly.[84]

The primary goals of ELP Phase I were to identify innovative environmental management techniques used by participating firms, and to explore ways in which those techniques could be made available to other, less sophisticated companies. An additional purpose of Phase I was to explore ways in which the EPA could extend the ELP process beyond the original 15 participants.[85] By most accounts, Phase I was a success in that it helped the EPA to identify innovative approaches to environmental management, and built trust between EPA representatives and the participating firms.[86] Relatively few compliance violations were discovered during the environmental audits performed during Phase I, and all were corrected in a timely manner.[87] Phase I was less successful in identifying ways in which the EPA could extend the ELP approach more broadly, and the participants have been unable to come to any consensus about other ways of extending the program further. As of this writing, the program is "on hold."[88]

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83. *See* Kira A. Jacobs, The Environmental Leadership Program: A Case Study of an EPA Pilot Project 14-17 (1997) (unpublished Master's Project, Duke University Nicholas School of the Environment) (on file with authors); *Companies Might See Fewer Inspections, Faster Permitting Under EPA Initiative*, 26 Envtl. Rep. (BNA) 1289, 1289 (Dec. 1, 1995) (*Companies Might See Fewer Inspections*); *Innovative Initiative to Provide Facilities Relief Headed for Launch in 1997, Program Chief Says*, 27 Envtl. Rep. (BNA) 1347, 1347 (Oct. 18, 1996) (*Innovative Initiative*).

84. *See Enforcement: Inspections at Plants to be Suspended in Environmental Leadership Pilot Program*, 25 Envtl. Rep. (BNA) 2448 (Apr. 14, 1995); Jacobs, *supra* note 83, at 3; *Innovative Initiative*, *supra* note 83; *Companies Might See Fewer Inspections*, *supra* note 83.

85. *See Innovative Initiative*, *supra* note 83; Jacobs, *supra* note 83, at 3-5; EPA, *Environmental Leadership Program*, <http://es.epa.gov/elp/pilots.html>.

86. The program director pronounced the pilot phase a success. *See Innovative Initiative*, *supra* note 83, at 1347; *see also* Jacobs, *supra* note 83, at 46-47.

87. The discovery of these violations in the facilities of environmentally sophisticated firms who had advance notice of the audits seems to underscore the difficulty of maintaining perfect regulatory compliance.

88. *See* EPA, *Environmental Leadership Program*, <http://es.epa.gov/elp/>. The EPA has repeatedly postponed the date for launching the next, broader phase of the program, and the program's fate is in the hands of the Office of Enforcement and Compliance Assurance. *See*

C. Regulatory Reform at a Crossroads

It seems clear that none of these initiatives has produced the kind of widespread efficiency improvements that might have been expected based upon bargaining theory, though that may be an unrealistic goal in the contentious, polarized world of environmental policymaking. In each of these examples, the EPA was able to bring industry and environmental interests (from inside and outside the Agency) together to share information and to seek positive-sum change through consensus. However, consensus was not always forthcoming, even in support of what appear to be clear Pareto improvements. No doubt, critics of reform are at least partially correct when they ascribe the disappointing performance of the EPA reforms to legal and political impediments. That is, some regulatory reforms do run up against statutory and other legal constraints, and those constraints certainly do reflect policy values other than cost-effectiveness and flexibility. Legal impediments are only part of the story, however. Rather, the better part of the explanation is political—and logical. The next Section examines arguments raised by the anti-reform constituency, then looks behind those arguments to explore the logical and strategic reasons why important stakeholders might oppose efficiency improvements.

III. BARGAINING, COLLABORATION, AND STRATEGIC BEHAVIOR

A. The Critique of Reform

In recent years, defenders of traditional regulatory approaches have answered the pro-reform critique with their own vigorous critique of reform generally, and of cooperative approaches to regulation in particular. Their critique boils down to two basic and overlapping arguments. The first challenges the goals of regulatory reform, particularly its emphasis on "efficiency" as an evaluative criterion for regulation. It argues that the very inefficiencies about which reform advocates complain serve other important purposes that trump the goal of efficiency. The second argument is that by seeking new ways to integrate stakeholders into the policy process, cooperative regulation amounts to an abdication of decisionmaking responsibility by regula-

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Cheryl Hogue, *Targeted Violations, Audit Policy Review Among EPA's 1998 Activities, Officials Say*, 28 Envtl. Rep. (BNA) 1769, 1769 (Jan. 16, 1998).

tory agencies. Critics of reform contend (or fear) that these collaborative processes are leading the EPA to cede its authority to stakeholder groups, thereby elevating the interests of these ad hoc groups over the public interest. The proponents of each of these arguments see regulatory reform as undermining the rule of law, and contend that traditional means of making law—statutes and regulations—better reflect these important values than the collaborative and/or ad hoc decision-making processes used in the EPA's various reform initiatives.

1. At What Price Efficiency?

Even if the EPA's reform initiatives were to achieve their twin goals of substantive and procedural efficiency, one might ask whether those goals are worth pursuing or, more specifically, whether the pursuit entails unacceptable costs. Defenders of traditional regulation contend that each of these goals holds a relatively low place in the list of environmental regulatory priorities, and for good reason. With respect to substantive inefficiencies, there are reasons why environmental interests might sincerely prefer regulation that is relatively cost-inefficient. After all, say defenders of traditional approaches, the primary goal of the current system is not cost-efficiency, but rather environmental protection. Hence, we ought to be careful about modifying the system, particularly in ways that divert the focus from that central goal or elevate other goals, like efficiency or flexibility, to an equal station.[89] Indeed, environmental interests argue that certain inefficient attributes of regulation—like technology-based standards—are easier to enforce than more efficient alternatives.[90] This has long been a central pillar in the case against reform. Environmental interests may also fear that efficiency and flexibility improvements are a Trojan horse bearing hidden environmental costs. Several commentators have lamented that while EPA reforms may yield overall environmental gains, they may also allow specific environmental losses in the context of those overall gains.[91] There is a general suspicion that

89. This theme runs throughout several of the critiques of regulatory reform. *See, e.g.*, Steinzor, *supra* note 64, at 105 (stressing the need to remain cognizant of the EPA's "overarching mission" of environmental protection); Heinzerling, *supra* note 18, at 460 ("[T]he express purpose of the laws regulating pollution in this country is the protection of human health and natural resources.").

90. *See generally* ROBERT V. PERCIVAL ET AL., ENVIRONMENTAL REGULATION: LAW, SCIENCE, AND POLICY. 161 (1992); *see also* Mank, *supra* note 40, at 4.

91. This is analogous to the argument that using marketable permits to regulate air pollution can create "hotspots" of concentrated emissions. *See* Steinzor, *supra* note 64, at 112, 115, 131-35 (making a similar argument in connection with Project XL).

reform in the name of efficiency may bring laxity.[92] Thus, critics of reform argue, statutory admonitions compelling inefficient regulation reflect, at least in part, a social choice in favor of giving priority to these other goals, even at the cost of substantive inefficiency.[93]

Critics of reform also challenge reformers' concern with, and prescription for, procedural inefficiencies. The critics' argument tracks closely the original justification for using rules, and reflects a continuing concern with the problem of regulatory capture. That concern, in turn, stems from a deep suspicion of the motives and trustworthiness of business participants in collaborative policy processes.[94] Rena Steinzor, for example, sees virtue in the "transparency" of rules. Rules enable environmental interests to know with greater certainty what the law is, and what it requires.[95] By introducing the possibility of individual variances into the regulatory process—indeed, by promoting that possibility—reform initiatives make it more difficult for environmental groups to keep track of the legal requirements to which regulated firms are subject.[96] Environmental groups' relative resource disadvantages exacerbate the problem,[97] making it difficult for national environmental groups to monitor developments in a more decentralized regulatory process.[98] Critics of reform note also that rules promote objectivity by treating regulated firms equally.[99] By institutionalizing departures from rules, even in the name of efficiency improvements, reform increases the opportunity for regulated firms to

92. *See id.; see also* Mank, *supra* note 40, at 4-10 (summarizing these arguments).

93. This is part of the argument raised in opposition to regulation based on risk. For a survey of that literature, see, e.g., Cross, *supra* note 18; Heinzerling, *supra* note 18.

94. Steinzor, for example, argues that industry's professions of support for environmental protection are usually disingenuous, and systematically so. *See* Steinzor, *supra* note 64, at 156-62.

95. *See id.* at 135.

96. Steinzor says that in this way Project XL promotes a "regulatory free for all." *See id.* at 138.

97. For a detailed treatment of interest group theories of environmental politics, see Daniel A. Farber, *Politics and Procedure in Environmental Law*, 8 J. L. ECON. & ORG. 59, 60-61 (1992); David B. Spence, *Paradox Lost: Logic, Morality, and the Foundations of Environmental Law in the 21st Century*, 20 COLUM. J. ENVTL. L. 145, 149-50, 168-71 (1995).

98. This is a problem primarily for individual national environmental groups trying to keep track of, or participate in, individual bargaining processes. Local environmental groups are often included in XL negotiations and negotiated rulemaking sessions as well. Steinzor claims that local environmental groups lack the sophistication to hold their own in the XL process. *See* Steinzor, *supra* note 64, at 180 ("[L]ocal citizen activists . . . lack confidence in their ability to negotiate with experts in regulatery debates . . . [and] are forced te rely on an intuitive sense of which players are trustworthy in [disputes], recognizing that their intuitions can fail.").

99. *See* Steinzor, *supra* note 64, at 135.

subvert the regulatory process—that is, to capture it.[100] Only rigorous transparent standards, say critics of reform, can prevent regulatory capture and adequately protect the environment.[101]

2. Reform as Abdication

The specter of regulatory capture also hangs over the second general argument raised against reform: namely, the argument that collaborative policy processes represent a de facto cession of EPA decisionmaking authority to private parties.[102] According to this view, collaborative processes lack legitimacy for a variety of reasons. First, reform initiatives that are designed to promote collaboration and cooperation between private stakeholders assume an interest group bargaining model of the policy process.[103] In so doing, the initiatives ignore the notion of a "public interest" apart from the collision of private interests.[104] Perhaps the most vigorous proponent of this view is William Funk, who sees some collaboration-based reforms as "perversions" of the public interest.[105] He argues that the primary purpose of administrative law is to promote the rule of law, and that agencies' actions are justified and legitimized by their faithfulness to statutory

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100. That concern over capture lies at the core of Steinzor's argument seems clear, even if she does not use the term "capture" to describe her concerns. *See id.; see also*, Funk, *supra* note 70, at 1383-85.

101. *See* Steinzor, *supra* note 64, at 182.

102. Advocates of this view include Funk, *supra* note 70; *see generally* Stephen H. Linder, Deconstructing the Public-Private Partnership, (unpublished paper presented at the Annual Meeting of the American Political Science Ass'n, Boston, MA (Sept. 3-6, 1998)); *see also* Steinzor, *supra* note 64, at 104 (seeming to endorse this view when she calls consensus-based regulation "self-regulation"); *but see id.* at 197 n.306 (acknowledging that the EPA retains final decisionmaking authority under these collaborative processes). For a good summary of the abdication argument in a larger theoretical context, see Freeman, *supra* note 36, at 82-90 (noting that fears of collusion and capture sometimes drive this argument).

103. For a good discussion of the relevance of interest group bargaining models of politics to the environmental policy process preceding the literature on regulatory reform, see Daniel A. Farber, *Contract Law and Modern Economic Theory*, 78 NW. U. L. REV. 303, 306-10 (1983). For a discussion of why we believe bargaining models illuminate the debate over regulatory reform, see *infra* text accompanying note 195.

104. This view implicitly assumes the existence of a "public interest" apart from the pull and tug of private interests, contrary to the views of most law and economics scholars who, citing Kenneth Arrow, dispute the notion of the "public interest." For a discussion of public interest model of administration and its relationship to "the Arrow problem," see Spence, *supra* note 16, at 408-15, 443-46. For a more detailed discussion of how consensus-based reform implicates these issues, see *infra* Section V.

105. Funk, *supra* note 70, at 1374 (arguing that the APA "reflects the notion of an agency acting consequentially, not politically, in an exercise of instrumental rationality," and that consensus-based processes contradict that notion).

directives.[106] This view contends that group consensus is a poor substitute for statutory authority as the basis for legitimacy. Indeed, collaborative policies stray even further from traditional sources of legitimacy by viewing statutory directives as impediments to, or constraints on, policymaking.[107] This substitution contradicts the notion of the "agency as sovereign decision-maker."[108] Several commentators also have implied that it raises potential constitutional problems under the nondelegation doctrine.[109]

A second, closely-related criticism is that collaborative processes lack legitimacy because they almost invariably omit important interests from the bargaining table. This has been a persistent criticism of negotiated rulemaking in particular[110] and of Project XL as well.[111] Because environmental problems are complex and implicate many diverse interests, it is often impossible to convene all important stakeholders in negotiation meetings. This, in turn, raises the possibility of collusion between the Agency and included interests (presumably industry) at the expense of excluded interests.[112] As a result,

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106. *See id.* Other commentators go further, seeming to take offense at the very notion that an agency might waive a rule in any given circumstance. Marianne Lavelle, for example, calls Project XL a "wink and a nod" arrangement, and describes the program this way: "Anheuser-Busch Co., Inc., 3M Co. and a handful of other corporations want the opportunity to break some federal laws in the coming months. And surprisingly, the federal government has offered its blessing." *See* Marianne Lavelle, *Bending the Rules*, NAT'L L. J., June 10, 1996, at A1.

107. Funk argues that while the APA has "accommodated" negotiated rulemaking, "it has done so in an insidious way, by having agency preamble writers make up rationalizations for decisions made on other grounds." *See* Funk, *supra* note 70, at 1374. This process, he says, "masks the reality of bargained for exchanges." *Id.* at 1375; *see also* Freeman, *supra* note 36, at 82 (giving a dispassionate summary of the legitimacy critique of collaborative approaches to policymaking, including Funk's argument).

108. Funk, *supra* note 70, at 1377; *cf.* Steinzor, *supra* note 64, at 197 n.306 (criticizing collaborative processes seems to acknowledge that the EPA retains final decisionmaking authority over policy choices); *see also* Freeman, *supra* note 36, at 87 (agreeing with Steinzor and contradicting Funk's view). For an interesting discussion of this issue in a larger context, see Jim Rossi, *Participation Run Amok: The Costs of Mass Participation for Deliberative Decisionmaking*, 92 NW. U. L. REV. 174, 203-5 (1997); see also our discussion of Rossi's view of collaborative policymaking in this context, *infra* note 198.

109. *See* Freeman, *supra* note 36, at 82 (discussing the "subdelegation" issue generally); Rose-Ackerman, *supra* note 16, at 1210 (raising potential issues).

110. *See* Coglianese, *supra* note 65, at 1321-24 (arguing that disputes over who participates in negotiations make negotiated rulemakings more conflictual than traditional rulemakings); Rose-Ackerman, *supra* note 16, at 1210;.

111. *See* Steinzor, *supra* note 64, at 180.

112. *See* Freeman, *supra* noto 36, at 83 (discussing this issue); *see also* Mark Seidenfeld, *Empowering Stakeholders: Limits on Collaboration as the Basis for Flexible Regulation*, __ WM. & MARY L. REV. __, 113-20 (2000) (arguing that Project XL stakeholder groups exclude important interests). For a particularly skeptical view of business-government collaboration, including in the environmental context, see Linder *supra* note 102, at 2 ("The idea of government and business partnering for some common purpose . . . seems to draw on communal traditions of coopera-

omitted interests see the process as illegitimate, or at least less legitimate than traditional regulatory policymaking methods.[113]

In sum, the defense of the traditional regulatory system and corresponding critique of reform is picking up steam. The next subsection offers a framework for evaluating the progress of collaboration-based reform initiatives, one that also sheds some light on the debate over those initiatives.

B. Strategic Bargaining as an Impediment to Reform

1. Two Views of the Bargaining Process

We have suggested that the Edgeworth Box can be used to analyze bargaining conflicts in the context of regulatory reform. Indeed, it is common to conceive of laws and policies in this way,[114] and many of the EPA's reforms seek to facilitate exactly this kind of bargaining. Thus, reconceiving regulatory reforms in these terms may shed some light on the debate. Figure 2 illustrates one view of bargaining over regulatory reform, one we might ascribe to proponents of reform.

In Figure 2, the "goods" at issue are attributes of regulation: namely, the legally mandated total amount of pollution reduced on the *x-axis*, and the mandated cost per unit of pollution reduced on the *y-axis*.[115] We can think of the *y-axis* as representing the means of environmental regulation, or legal mandates about how to reduce pollution, that is, the substantive or cost-efficiency of regulation. The *x-axis* represents the ends, or legal mandates about how much to reduce pollution. In Figure 2, conflict on the *x-axis* is a zero-sum conflict, in that we typically expect industry and environmental interests to clash over the question of how much to reduce pollution. However, in Figure 2, proponents of reform do not necessarily conceive of conflict on the *y-axis* as zero-sum. While industry presumably desires greater effi-

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tion that are, at once, vaguely familiar and socially valued. Of course, when we scratch the surface of these arrangements . . ., the spectacle of machine politics of graft and corruption shine through.").

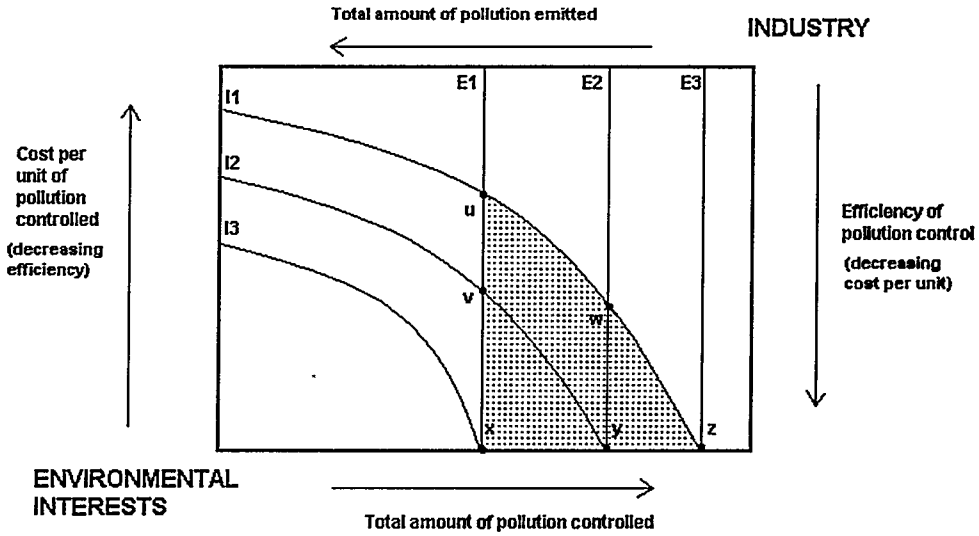
113. *See* Coglianese, *supra* note 65, at 1321 (arguing that this dynamic encourages omitted interests "to disrupt the consensus").

114. *See* Farber, *supra* note 103, at 306-10

115. Of course, most pollution control laws do not specify directly how costly pollution control must be, but they sometimes do so indirectly by specifying how emissions goals must be met. Indeed, many of the EPA's regulatery reform initiatives are aimed at overcoming or changing mandates that require inefficient means to reach agreed-upon ends. See *supra* Section II for a discussion of this.

ciency, proponents of reform might believe that environmental interests should not view greater efficiency for industry with disfavor.[116] We might infer from the various efficiency critiques that proponents of reform believe that environmental interests care, or ought to care, only about the amount of pollution controlled and not about the cost-per-unit-controlled borne by industry. Thus, in Figure 2 we depict industry's indifference curves to reflect that view of the conflict.[117]

FIGURE 2: Edgeworth Box Analysis of Regulatory Reform Bargaining--Industry View



Given an initial policy at point *u*, industry and environmental interests alike ought to prefer any point in the shaded area to *u*. Indeed, we would expect that bargaining between industry and environmental interests would leave them somewhere on the line that runs between *x* and *z*, which represents the set of maximally efficient (and Pareto optimal) policies. The EPA's incentives-based regulatory

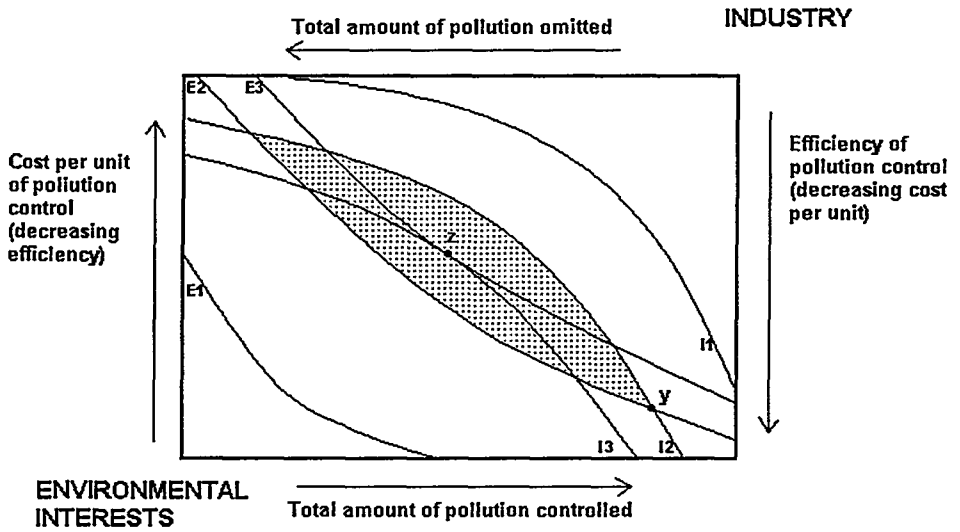
116. In fact, environmental groups have not spoken with one voice on this issue in the past. Unlike most other environmental interest groups, the Environmental Defense Fund, for example, has long advocated efficiency improvements in regulation, including the use of incentives-based regulation. *See, e.g., SO2 Trading Program Offers Answers for Other Pollution Problems, Group Says*, 28 Envtl. Rep. (BNA) 1408 (Nov. 21, 1997).

117. That is, environmental interests' indifference curves are vertical, reflecting the assumption that environmental interests would be unwilling to trade any amount of pollution control for "gains" on the y-dimension. In Figure 2, industry cares about both "goods," while environmental interests' utility is a function only of gains on the x-dimension (amount of pollution controlled).

programs and many of its reform initiatives are designed to produce just that kind of movement into Pareto superior outcomes.[118] Yet, policy proposals that seem to fit this description have not found their way into existing laws, and have been rejected by the EPA and stakeholders under the Agency's regulatory reform initiatives.[119] Given the bargaining environment depicted in Figure 2, it is easy to see why proponents of reform find this result inexplicable.

Critics of reform respond that opposition to efficiency improvements is not surprising at all because Figure 2 does not accurately represent bargaining over environmental policy generally. Defenders of traditional regulation appear to posit a bargaining environment more like that depicted in Figure 3, in which bargaining in both dimensions (over how much to reduce pollution, and over how to reduce pollution) is zero-sum bargaining. In other words, in Figure 3, environmental interests sincerely prefer inefficient regulation to efficient regulation, perhaps because they see the inefficiency of regulation as inextricably intertwined with other valued attributes of the regulation.[120]

FIGURE 3: Edgeworth Box Analysis of Regulatory Reform Bargaining--Environmental Interests' View



118. Of course, Project XL offers a structured process that attempts to identify Pareto superior policies compared with the status quo. Likewise, we can think of negotiated rulemaking as an attempt to find policies that are Pareto superior to those that would have been adopted under traditional notice and comment rulemaking.

119. See the discussion *supra* Section II.B.1.

120. *See supra* notes 90-91 and accompanying toxt.

In that case, we ought not expect necessarily that such bargaining will result in cost-efficient regulation.[121] For example, if environmental interests believe that incentives-based regulation is inherently more difficult to monitor and enforce than technology-based regulation, then they may resist movement to the more efficient means not because they object to efficiency, but rather because efficiency cannot be separated from other dimensions of the problem. Likewise, national environmental groups may view ostensible efficiency improvements in zero-sum terms because (i) they cannot adequately monitor the bargaining processes, (ii) they fear that the proposal may be a Trojan horse carrying unseen environmental harm, and (iii) they cannot trust local environmental groups to represent their interests.

We find many of these arguments against the use of collaborative processes to identify positive-sum policy changes to be unpersuasive and/or incomplete. First, none of these arguments explain problems with negotiated rulemaking, which is merely one way of developing a broad-based rule, or of establishing the status quo policy. While the process may be less accessible or more difficult to monitor than traditional notice and comment rulemaking,[122] the product is not. While the process is resource-intensive, groups may or may not choose to participate in the early stages of negotiated rulemaking, and forfeit no rights to comment or to litigate by opting out of the negotiation process.

Second, the monitoring argument seems predicated on the assumption that national environmental groups are the only competent or trustworthy guardians of the public interest. The EPA has designed and implemented most of its consensus-based regulatory reforms so as to ensure that other environmental interests, such as state regulators and local citizens' groups, are well represented in the process. Indeed, given the strength of environmental interests within the Agency itself, it seems unlikely that environmentally harmful changes to the status quo will slip into effect unnoticed. Thus, the argument that regulatory

121. The Edgeworth Box analysis still predicts that the outcome will be Pareto optimal. However, if environmental interests value less efficient regulation, then their indifference curves will not be perpendicular to the *x-axis* (as in Figure 2), and we ought not to expect a corner solution.

122. Cary Coglianese has shown that participation in negotiated rulemaking is resource-intensive, which means that environmental groups face a relative disadvantage in the process compared to better-heeled industry groups. *See* Coglianese, *supra* note 65, at 1329. However, since negotiated rules must navigate the notice and comment process anyway, they offer the same opportunities for input as other rules, and are no less transparent.

reforms allow business to disguise environmentally harmful changes as Pareto improvements looks like a red herring.

Third, the argument that technology-based standards are easier to enforce has been eclipsed by advancements in monitoring technologies[123] and increasingly cooperative and open business approaches to environmental compliance.[124] As self-reporting of violations becomes more routine[125] and monitoring becomes easier, there is less of a trade-off between regulatory flexibility and regulatory transparency. For that reason, regulation that prescribes inefficient control technologies makes even less sense now than ever before.

However, there is another possible explanation for why bargaining may not produce Pareto improvements, one that comes from the experimental literature on bargaining. Experimental economists have found that simulations of Edgeworth Box bargaining often do not produce Pareto optimal outcomes.[126] To the contrary, players in two-person bargaining games often forgo clear Pareto improvements;[127] the common supposition is that such refusals are traceable to one or both

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123. For example, in the case of air emissions, there are now continuous emission monitors ("CEMs") that use lasers to measure the opacity of plumes coming out of a plant stack. The readings produced by these monitors are more frequent and, in many cases, more reliable than the estimates prepared by even the best-trained professionals using human measurement methods. In addition to CEMs, there are often physical process parameters related to plant emissions—such as the temperature, pressure, and speed of gas flows—that can be used to reliably estimate plant emissions of certain pollutants. *See* George Van Cleve & Keith W. Holman, *Promise and Reality in the Enforcement of the Amended Clean Air Act Part I: EPA's "Any Credible Evidence" and "Compliance Assurance Monitoring" Rules*, 27 ENVTL. L. REP. 10097 (1997).

124. The last decade has brought a sea change in industry relationships with outside groups who are interested in environmental compliance issues. Spurred in part by right-to-know laws, their own changing attitudes toward pollution regulation, and EPA policies promoting openness, more and more companies are institutionalizing information sharing relationships with citizens' groups. For a sampling of the extensive multi-disciplinary literature discussing this trend, see generally THE GREENING OF AMERICAN BUSINESS: MAKING BOTTOM-LINE SENSE OF ENVIRONMENTAL RESPONSIBILITY (Thomas F.P. Sullivan, ed., 1992); BEYOND COMPLIANCE: A NEW INDUSTRY VIEW OF THE ENVIRONMENT, WORLD RESOURCES INSTITUTE (Bruce Smart ed., 1992); Mark A. Cohen et al., Environmental and Financial Performance: Are They Related?, (unpublished paper, Vanderbilt University (1995)) (on file with authors); Douglas J. Lober, *Evaluating the Environmental Performance of Corporations*, 8 J. MANAGERIAL ISSUES 184 (1996); Eric W. Orts, *Reflexive Environmental Law*, 89 NW. U. L. REV. 1227 (1995); Geltman & Skroback, *supra* note 64.

125. For a discussion of self-reporting of enviroumental violations, see Spence, *supra* note 97, at 167.

126. For a summary of this literature, see KREPS, *supra* note 41, at 551-73.

127. A typical experiment requires players to agree on how to divide a dollar provided by the experimenter. It is not atypical for players to refuse to accept divisions proposed by the other player (and therefore to receive nothing rather than something). *See generally* Alvin E. Roth & Francoise Schoumaker, *Expectations and Reputations in Bargaining: An Experimental Study*, 73 AM. ECON. REV. 362 (1983).

players' belief that the proposed division of the gains was "unfair."[128] Players recognize that each has the power to deny the other desired gains; that is, each can veto potential changes from the status quo.[129] Thus, each player tries to use that veto power to extract as many gains as possible from the opponent, resulting in competition to see which player can improve her relative position the most. If one player believes that the other's offer is not reasonable or fair, that player may refuse the offer even if it represents a Pareto improvement.[130]

In the context of regulatory reform, environmental interests may veto proposed positive-sum changes in the status quo (such as reductions in the cost of compliance coupled with modest pollution reductions) based on the belief that industry has not done enough to control pollution, or that polluting behavior is morally wrong. That is, environmentalists may view the status quo as both inadequate and, in a sense, illegitimate. They may view the status quo as a stepping stone to a more stringent future policy. This view is evident in the rich history of citizen suit litigation brought by environmental groups to force the EPA to tighten environmental standards.[131] It is also why environmental laws are sometimes called "aspirational."[132] Not only do they set extraordinarily ambitious goals,[133] but the major pollution control statutes also are designed to move policy toward those goals by producing ever more stringent pollution control limits in self-executing ways.[134] Similarly, the long history of struggle to establish

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128. For a more recent discussion of this issue, see KREPS, *supra* note 41, at 556 ("[B]argaining outcomes depend upon individuals' expectations as to what the outcomes should be."); Ido Erev & Alvin E. Roth, *Predicting How People Play Games: Reinforcement Learning in Experimental Games with Unique Mixed Strategy Equilibria*, 88 AM. ECON. REV. 848, 848-50 (1998).

129. In the literature on bargaining games, this is called the "bilateral monopoly" problem.

130. This is precisely what Ochs and Roth found in a series of experiments in which players sometimes chose to receive nothing rather than to acquiesce to a division of gains that seemed unfair. *See* J. Ochs & Alvin E. Roth, *An Experimental Study of Sequential Bargaining*, 79 AM. ECON. REV. 355, 365-66, 373 (1989).

131. For a good history of the use of citizen suits in this way, see ROSEMARY O'LEARY, ENVIRONMENTAL CHANGE (1993).

132. *See* WILLIAM H. RODGERS, ENVIRONMENTAL LAW 141-42 (2d ed., 1994).

133. For a basic discussion of the ambitious and unattained goals of the 1970 Clean Air Act and the 1972 Clean Water Act, see Robert V. PERCIVAL ET AL., ENVIRONMENTAL REGULATION: LAW, SCIENCE, AND POLICY 763-65, 866-68 (2d ed., 1996).

134. The Clean Air Act and the Clean Water Act establish standards for limiting air and water emissions, respectively, that are defined in relative terms: that is, relative to the mean. For example, certain new sources of air pollution must employ "best available control technology" te control their emissions. *See* 42 U.S.C. § 7479(3) (1995); *see also id.* § 7501(3) (other technology-based standards under the Clean Air Act, including the Lowest Achievable Emission Rate ("LAER") standard). Similarly-defined technology-based standards apply to emitters of water pollutauts. *See* 33 U.S.C. § 1311 (1994). In this way, technological innovation affects de facto changes in the regulatory standards without formal changes in the law.

the status quo policy may contribute to the sense that the policy lacks democratic legitimacy.[135] Environmental groups' may suspect that industry can manipulate the policy process in unseen ways, and that they may be forced in the end to accept grudgingly a policy they deem inadequate.

For all these reasons, we might expect environmental interests to demand a high price for the efficiency improvements industry seeks, thus granting industry regulatory flexibility only in exchange for significant environmental improvements. If environmental interests inside or outside the EPA deem insufficient the ostensible environmental improvements industry offers, or those interests view the pollution reductions that industry offers as something for which they ought not to have to pay (in the form of compliance cost reductions),[136] they will refuse the deal. This appears to be what happened in connection with 3M's XL proposal.[137] Certainly the long history of distrust between industry and environmental interests feeds this dynamic in ways that interfere with positive-sum change.[138]

2. The Implications of Strategic Bargaining for Reform

Returning to Figures 2 and 3, we might infer that Figure 2 reflects environmental interests' sincere preferences while Figure 3 represents their strategic posture.[139] It is impossible to know with certainty whether environmental interests' opposition to reform is sincere, strategic, or some combination of the two. However, conceiving of the bargaining process in this way reveals some interesting implications for the bargaining process, and may help explain the trajectory of regulatory reform initiatives to date.

First, the bargaining model implies that environmental interests may view site-specific bargaining with individual firms (as in the

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135. For a more thorough explanation of this idea, see generally Spence, *supra* note 97.

136. Indeed, there is a rich literature supporting the view that pollution is wrong and ought not to be commoditized. *See id.* at 158-63.

137. *See infra* notes 159-164 and accompanying text.

138. *See supra* notes 28-34 and accompanying text.

139. This is akin to the notion of "nonseparable" or "conditional" preferences, which social scientists have studied in other contexts. *See, e.g.*, Dean Lacy & Emerson M.S. Niou, Nonseparable Preferences, Issue Linkage, and Economic Sanctions, (unpublished paper presented at the Annual Meeting of the American Political Science Association, Boston, Mass., (Sept. 3-6, 1998)) (on file with authors). Here, we might hypothesize that environmental interests' de facto preferences are strategic and guide their behavior, even if their sincere preferences would not lead them to oppose efficiency improvements. That is, they would not object to efficiency improvements but for the fact that objecting permits them to extract highly-valued gains from industry. In that way their preferences over outcomes on the efficiency dimension are conditioned by their preferences over outcomes on the pollution reduction dimension.

Project XL context) differently than bargaining over broad policy choices (as in the negotiated rulemaking context). In the former situation, we might expect participants in the process to be able to get a sense of the amount of pollution reduction gains that they can extract from individual firms in exchange for efficiency improvements. As a consequence, we might expect these smaller bargaining groups to reach consensus more readily than larger groups. On the other hand, if environmental interests use bargaining to try to extract the maximum possible pollution reduction gains from firms in return for efficiency improvements, that process will be extremely difficult in any negotiation that involves multiple firms, such as a negotiated rulemaking. Indeed, the task of agreeing on a policy change (in other words, writing a rule) that extracts the maximum possible gains from each firm confronts the already-familiar procedural inefficiency problems inherent in the rule writing process.[140]

Second, this view of bargaining suggests another, competing explanation for the problem of in-group/out-group disagreement over the outcome of bargaining. Recall that nonparticipants in bargaining processes tend to be less satisfied with the outcomes of those negotiations than participants.[141] While nonparticipants may be suspicious of hidden environmental dangers in the outcome of the process, nonparticipants may also suspect that the participants set the price of efficiency improvements too low by failing to extract the maximum amount of pollution reduction gains from industry. If that concern motivates nonparticipants, we would expect them to be more likely to oppose proposals produced by bargaining, even if those proposals represent Pareto improvements. In this way, the bargaining process offers only participants an opportunity to get a true sense of the gains from trade to be had. Nonparticipants have no such opportunity.[142]

Third, if environmental interests can trade efficiency improvements for environmental improvements beyond those required by law, environmental interests may prefer inefficient regulations precisely because those regulations hamstring industry. This is true in cases of bargaining over efficiency improvements for individual firms or entire industries. The costlier the status quo is to industry, the greater will

140. Indeed, this may be possible only when the price extracted from industry, in terms of pollution reduction, is very high. This is one possible explanation of the bargaining process that produced the acid rain trading program under 1990 Clean Air Act amendments.

141. *See supra* notes 110-11 and accompanying text.

142. Jacobs reports that trust-building was a key byproduct of the information sharing processes that took place during the early phases of the Environmental Leadership Program. *See* Jacobs, *supra* note 83, at 33-34.

be industry's willingness to pay (in environmental improvements) to eliminate those inefficiencies. This offers another reason why, in the context of bargaining-based regulatory reform, environmental interests' preferences over how to reduce pollution (the *x-axis*) are conditional on their preferences over how much to reduce pollution (the *y-axis*). Recall that in Figure 2 the most cost-efficient pollution control policies lie on the *x-axis*. If the status quo policy lies a great distance from the *x-axis* (say at point *u* rather than point *v* in Figure 2), environmental interests should be able to extract larger pollution reduction gains from industry in return for a new policy somewhere on the *x-axis*.[143]

Fourth, this analysis suggests two additional reasons why players on the national environmental policymaking stage, like national environmental groups and EPA headquarters (call them "national environmentalists"[144]), might be more likely to oppose collaborative reforms than local environmentalists and EPA regional personnel, even if those reforms produce significant environmental benefits. First, unlike their local counterparts, national environmentalists are repeat players in this bargaining game. By driving a hard bargain at individual sites, they may establish a reputation for firmness in the iterated game, thereby maximizing their long-run payoffs. Second, national environmentalists are engaged in another, larger bargaining process over changes to the status quo, but on a policy-wide basis. Their lobbying efforts involve a continuous process of trying to move broad policy—that is, the rule itself, not just its application in a single instance or set of instances—toward a more preferred position. For example, if the status quo policy is somewhere on indifference curve E1 in Figure 2, national environmentalists are continually seeking ways to move it to a point on E2 or E3. We can view the long process that preceded the 1990 acid rain marketable permits program in this way. Environmental interests consented to allow the acid rain allowance trading program, an incentives-based approach to sulfur dioxide pollution, to become law only in exchange for an additional 10 million tons in annual reductions in sulfur dioxide emissions beyond those required under the existing regulatory regime.[145]

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143. If the status quo is at point *v*, the best that environmental interests can expect to do is to move to indifference curve E2. If the status quo is at point *u*, there is the potential to move to indifference curve E3.

144. This term may be a bit of a misnomer in that it refers to environmental interests whose concern is moving national policy. These people may be located anywhere in the EPA, or throughout the environmental policy community.

145. *See* 42 U.S.C. § 7651(b) (1995) (outlining the purpose of the 1990 acid rain program, namely "to reduce the adverse effects of acid deposition through reductions in annual emissions

Thus, the incentives facing national environmentalists are different. They are playing a dynamic, or longer-term, game not well represented by the static Edgeworth Box. Because they seek positive-sum changes at the broad policy level, national environmentalists also benefit if the status quo policy lies a greater rather than lesser distance from the *x-axis*—that is, if it is more inefficient rather than less. The more inefficient the policy, the more industry will be willing to pay (either by reducing their own pollution or acceding to changes in policy that mandate those same reductions) to change the policy in order to realize efficiency gains.[146] Furthermore, to the extent that individual firms or sets of firms can realize efficiency improvements through reform initiatives, national environmentalists lose their leverage over those firms, thereby decreasing the likelihood of arranging a future positive-sum change at the broad policy level.[147] Thus, national environmentalists have reasons to resist collaborative reforms apart from any concerns over industry motives or the ability of local environmental groups to participate effectively in the process.

IV. THE TRAJECTORY OF PROJECT XL

A closer look at the short history of the Project XL program illustrates how these strategic considerations have undermined the pursuit of Pareto improvements. Since its inception, the program has been plagued by arguments over the appropriate price (in terms of environmental improvements) that the EPA should charge for granting efficiency improvements to industry. These conflicts have been evident in the evolution of the substantive criteria that govern the selection and approval of XL project proposals, and the application of those criteria in practice. Formal project criteria have evolved over time to place increasing emphasis on the importance of environmental benefits and stakeholder consensus, reducing the relative importance of other Pareto improvements in the process. This new bargaining

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of sulfur dioxide of ten million tons from 1980 emission levels," a more than 50 percent reduction).

146. We might also speculate that national groups will place a lower value on local, site-specific environmental improvements than local groups do.

147. The corollary to this is that when bargaining produces exchanges of efficiency improvements for environmental improvements, it removes from the table the object of national environmentalists' future attention. That is, programs like Project XL lead to emissions reductions or other environmental improvements that national environmentalists may have hoped to address legislatively in the future. Thanks to Don Eliot for helping us to clarify this point.

environment has, in turn, provided additional leverage for national environmentalists to veto or delay the pursuit of positive-sum bargains.

A. The Evolution of Project Criteria and the Price of Efficiency

Recall that in the Project XL framework, bargaining occurs on a proposal-by-proposal basis.[148] The EPA designed the Project XL program to provide an institutional framework that would help stakeholders realize positive-sum improvements through individual bargaining processes.[149] Consistent with this view of the program, the original criteria by which the EPA evaluated proposals[150] can be grouped into three categories: (1) those that represent improvements for project sponsors, mostly industry; (2) those that represent improvements for environmental and interest groups other than project sponsors; and (3) procedural rules that govern the bargaining process. As originally designed, the program envisioned a process under which applicants would offer category 2 improvements to other stakeholders in exchange for category 1 improvements, all in the context of a process governed by category 3 rules.[151]

Category 1 improvements include the "cost savings," "technical and administrative feasibility," and "new and innovative approaches" criteria.[152] That project sponsors benefit from reduced compliance costs is obvious, as is the requirement that projects meet certain feasibility thresholds. The "new and innovative approaches" criterion goes hand-

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148. *See supra* Section B.1.

149. This much is widely accepted. *See* Caldart & Ashford, *supra* note 40, at 10-11 (noting that collaborative processes can facilitate better understanding of issues and provide opportunities for creative problem-solving); Freeman, *supra* note 36, at 7 (arguing that "multistakeholder collaboration" facilitates innovation that increases the "quality" of regulation); Mank, *supra* note 40, at 4 ("Project XL has the potential to reduce both regulatory costs *and* pollution by allowing companies to try innovative pollution control strategies that are customized for individual facilities rather than relying on the current one size fits all approach . . . ."). More importantly, the EPA's initial solicitation of XL proposals reflects this view. *See* Regulatory Reinvention (XL) Pilot Projects [hereinafter "Initial Solicitation"], 60 Fed. Reg. 27,282 (May 23, 1995) ("National environmental requirements may not always be the best solution to environmental problems. Substantial cost savings can sometimes be realized, and environmental quality enhanced, through more flexible approaches involving pollution prevention.").

150. *See* Initial Solicitation, 60 Fed. Reg. at 27,282.

151. The EPA's initial solicitation of XL proposals envisioned a process under which projects that survived the initial EPA screening would move forward into the bargaining process. That process would involve interested stakeholders and would produce, if successful, a "Final Project Agreement," or "FPA," specifying the terms of the bargain. *See id.* at 27,284-85.

152. *See id.* at 27,287. We should note that some industries may have had less tangible and self-interested reasons for participating in the Project XL program, such as the desire to promote innovation and change for its own sake. *See* Marcus et al., *supra* note 56.

in-hand with the "cost savings" criterion in that, in XL parlance, the most commonly touted innovation is some version of increased flexibility, such as cross-media permitting, or multi-pollutant permit limits.[153] Category 2 improvements include the "superior environmental performance" and "ensuring compliance with environmental justice policies" criteria.[154] The former criterion ensures that environmental interests will realize gains along with project sponsors. The latter criterion ensures that the process will not hurt interests who are typically not represented at the XL bargaining table. Category 3 rules include the "support of stakeholders" and "information availability" criteria.[155] These criteria are designed to ensure that the product of the bargaining process is a verifiable Pareto improvement over the status quo. The former criterion protects the interests of participants in the bargaining process by ensuring that all must agree on proposed changes in the status quo. The latter protects the interests of non-participants by facilitating their monitoring and evaluation of the process and its outcome.

As we have noted, it was not clear at the outset of the program how the EPA would balance these criteria in reaching decisions on proposed projects, or exactly how it would define each of the criteria in application.[156] The ill-fated 3M proposal highlighted the difficulty of these tasks for the EPA. The 3M proposal was premised on the notion that significant reductions in permitted emissions of pollutants would constitute superior environmental performance. 3M proposed to cap plant-wide emissions of VOC's[157] and hazardous air pollutants at levels significantly lower than those currently required under the Clean Air Act.[158] The benefit to 3M was that the implementation of the permit as proposed would cut its personnel and monitoring costs. The proposal was supported by a stakeholders' advisory council consisting of state and local officials, local environmental advocacy groups, university

153. The EPA's description of this criterion is as follows: "EPA is looking for projects that test innovative strategies for achieving environmental results. These strategies may include processes, technologies, or management practices." *See* Initial Solicitation, 60 Fed. Reg. at 27,287. In practice, most of the innovations have involved ways to regulate pollution, though some innovations have involved technical processes. An example of the latter is the recently approved Andersen Corporation proposal. *See EPA Web Site* (visited Jan. 7, 2000) <http:// yosemite.epa.gov/xl/xl_home.nsf/all/anderson.html>.

154. *See* Initial Solicitation, 60 Fed. Reg. at 27,287.

155. *See id.*

156. *See supra* Section II.B.1.

157. *See supra* note 59.

158. *See* Buelow, *supra* note 56, at 15-17.

representatives, and other members of the public.[159] However, the EPA withheld approval of the plan as approved by the stakeholders, apparently based on its belief that, while permitted emissions would decrease under the 3M proposal, actual emissions might not. For participating stakeholders, including local regulators and environmental interests,[160] the permit reductions satisfied the "superior environmental performance" criterion; for environmental interests outside the bargaining process, including national environmental groups[161] and some at EPA headquarters,[162] only actual reductions would suffice. Eventually, 3M and the Minnesota Pollution Control Agency withdrew their proposal[163] in a letter accusing the EPA of "clinging to its command and control habits."[164]

A second promising early proposal met a similar fate. Anheuser-Busch, another company with an environmentally progressive reputation, developed a Project XL proposal that would have made the company's Jacksonville, Florida brewery operations a model for multimedia permitting.[165] However, after negotiations bogged down over a

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159. Stakeholder support for the 3M-Hutchinson proposal is memorialized in the June 12, 1995, letter from the stakeholder committee to Charles Williams, Commissioner, Minnesota Pollution Control Agency. *See* <http://yosemite.epa.gov/xl/xl_home.nsf/all/3MStakeholders-to-Williams-6-12-96.html>.

160. The disagreement over whether the imposition of more stringent legal limits on 3M satisfied the "superior environmental performance" criterion is evident in the July 24, 1996, letter from 3M to the EPA: "With our experiment at Hutchinson, we hope to help government develop common sense ways of achieving superior environmental performance which is simply performance (measured in a number of different ways) which is better than required under existing regulation." *See What Is "Superior Environmental Performance"? 3M's Perspective* (July 24, 1996) <http://yosemite.epa.gov/xl/xl_home.nsf/all/3m-sep-position.html>.

161. The Natural Resources Defense Council, a national environmental group that did not participate in the bargaining process, objected to the 3M proposal:

> Contrary to both the spirit and explicit criteria of Project XL, the 3M proposed agreement . . . offers "reductions" only on paper. The stated intention of the project is to provide broad pre-approval of facility expausions and modifications in exchange for less permissive emissions limits in the facility's permits. However, the proposed limits remain so permissive as to allow the facility to increase its emissions to very high levels.

See NRDC's Comments on 3M Proposal (July 3, 1996) <http://yosemite.epa.gov/xl/xl_home.nsf/all/nrdc-comments-7-3-96.html>.

162. *See* Buelow, *supra* note 56, at 22-24.

163. *See General Policy: 3M Decides to Drop Out of Project XL Process After Disagreement Over Performance Guarantees*, 27 Envtl. Rep. (BNA) 1045, 1046 (Sept. 13, 1996).

164. 3M's letter also said that "EPA's proposal fails to entrust 3M, a company with a proven record of exemplary environmental performance, te take on the responsibility and accountability for proving that Project XL flexibility will result in superior environmental performance," and that 3M "never envisioned requiring prescriptive permit conditions that render the experimental nature of XL moot." *See Inflexibility?: EPA Clings to Command and Control; 3M Shelves Project XL Proposal, Environmental Remediation Technology* (Information Access Company Newsletter Database) at No.19, Vol.4 (Sept. 18, 1996).

165. *See Anheuser-Busch Proposal* (visited Jan. 13, 2000) <http://yosemite.epa.gov/xl/xl_home.nsf/all/a-b.html>.

similar dispute over the meaning of the superior environmental performance criterion, Anheuser-Busch withdrew its proposal.[166]

As it became evident that project sponsors (and some, particularly local, stakeholders) were applying the Project XL evaluation criteria differently than the EPA, the Agency moved to bolster the bargaining position of environmental interests in the process. The 1997 revision of the Project XL evaluation criteria places added emphasis on the "environmental results" and "stakeholder support" criteria.[167] The Agency clarified the meaning of superior environmental performance by specifying a two-tiered test[168] that project proposals must meet. Tier 1 addresses the 3M proposal dispute by requiring that superior environmental performance be judged against the "benchmark" of current facility performance or future allowable performance, whichever is more stringent.[169] Tier 2 specifies that the EPA will look at the proposed quantitative increments of improvement over the Tier 1 benchmark in determining whether performance will be superior enough.[170]

Whether intentionally or not, the 1997 changes to the XL program appear to strengthen the hand of national environmentalists in the XL bargaining process. The new rules give additional leverage to environmental groups seeking to increase the cost of securing efficiency improvements by ensuring that the price would be higher than that offered by 3M (that is, more than mere permit limit reductions),

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166. A representative of Anheuser-Busch, Chris Spire, presented his views of the problems associated with Project XL at an environmental management conference. He listed several problems associated with the XL process: the higher priority given to the EPA's goal of superior environmental benefit relative to the parallel goal of efficiency and flexibility for the good of the business; refusal by the EPA to credit prior "beyond compliance" efforts; the EPA's ever-cognizant need to sell the initiative to environmental activists; and the lack of trust and credibility between the EPA, environmentalists, and industry. *See* Kevin A. Fletcher, *EPA's Project XL Voluntary Initiative: The Struggle for Enhanced Environmental Protection at a Lower Cost*, 3 ALB. L. ENVTL. OUTLOOK 51, 56-57 (1997).

167. *Regulatory Reinvention (XL) Pilot Projects* [hereinafter XL Modifications] 62 Fed. Reg. 19,872 (Apr. 23, 1997).

168. The EPA described the test as follows:

> EPA is establishing a two tiered assessment of superior environmental performance for Project XL Proposals. Tier 1 is a quantitative benchmark of the project against the environmental performance that would have occurred absent the program. It establishes a baseline of equivalence from which superior environmental performance can be measured. A project that is not at least equivalent, based on the factors discussed in Tier 1, can not be considered superior overall. Tier 2 is an examination of factors, both quantitative and qualitative, that lead EPA to judge that a project will produce a superior level of environmental performance that merits testing the innovation being proposed.

Id. at 19,874.

169. The EPA defined this Tier 1 benchmark as "either the current actual environmental loadings or the future allowable environmental loadings, whichever is more protoctive." *Id.*

170. *See id.* at 19,875.

and by ensuring that in each case the price would be high enough to satisfy all the participating stakeholders. Likewise, the Agency gives additional leverage to nonparticipating national environmental groups by stating explicitly that such groups fall within the Project XL definition of "stakeholders."[171] By implication, then, the 1997 changes to the program decrease the leverage of local and regional stakeholders in the bargaining process.

B. Balancing the Criteria in Practice

Have national environmentalists used this leverage to their advantage? Since these changes in the project criteria took effect, the Agency has approved some other high-profile projects, most notably proposals by Intel, Merck, and Weyerhauser, that satisfied the Agency's definition of superior environmental performance while offering project sponsors enough efficiency improvements to make the projects worthwhile.[172] As of this writing, 15 XL projects have moved from proposals to the implementation stage, while more than thirty have been rejected or withdrawn.[173]

1. The Bargained-for Exchanges

As we have noted, many of the Project XL battles are fought over the price to be charged (in environmental improvements) for efficiency improvements. That is, agency and private sector stakeholders negotiate with the project sponsor in an attempt to reach agreement on a set of positive-sum changes to the status quo. If the EPA is satisfied with the outcome of the bargaining process, the project moves from a proposal to the implementation stage. What kinds of proposed environmental improvements have been deemed sufficient in practice? Do successful project proposals offer greater, or more tangi-

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171. Specifically, the 1997 notice stated that, while stakeholders were originally defined as including "communities near the project, local or state governments, businesses, environmental and other public interest groups, or other similar entities . . . [that] definition includes both those stakeholders in the proximity of the project and those stakeholders interested in the broader implementation of the concepts being tested in the project, such as state, regional or national environmental groups." *Id.* at 19,877.

172. *See* Project XL, *Weyerhauser proposes multi-media approach to environmental protection* (visited Dec. 29, 1999) <http://yosemite.epa.gov/xl/xl_home.nsf/all/weyer.html>; Project XL, *Intel Drafts Environmental Operations Plan and Obtains Flexible Air Permit* (visited Dec. 29, 1999); <http://yosemite.epa.gov/xl/xl_home.nsf/all/intel.html>; *Project XL*, (visited Dec. 29, 1999) <http://yosemite.epa.gov/xl/xl_home.nsf/all/merck.html>.

173. *See XL Projects* (visited Dec. 29, 1999) <http://yosemite.epa.gov/xl/xl_home.nsf/all/xl_info>.

ble, environmental benefits generally? How have local and national stakeholders influenced the process?

As of this writing, of the 36 industry-sponsored proposals that the EPA has disposed of, 12 have moved beyond the application stage, while 24 have been rejected or withdrawn.[174] All of the proposed projects have included some form of efficiency improvements for the company, such as reduced compliance costs, reporting flexibility, flexibility in the means of compliance, or waivers of particular emission or other regulatory requirements. These latter two categories of company benefits included things like multi-pollutant or multi-source permit caps on air emissions,[175] de-listing[176] of listed hazardous wastes, and permission to make process changes without triggering new permitting requirements under the Clean Air Act.[177] In return, most companies proposed some combination of reduced permit limits (what 3M offered), reduced emissions of pollution, enhanced environmental management of the facility, and/or other environmental benefits. Table 1 shows the distribution of kinds of environmental benefits companies have proposed to date.

Based on the data in Table 1, the EPA's actions appear to be consistent with their (revised) rhetoric. Not surprisingly, proposals that have offered more tangible and guaranteed environmental bene-

174. Data were coded using information from the EPA Project XL Web Site and supplemental research. We elected to focus only on projects that involved bargaining between the regulator and the regulated. Consequently, we chose to exclude from our data set projects proposed by public entities in their capacity as regulators. Thus, for example, proposals by state environmental agencies to change the state regulatory regimes that they administer were excluded, while proposals by public sector owners of regulated facilities seeking compliance flexibility were included. Though it is a bit of a misnomer, we refer to our sample as "industry-sponsored" proposals for that reason. Our final sample included 12 successful projects and 24 unsuccessful ones, all proposals by regulated entities offering some sort of environmental improvement in return for efficiency improvements.

175. Under a multi-pollutant cap, pollutant-specific permit limits would be replaced by a multi-pollutant volume or other limitation. Under a multi-source cap, individually regulated emission points would be regulated as one emission point (or bubble), which is what the Intel project involves. *See* Project XL, *Intel Drafts Environmental Operations Plan and Obtains Flexible Air Permit* (visited Dec. 29, 1999) <http://yosemite.epa.gov/xl/xl_home.nsf/all/intel.html>. Either approach would allow increases in emissions of one pollutant without prior agency approval so long as the overall limitation or cap is not exceeded.

176. Under the Resource Conservation and Recovery Act ("RCRA"), the EPA lists certain specific wastes or waste streams (sometimes company or facility-specific wastes) as "hazardous wastes," triggering a variety of regulatory requirements. *See* 42 U.S.C. § 6921 (1994). "De-listing" refers to the process by which companies seek to have their wastes removed from the list by demonstrating that the wastes ought not to be considered hazardous under the statute.

177. Specifically, sponsors seek to avoid the need for an air permit modification that may be triggered by changes in production or other changes in the facility. *See, e.g., Project XL* (visited Dec. 29, 1999) http://yosemite.epa.gov/xl/xl_home.nsf/all/merck.html (explaining Merck's successful XL project).

fits, in the form of reduced pollution emissions,[178] have tended to succeed more often than projects that did not. Note, however, the presence of some projects that promised reduced pollution but nevertheless were not selected. These included projects promising reduced hazardous waste generation in return for relief from hazardous waste regulatory requirements, relief that the EPA was apparently not prepared to give.[179] Of the projects that did not promise quantifiable and guaranteed reductions in pollution or waste generation, only 10 percent (2 projects) were successful. Predictably, the mere promise of the reduced risk, through tightened permit limits or enhanced environmental management at the project site, was not as highly correlated with success in the XL program. In particular, while 14 proposals promised enhanced environmental management at sponsor facilities, only four of those were successful. While the combination of efficiency improvements for project sponsors and reduced risk represents a clear Pareto improvement over the status quo at the site, the EPA deemed the latter an insufficient price to pay for the former. Rather, satisfaction of the "superior environmental performance" criterion through guaranteed pollution reduction seems to be a surer path to success in Project XL.

178. These data include a few projects, including some successful projects, for which a so-called "multimedia cap" on emissions was proposed. In such cases, the overall effect of the proposed change is to reduce emissions, though the emissions of any single pollutant could increase over time. We coded such cases as promising emissions reductions.

179. In 1996, the EPA rejected proposals from DuPont and Eastman Chemical for de-listing of specific RCRA listed hazardous wastes or waste streams, saying that the de-listing should be pursued outside of the XL process. *See* Project XL, *DuPont Proposes Flexibility for Hazardous Waste Listing at Its Victoria, Texas Facility* (visited Dec. 29, 1999) <http://yosemite.epa.gov/xl/xl_home.nsf/all/dupont.html>; *Project XL*, (visited Dec. 29, 1999) <http://yosemite.epa.gov/xl/xl_home.nsf/all/eastman.html>. Subsequently, however, the Agency approved another de-listing proposal by HADCO. Interestingly, the EPA approved the HADCO de-listing proposal after the 1997 revisions to the XL program. *See* Project XL, *HADCO Proposes To De-List Its Wastewater Sludges From RCRA* (visited Dec. 29, 1999), <http://yosemite.epa.gov/xl/xl_home.nsf/all/HADCD.html>.

TABLE 1: Types of Environmental Benefits Proposed in Project XL[a]

	Did Project Guarantee Reduce Actual Emissions?[b]		Did Project Propose Reductions in Permit Limits?		Did the Project Propose an Environmental Mgt. System?[c]	
	YES	NO	YES	NO	YES	NO
Successful Projects[d]	10	2	2	10	4	8
Unsuccessful Projects	4	20	4	18	14	9

a. Note that projects often propose more than one kind of environmental benefit, and that some propose other kinds of environmental benefits not listed here.
b. Projects proposing guaranteed net reductions in pollution were placed in the "yes" category. Projects not proposing guaranteed net reductions, like the 3M proposal and other projects promising "potential" reductions, were placed in the "no" category.
c. For one of the unsuccessful projects, we could not determine from the project dockets whether or not an environmental management system was proposed.
d. We coded all projects that survived to the implementation stage as "successful" projects; those that did not were coded as "unsuccessful."

For most of the unsuccessful projects, we were able to identify reasons for their failure from the information in the project dockets. Of the 24 unsuccessful projects, 18 were unsuccessful because of their failure to satisfy the "superior environmental performance" criterion, while four were rejected or withdrawn for other reasons, and two others failed for reasons we could not determine.[180] In other words, in 75 percent of the unsuccessful cases, the EPA was unwilling to grant the company its proposed efficiency improvements because the environmental benefits offered were insufficient.[181] This remains the most common reason for failure of XL project proposals, even after the EPA's 1997 revision of its decision criteria emphasizing the importance of quantifiable environmental improvements.[182] All of this im-

180. We could not determine from the EPA docket any specific reason for the failure of the Coeur Alaska and PCS Nitro projects.

181. Only four of the unsuccessful projects proposed guaranteed reduced emissions. Of those four, three projects were rejected for failure to satisfy the SEP criterion. However, the three comprised a package of proposals by Dow Chemical that the EPA rejected in May, 1996.

182. Not surprisingly, however, the success rate of proposals has gone up since the 1997 revisions to the program. Presumably, prospective sponsors are learning what sort of proposals are likely to succeed, particularly given the guidance contained in the 1997 revisions. Thus, we might infer that this censoring of prospective XL proposals from the data set by sponsors means that the data tend to understate the impacts of the 1997 revisions over time. That is, projects

plies that the EPA has been fairly successful in its attempts to increase the price of obtaining efficiency improvements using the XL bargaining process.

2. Stakeholder Support

Of course, the EPA's 1997 revision of its Project XL decision criteria indicates that the success or failure of a Project XL proposal is determined not only by the characteristics of the project involved, but also by the support (or lack thereof) by interested stakeholders. Has that been the case in practice? Do stakeholders have de facto veto rights? Can they veto proposed projects that offer substantial environmental improvements, like significant emissions reductions beyond those required by law? Or will the EPA overrule stakeholders in such instances? Conversely, will the EPA veto projects that enjoy unanimous local stakeholder support?

Unfortunately, the data on stakeholder support are sketchy, particularly with respect to unsuccessful projects. This is due partly to the fact that the EPA rejected a significant percentage of unsuccessful proposals prior to any opportunity for stakeholders to express opinions one way or the other.[183] Hence, Table 2 summarizes data on stakeholder support or opposition for only a subset of the total number of XL projects. Among projects on which stakeholders did express opinions, unanimous local stakeholder support does not always correlate with success. While it is the exception rather than the rule, the EPA on a few occasions has approved projects that were opposed by a minority of local stakeholders, contrary to the Agency's stated preference for consensus. Three such projects—the Weyerhauser, HADCO, and Merck projects—proposed guaranteed pollution reductions, and in each case the opposing stakeholders represented a clear minority view. Likewise, the EPA has rejected some projects that enjoyed unanimous local stakeholder support, the 3M project being a case in point. None of those projects proposed guaranteed pollution emissions reductions. Therefore, it appears that the EPA places more emphasis on its "superior environmental performance" criterion than on

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that would have been rejected for failure to propose sufficient environmental benefits are less likely to find their way into the proposal pool now than they were before the 1997 revisions.

183. These proposals included projects deemed inappropriate for the XL program for one reason or another. *See* Project XL, *U.S. Coast Guard Grant Proposal* (visited Dec. 29, 1999) <http://yosemite.epa.gov/xl/xl_home.nsf/all/uscg.html>; Project XL, *Uniroyal Chemical Co. Proposed Pollution Prevention Projects That Will Reduce the Generation Of Hazardous Wastes and Pollutants* (visited Dec. 29, 1999) <http://yosemite.epa.gov/xl/xl_home.nsf/all/uniroyal.html>.

stakeholder consensus. Unfortunately, in those cases where the EPA overruled a local stakeholder consensus, the data do not permit us to distinguish proposals rejected by EPA headquarters from proposals rejected by EPA regions. We have only anecdotal evidence to support the notion that support for XL proposals is stronger in the regional offices.[184]

Table 2: Stakeholder and National Environmental Group Support and Success in Project XL

	Unanimous local stakeholder support		Opposition from national environmental group	
	YES	NO	YES	NO
Successful projects (12 Cases)	5	3	3	3
Unsuccessful projects (24 Cases)	4	1	5	—

What about the EPA's professed intention (in its 1997 modification of program decision criteria) to give additional weight to the opinions of non-participant environmental interests? While the opposition of non-local environmental groups is not necessarily fatal to XL proposals,[185] it has correlated mildly with failure. Of the eight instances in which national environmental groups objected formally to XL proposals, five resulted in rejection or withdrawal of the project. Of those five, three involved situations in which local stakeholder support for the project was unanimous, yet the project failed. The Natural Resources Defense Council ("NRDC"), in particular, has expressed opposition to several XL projects, including the 3M proposal, and has

184. *See* Susskind & Secunda, *supra* note 29, at 95-97 (quoting one EPA staffer who commented that "those who participated in Project XL [within the Agency] were considered turncoats by certain important middle level managers").

185. For example, it appears from the Merck project docket that the NRDC strongly opposed the multi-pollutant cap and other aspects of the Merck proposal. Yet the project ultimately succeeded. *See* <http://yosemite.epa.gov/xl/xl_home.nsf/all/merck.html>.

intervened in some others in an attempt to persuade the EPA to demand a higher price for the efficiency improvements that the project sponsor sought.[186] On the other hand, the EPA approved some XL proposals over the objection of national environmental groups, though two of the three instances of this occurred prior to the EPA's 1997 revision of its Project XL criteria.[187]

What does come through clearly in the data is that national environmental organizations distrust the process in ways that local organizations do not. A review of the EPA's XL proposal dockets reveals only a single expression of qualified support for a proposal by a national environmental group,[188] and at least eight interventions in opposition to a proposal.[189] Yet the records reveal numerous expressions of support for XL proposals by local stakeholders, including local citizens groups.[190] This is consistent with our expectations, and with prior anecdotal evidence.[191] This could be a manifestation of the in-group/out-group problem, consistent with the idea that participation in the bargaining process builds trust in the outcome. However, it is also consistent with the expectation that local stakeholders place more value on the local environmental benefits that the company offers. National environmental leaders care about a different bargaining

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186. *See, e.g.*, Letter from David Lennett, Representing NRDC and the Environmental Defense Fund ("EDF") to EPA Representatives In Connection With the Ultimately Successful Molex Project Proposal, Dec. 3, 1997, at *Project XL*, (visited Dec. 1999) <http://yosemite.epa.gov/xl/xl_home.nsf/all/lennett-ltr-12-3-97.html> (urging the EPA to impose additional conditions on the project sponsor before approving the project).

187. NRDC objected to both the Intel and HADCO projects in 1997 and 1996 respectively, both of which were approved by the EPA before the 1997 revision of program criteria. *See* <http://yosemite.epa.gov/xl/xl_home.nsf/all/intel.html>; <http://yosemite.epa.gov/xl/xl_home.nsf/all/hadco.html>. The EPA also approved the Molex proposal in 1998, after receiving correspondence from NRDC and EDF expressing mild or qualified objections to the project. *See* <http://yosemite.epa.gov/xl/xl_home.nsf/all/molex.html>.

188. In a letter to the Regional EPA Deputy Director, a representative from the Environmental Defense Fund expressed concern that the XL plan for the Atlanta Atlantic Steel Project "would not provide for the implementation of all reasonably available control measures to assure the timely attainment of air quality in the region." *See* <http://yosemite.epa.gov/xl/xl_home.nsf/all/edfcomm.html>. The representative nevertheless expressed support for the XL process stating "[w]e would very much like to see the Atlantic Steel project XL process succeed as a national model for how Clean Air Act conformity and Brownfield problems can be turned into opportunities for urban revitalization, livable communities, improved access of low income communities to jobs, and economic growth with environmental progress." *See id.* For a description of the successfully implemented Atlanta Atlantic Steel Project, see <http://yosemito.epa.gov/xl/xl_home.nsf/all/atlantic.html>.

189. *See* <http://yosemite.epa.gov/xl/xl_home.nsf/all/xl_info>.

190. *See id.*

191. *See* Susskind & Secunda, *supra* note 29, at 107 (describing an environmental organization representative's concern over their inability to moniter the process "at least until the first federal register notice").

game—bargaining over national policy—and will grant efficiency improvements for industry only when paid in that other currency. We cannot say which phenomenon drives these results. Nor can we confirm whether this same sort of fault line exists between regulators from EPA regional offices and EPA headquarters, as was apparently the case in the context of the 3M project. We note simply that either or both may be at work here.

In sum, the trajectory of the Project XL program to date reflects some common pitfalls in the bargaining process, pitfalls that lead to outcomes that sometimes do not comport with bargaining theory. Politics, it is said, is a zero-sum game. The theoretical expectations of the bargaining game do not accommodate well the larger political context in which bargaining over environmental outcomes occurs. That is why Project XL bargaining, like bargaining in the experimental lab, has yielded only a subset (and probably a small subset) of the available Pareto improvements.

V. CONCLUSION

So where does this leave collaborative regulation? This Section addresses that question briefly. We note first, however, that our primary purpose in this Article has been diagnostic, to offer an alternative explanation for the failure of collaborative regulation to meet its proponents' expectations. The strategic bargaining dynamic outlined here offers some insight into industry's (and others') impatience with, and environmental interests' wariness toward, collaborative regulation. A variety of participants, including national environmental interests within the EPA, retain the power to veto project proposals, making agreement difficult to achieve. Believing that environmental interests have, or ought to have, preferences over policy outcomes like those shown in Figure 2, proponents of collaborative regulation wonder why environmental interests veto proposals that would combine efficiency improvements with improvements in environmental conditions, even when the latter are more modest than the former. The testimony of a state environmental agency director before a House subcommittee illustrates this view:

> EPA's Project XL has . . . potential for success, but EPA's approach has severely limited its effectiveness. EPA's April 1997 guidance defining "superior environmental performance" has become a barrier to approvals of projects . . . . If innovations have the poten-

> tial to demonstrate achievement of existing environmental requirements in a more efficient and effective manner, then by all means those projects should be pursued.[192]

Stated differently, proponents of Project XL approach the bargaining process by accepting the ends of the status quo policy (its prescription for how much pollution will be reduced) and challenging its means (its prescription for how to achieve that pollution reduction goal). For their part, environmental interests take a polar opposite view: they are more inclined to challenge the ends of the status quo policy and to accept the means. Moreover, environmental interests' view of the status quo is colored not merely by their preference for more pollution reduction than the status quo policy requires, but also by their belief that industrial interests were over-represented in the process by which that policy was created in the first place. Those predispositions, coupled with the opportunity to achieve highly valued pollution reduction gains, offer a powerful incentive for strategic behavior in negotiations with industry. This dynamic pervades American environmental regulation. The politics of the environmental policy process have created centrifugal forces that have made the search for common ground difficult. In this larger context, the inability of industry and environmental interests to realize positive-sum gains through bargaining seems less surprising.

In a sense, then, the picture we have painted here is a bleak one—bleak in that it points to reasons why we might expect to find deeply embedded resistance to regulatory change, even positive-sum change. The picture is bleak only in the relatively short term, however. Indeed, there are good reasons to believe that the long-term prospects for increased use of collaborative regulation are strong, reasons that become evident when we consider the arguments for and against it. Commentators seem to be split over the two-pronged question of whether collaborative regulation can or should succeed, between those who favor collaborative regulatory reform but fear that it is unworkable under the current legal regime and those who oppose collaborative regulatory reform. As we have noted, many in the latter

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192. *See* Testimony of Russell J. Harding, *supra* note 77. Karen A. Studders, Commissioner of the Minnesota Pollution Control Agency, echoed these same concerns in her comments on a draft of federal legislation aimed at facilitating programs like Project XL. *See* Letter from Karen A. Studders to Judy Borgers, Legislative Director for Rep. James Greenwood (June 11, 1998) at <http://www.pca.state.mn.us/programs/projectxl/mpca-com.pdf> ("A key part of why EPA reinvention initiatives have had disappointing results is EPA itself. Instead of allowing innovation experiments to happen, . . . EPA chose to focus on requiring guarantees of up-front success. This has resulted in resource intensive up-front review and micro-management of the proposed pilots."). For a discussion of the proposed legislation that is the subject of these comments, see *infra* notes 203-09 and accompanying text.

group disapprove of the use of stakeholder bargaining as a policy-making technique on principle, arguing that it is an abdication of authority by agencies and therefore contrary to the fundamental underpinnings of our system of administrative law.[193] We have two additional responses to this argument.

First, the argument says nothing about the substantive critique of traditional regulation; rather, it is an attack on the process of making policy, not its content. If there are positive-sum gains to be had, the presence of flaws in the process of realizing those gains does not imply that we should forgo those gains entirely. In the Amoco-Yorktown project, the EPA waived legal requirements so that Amoco could control more pollution at less cost.[194] Few would argue that granting that waiver was a bad idea, even though the result departed from existing regulations. The obvious merits of these regulatory bargains not only compel serious consideration of regulatory bargaining as a process, but also offer hope that the slow and incremental realization of these gains already underway will demonstrate the value of the process to an ever-wider circle of people. As these bargaining processes navigate currents of resistance and lurch unevenly forward, resistance should diminish from those whose primary fear is that collaborative regulation is a tool for subverting hard-won environmental gains.

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193. For the discussion of this view, see *supra* notes 94-101 and accompanying text. While we have not yet seen the argument made in print, the recent resurrection of the delegation doctrine in the federal courts offers support for the critics of informal, ad hoc processes like Project XL. The argument is as follows. There are signs that the federal courts are growing increasingly willing to strike down broad or unconstrained legislative delegations of authority to agencies if those agencies fail to impose restrictions on the exercise of their own discretion by promulgating standards that they will follow in making decisions. *See* American Trucking Ass'ns, Inc. v. EPA, 195 F.3d 4 (D.C. Cir. 1999) (overturning EPA air quality standards on nondelegation doctrine grounds). For a commentary on this case, see Cass R. Sunstein, *Is the Clean Air Act Unconstitutional?*, 98 MICH. L. REV. 303, 309-10 (2000). As of this writing, the EPA is seeking rehearing of the *American Trucking* decision in the D.C. Circuit. However, Lisa Bressman argues that the decision follows the Supreme Court's prior signals in *AT&T v. Iowa Utilities Board*, 119 S.Ct. 721 (1999), which reached a similar conclusion with respect to the Telecommunications Act of 1996. *See* Lisa Schultz Bressman, Schecter Poultry *at the Millenium: A Delegation Doctrine for the Administrative State*, __ YALE L.J. __ (forthcoming 2000). One could argue that these decisions sigual a de facto constitutional requirement that published rules guide agency decisions, and that privately negotiated waivers from rules (even when sanctioned by agencies) like Project XL run counter to that principle. While a full consideration of that argument is beyond the scope of this Article, the argument seems to stretch those decisions too far, particularly in light of other decisions recoguizing (1) the right of agencies to make policy on a case-by-case basis, and (2) the right to waive regulatory requirements. *See* SEC v. Chenery Corp., 332 U.S. 194 (1947); *supra* note 37 and accompanying text (discussing waivers).

194. *See supra* note 24 and accompanying text.

Second, and more importantly, the bargaining-as-abdication argument attacks a straw man model of the administrative process. One need not subscribe to a pure interest group bargaining model of the policy process in order to favor collaborative regulation of the kind discussed here. Conversely, these experiments in collaboration involve no cession of authority by agencies to private actors. In each case, the EPA retains ultimate policymaking authority and has not been hesitant to use that authority irrespective of the wishes of industry and environmental stakeholders alike.[195] Our data analysis implies that fears that collaborative regulation leaves the fox in charge of the henhouse are unfounded. The EPA has vetoed Project XL proposals even when those proposals were endorsed by stakeholder bargaining groups; the EPA has done the same in the context of negotiated rulemakings. In fact, contrary to the claims of critics of reform, there is no inherent inconsistency between collaborative regulatory reform and the various public interest models of the administrative process.

To the contrary, there is a strong argument that collaborative regulation improves agencies' pursuit of the public interest, and not simply by identifying positive-sum policy changes. Collaborative bargaining can be seen as one embodiment of a more deliberative and less adversarial policy process, one that comports with the constitutional model of deliberative democracy. Indeed, some scholars have argued that elected officials can no longer deliberate in the way the founders intended, and that agencies do a better job of deliberating over policy change in the modern world.[196] It does not stretch this notion to argue that collaborative regulatory reforms embrace deliberation better than their more adversarial and legalistic alternatives. This is what some defenders of collaborative processes have argued. Jody Freeman, for example, rejects interest group bargaining models of policymaking, but is an advocate of flexible policies produced by "collaborative governance," including negotiated rulemaking and processes like Project XL.[197] Jim Rossi offers an even more self-conscious version of this argument, and sees "consensus solutions" as more consistent with deliberative democracy than traditional alternatives.[198] For these

195. William Funk argues that the EPA has ceded policymaking initiative, if not policymaking authority, to private groups. *See* Funk, *supra* note 70, at 1382. If so, it is hard to see how this represents a change from traditional policymaking processes, whether legislative or agency-based. Interest groups are a common source of policy initiatives, and always have been.

196. *See generally, e.g.*, ROHR, *supra* note 15 (making this general argument outside of the context of regulatory reform).

197. Freeman, *supra* note 36, at 82-90.

198. Rossi, *supra* note 108, at 239 ("[C]onsensus solutions are more legitimate than mere preference aggregations. . . ."). In fact, Rossi's view is the polar opposite of William Funk's.

reasons, the normative argument against collaborative regulation as an abdication of authority seems weak.

Despite its merits, however, collaborative regulation faces some remaining obstacles. While collaborative regulation may sell itself to some of its current opponents over time, the incentive to bargain strategically remains. As this Article has shown, that incentive, combined with the statutory obstacles to widespread use of collaborative regulation, imposes formidable transaction costs on bargaining. As transaction costs go up, the number of positive-sum changes worth pursuing goes down. The problem is exacerbated by the EPA's efforts to structure the bargaining process in ways that increase those costs. Indeed, other studies of the XL program have pointed toward EPA resistance as a key component of transaction costs.[199]

Of course, there is no shortage of proposed solutions to this problem, and some proponents of collaboration are sanguine about the possibility of legislative or other changes that would ease restrictions on the EPA's ability to pursue positive-sum change. Edward Weber, for example, sounds a call for developing a system for pluralistic bargaining under rules that build trust and facilitate information sharing and consensus building.[200] Similarly, Freeman advocates legislation authorizing the EPA to waive legal requirements that would otherwise preclude positive-sum policy changes.[201] Others have issued similar calls for lifting statutory constraints to policy proposals produced by consensus bargaining.[202] Policy proposals produced by collaborative

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Whereas Funk sees agencies as making policy through a process of "instrumental rationality", *see supra* note 105, Rossi sees the administrative process as neither "solely instrumental [n]or strategic . . ." *See* Rossi, *supra* note 108, at 205-06. Like Funk, Rossi sees government as responsible for "defining virtue," but argues that this can best be achieved through consensus processes. For a good discussion of the deliberative democracy model, see generally Seidenfeld, *supra* note 36.

199. *See, e.g.*, GENERAL ACCOUNTING OFFICE, ENVIRONMENTAL PROTECTION: CHALLENGES FACING EPA'S EFFORTS TO REINVENT ENVIRONMENTAL REGULATION, GAO/RCED-97-155, at 6 (July 2, 1997) (concluding that XL has been hampered by a failure to secure "buy-in" from EPA staff). Another study by Resources for the Future allocated transactions costs into several categories; most frequently cited were: (i) those related to the "lack of coordination among EPA offices" and (ii) those related to the lack of clarity of the superior environmental performance criterion. Allen Blackman & Jan Mazurek, *The Cost of Developing Site-Specific Environmental Regulations: Evidence from EPA's Project XL*, Resources for the Future Discussion Paper #99-35, at 16 (Apr. 1999).

200. Indeed, Weber thinks that collaboration will grow even in relatively inhospitable environments because of the gains from trade to be had. *See* WEBER, *supra* note 24, at 256-64.

201. *See* Freeman, *supra* note 36, at 90.

202. *See* Geltman & Skroback, *supra* note 64, at 33-34; Mank, *supra* note 40, at 70-88. For a slightly different view, see generally Hirsch, *supra* note 40 (arguing that the EPA's implied

processes are sufficiently new that we do not yet know how courts will resolve disagreements over their legality. However, to the extent that the existing legal regime impedes positive-sum change, the argument in favor of reducing those impediments is a persuasive one, since there appear to be unrealized gains from trade to be had. As of this writing, two members of the U.S. House of Representatives are developing legislation that would grant the EPA additional authority to grant waivers from existing regulatory requirements where necessary to implement positive-sum regulatory bargains.[203]

While this kind of legislation does nothing to change national environmentalists' incentives, we believe it has value nevertheless, for three primary reasons. First, it reduces the leverage that opponents of bargaining within the EPA can exert, by eliminating two of their tools of opposition: (i) the procedural requirement of notice and comment rulemaking each time the EPA authorizes a regulatory waiver;[204] and (ii) the argument that such waivers are illegal.[205] This should ease the passage of stakeholder bargains through the maze of veto points, at least at the margins. Second, it enhances the legitimacy of collaborative regulation by adding the imprimatur of Congressional approval—that is, by adding a legislative endorsement to the bargaining process itself.[206] Third, it reaffirms the authority of the EPA to oversee and approve these bargains.[207]

The importance of this last attribute of the legislative fix cannot be overstated. Given the political history of environmental regulation and of the EPA's role in that contentious history, any attempt to circumvent EPA approval—even if that approval is sometimes unreasonably withheld—is doomed to failure. National environmentalists inside and outside the Agency have proven time and again that they will be heard in the environmental policy process. Any attempt to

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authority to waive legal requirements is sufficient). But see the discussion of waiver authority, *supra* note 40.

203. *See* Second Generation of Environmental Improvements Act of 1999 ("SGEIA") (draft) (on file with authors). The prospective bill is being developed by Representatives Calvin Dooley (D-Cal.) and James Greenwood (R-Penn.).

204. *See id.* at Title II (outlining the process and authorizing regulatory waivers).

205. For a discussion of this issue, see *supra* Sections II.B-C.

206. See *id.*, especially §§ 201-203 (outlining a process not unlike the current XL process, and specifying that bargains include "better environmental results"). In our view, the concept of "better environmental results" is defined unnecessarily narrowly in the current draft. The term appears to require actual reductions *of each pollutant* covered by any regulatory bargain, thereby excluding multi-pollutant or multimedia caps that might be viewed universally as environmental improvements.

207. *See id.* at § 203 (b)-(d).

ignore or avoid their input would strengthen the hand of opponents of collaborative regulation within the Agency.[208] Conversely, by affirming the EPA's authority to approve (and disapprove) regulatory bargains, legislation may foster an environment within the Agency that is more conducive to reform.[209] Perhaps proponents of collaboration have not fully appreciated the political context within which reform must occur, and why their every action has seemed to provoke an equal and opposite reaction. The question is whether the disappointing results of collaboration to date represent learning or failure. We hope they represent the latter. American environmental politics being what they are, the cause of collaborative regulation can be advanced only through a collaborative, and therefore incremental, process. In our view, it is a cause worth advancing.

208. Indeed, the fanfare and bold proclamations of fundamental change that accompanied the launch of Project XL may have contributed to its early problems by provoking just such a response within the EPA. By better defining the limits of the process, legislation may help the EPA embrace innovation.

209. For the same reasons, the SGEIA's inclusion of citizen suit provisions is wise politically. *See* SGEIA, *supra* note 203, § 205(b) (1).