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EPA's Oil and Gas Storm Water Discharge Rule Struck Down by Federal Court of Appeals

By Joel R. Burcat and Jane Kozinski

In a rebuke of the Environmental Protection Agency, a panel of judges on the Ninth Circuit Court of Appeals, vacated an EPA rule that exempted oil and gas exploration activities from storm water permit requirements. *Natural Resources Defense Council v. EPA*.¹

The Natural Resources Defense Council (NRDC) and other advocacy groups had challenged an EPA rule², that attempted to exempt from permitting requirements under the Federal Clean Water Act (CWA) discharges of sediment from oil and gas exploration, production and transmission activities that contribute to violations of water quality standards. In a 2-1 decision, a panel of the Ninth Circuit Court of Appeals agreed with the petitioners and vacated EPA's regulation.

Background

The CWA requires all discharges of pollutants from point sources to obtain an NPDES permit. Amendments to the CWA required NPDES permits for storm water sources. The CWA also exempted from permitting certain storm water sources; in particular, storm water from oil, gas and mining operations that were not contaminated with overburden, raw material, intermediate products, finished product, byproducts, or waste products located on the site of such operations.³

In 1990, EPA issued its Phase I storm water rule which required NPDES Permits for construction activities that disturb five acres or more. With respect to oil and gas operations, EPA codified the conditions that would be

¹ ___ F.3d ___, 2008 Westlaw 2152063 (9th Cir. 2008).

² Amendments to the National Pollutant Discharge Elimination System (NPDES) Regulations for Storm Water Discharges Associated With Oil and Gas Exploration, Production, Processing, or Treatment Operations or Transmission Facilities, 71 Fed. Reg. 33,628 (Jun. 12, 2006) (codified at 40 C.F.R. § 122.26).

³ CWA § 402(l); 33 U.S.C. § 1342(l) provides:

The Administrator shall not require a permit under this section, nor shall the Administrator directly or indirectly require any State to require a permit, for discharges or storm water runoff from mining operations or oil and gas exploration, production, processing, or treatment operations or transmission facilities, composed entirely of flows which are from conveyances or systems of conveyances (including but not limited to pipes, conduits, ditches, and channels) used for collecting and conveying precipitation runoff and which are not contaminated by contact with, or do not come into contact with, any overburden, raw material, intermediate products, finished product, byproduct, or waste products located on the site of such operations.

considered contamination, limiting the applicability of the CWA oil, gas and mining exemption to such operations.⁴ Forecasting how the majority would later rule, the Court set out at length those provisions of the oil and gas Phase I storm water regulation, and EPA's explanation of the regulation, that indicated there was a great likelihood of contamination of storm water as it comes into contact with residues associated with oil and gas operations.

In 1999, EPA issued its Phase II storm water rule, expanding the NPDES storm water program to address storm water discharges from construction sites that disturb one to five acres (small construction sites). Under this rule, small construction sites were required to obtain an NPDES permit by March 10, 2003. The Court pointed out that in 2002, EPA had determined that close to 30,000 oil and gas sites, annually, could be affected by the Phase II rule.⁵

After EPA granted itself several extensions to promulgate the NPDES permit to effectuate this Phase II requirement and prior to promulgating a new regulation, in 2005, Congress enacted the Energy Policy Act of 2005. The new law addressed the issue of permit requirements for storm water discharges from oil and gas construction sites.⁶ As the Court pointed out, the Energy Policy Act amended the CWA by defining "'oil and gas exploration, production, processing, or treatment operations, or transmission facilities' to specifically include related construction activities thereby bringing such activities within the CWA section 402(1)(2) exemption from the NPDES permitting requirement."

Based upon its interpretation of section 402(1)(2) of the CWA, as amended by the Energy Policy Act, EPA proposed to clarify its regulations so that a "water quality standard violation for sediment alone does not trigger a permitting requirement."⁷ EPA reasoned that "a plain reading of [Section 402(1)(2)] suggests that oil and gas sites where runoff is not contaminated by contact with raw material, intermediate products, finished product, byproduct or waste product located at the site are not required to obtain NPDES Permits, even in situations where runoff might be contributing to a violation of water quality standards." The final rule specified that EPA would not require NPDES Permits for discharges of storm water runoff from oil and gas operations.⁸ The Court held that "pursuant to this rule, EPA cannot require permits for storm water discharges comprised solely of sediment from oil and gas construction activities, even if such discharges contribute to a violation of a water quality standard."

Review of EPA's regulation

In their challenge to the final rule, the NRDC and the other advocacy groups argued that the final rule contravened Congressional intent and constituted an impermissible interpretation of section 402(1)(2) of the CWA, as amended by the Energy Policy Act of 2005. EPA responded by arguing that the new regulation merely codified Congress's "unambiguous intent" to exclude such discharges from NPDES permitting requirements. EPA further argued that even if Congressional intent was not readily ascertainable, EPA's interpretation of the statute was reasonable and permissible.

⁴ 40 C.F.R. § 122.26(c)(1)(iii).

⁵ NRDC v. EPA, at *4, citing 67 Fed. Reg. 79,828 (Dec. 30, 2002).

⁶ 33 U.S.C. § 1362(24).

⁷ 71 Fed. Reg. 894, 898 (Jan. 6, 2006).

⁸ 71 Fed. Reg. 33,628 (codified at 40 C.F.R. § 122.26(a)(2)(ii)):

(2) The Director may not require a permit for discharges of storm water runoff from the following:...

(ii) All field activities or operations associated with oil and gas exploration, production, processing, or treatment operations or transmission facilities, including activities necessary to prepare a site for drilling and for the movement and placement of drilling equipment, whether or not such field activities or operations may be considered to be construction activities, except in accordance with paragraph (c)(1)(iii) of this section. Discharges of sediment from construction activities associated with oil and gas exploration, production, processing, or treatment operations or transmission facilities are not subject to the provisions of paragraph (c)(1)(iii)(C) of this section.

Standard of review and decision

The Court followed the two-step approach for reviewing an agency's interpretation of a statute as set out by the Supreme Court in *Chevron U.S.A., Inc. v. Natural Resources Defense Council*. 467 U.S. 837, 842-44 (1984). The first step of the *Chevron* analysis requires a court to "use 'traditional steps of statutory construction' to determine whether Congress has unambiguously expressed its intent on the issue before the court." Under the statutory analysis step, the Court held that "the plain language of section 402(l)(2). . . does not indicate whether or not Congress intended that the NPDES permit exemption cover storm water discharges contaminated solely with sediment." Further, after reviewing the legislative history of CWA section 402(l)(2), the court held that Congress did not "unambiguously intend[] to exempt (or not exempt) from NPDES permitting requirements discharges of storm water runoff contaminated solely with 'sediment.'"

In step two of the *Chevron* analysis, a court must determine whether the agency's interpretation of the statute is permissible. The Court noted that it need not find that EPA's interpretation is the *only* permissible construction of the statute, but that the agency's interpretation was not arbitrary and capricious. In this case, the Court found that EPA's interpretation of the CWA was arbitrary and capricious:

Thus, EPA argues that, because "sediment is the pollutant most commonly associated with construction activities," Congress must have meant to exempt all construction-related sediment when it made construction activities eligible for the exemption, or else the amendment would be effectively meaningless. See 71 Fed. Reg. at 33634. We conclude, however, that EPA's interpretation of the CWA section 402(l)(2), as amended by the Energy Policy Act, is arbitrary and capricious because of the agency's changed position on what constitutes "contamination" under that section.

To interpret the regulation the Court focused on EPA's extensive statements, some of which were nearly 20 years old, relating to storm water permitting, as to what constitutes "contamination". The Court took EPA to task for attempting to "minimize and justify its earlier stance" regarding runoff contaminated with sediment. The Court found EPA's arguments to be "unpersuasive in light of EPA's own statements during its rulemaking process prior to the passage of the Energy Policy Act of 2005." The Court ruled that the new regulation "is arbitrary and capricious and constitutes and impermissible construction of 402(l)(2) of the CWA."

The dissent

In Judge Consuelo M. Callahan's dissent, she agreed with the majority that the *Chevron* analysis was the correct analysis for the Court to utilize and she agreed that Congress's legislative intent could not be gleaned from the "scant legislative histories" for section 402(l)(2). Judge Callahan, however, would have held that EPA's interpretation of the statute was a permissible interpretation. Further, Judge Callahan noted that the mere fact that an agency interpretation contradicts a prior agency position is not fatal.⁹ Judge Callahan stated that "EPA provided a reasoned analysis that adequately explains its revised interpretation of section 402(l)(2)."

What it means

Now that EPA's storm water permit exemption for oil and gas exploration activities has been vacated, what does that mean for the oil and gas industry?

⁹ NRDC at *12, citing *Smiley v. Citibank (South Dakota), N.A.*, 517 U.S. 735, 742 (1996).

EPA could choose to appeal the 9th Circuit's decision. In that case, it is impossible to predict if the Supreme Court would entertain such an appeal, and if so, how it might rule. If EPA chooses to live with the 9th Circuit's decision, it means that oil and gas exploration activities resulting in sediment discharges which violate water quality standards must seek an individual permit or coverage under a general permit. Storm water management and pollution prevention plan requirements would also be triggered for regulated sources. If EPA is correct that it will receive tens of thousands of storm water NPDES permit applications annually from the oil and gas industry, then EPA and the states will have a find a way to either manage the volume of applications or streamline the application procedure to keep pace with exploration activities.

For states like New York, Pennsylvania, Maryland and West Virginia, that are already seeing an onslaught of new gas well applications as a result of the Marcellus shale gas discovery and other new applications that are being filed as a result of the high cost of energy supplies, the burden of processing applications will be significant.

In any event, considering the time frame for either an appeal to the Supreme Court or a revision to the regulations to take into consideration the Court's ruling, the EPA will be under new management when all of this is finally resolved.

This Bulletin was written by Joel R. Burcat, Co-chair of Saul Ewing's Environmental Department and Jane Kozinski, a Partner in Saul Ewing's Environmental Department. If you have questions or wish to discuss the contents of this Bulletin, please feel free to contact Mr. Burcat at 717.257.7506 or jburcat@saul.com or Ms. Kozinski at 215.972.7981 or jkozinski@saul.com, or visit us at www.GasAndOilLawyers.com. This publication has been prepared by the Environmental Department for information purposes only.

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