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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS, *et al.*, Plaintiffs and Plaintiff-Intervenors, and SAN FRANCISCO CHAMBER OF COMMERCE, *et al.*, Plaintiff-Intervenors v. MICHAEL CHERTOFF, *et al.*, Defendants.	CASE NO. C07-cv-04472-CRB

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT AND IN OPPOSITION TO DEFENDANTS' MOTIONS FOR SUMMARY JUDGMENT AND TO VACATE THE PRELIMINARY INJUNCTION

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SUMMARY OF ARGUMENT

This matter is before the Court a second time to resolve a dispute over the Department of Homeland Security's ("DHS") promulgation of new regulations addressing the significance of an employer's receipt of a "no-match" letter from the Social Security Administration (the "No-Match Rule"). On October 10, 2007, this Court enjoined the No-Match Rule, in part, because Defendants had failed to conduct a Regulatory Flexibility Act ("RFA") analysis. *See AFL-CIO v. Chertoff*, 552 F. Supp. 2d 999, 1011-13 (N.D. Cal. 2007). Defendants had taken the position that an RFA analysis was unnecessary because the rule was voluntary and therefore, imposed no additional burdens on small entities. This Court disagreed concluding that "DHS's response that the safe harbor rule will impose no costs because compliance is 'voluntary' is wholly unavailing." *Id*. at 1013. Although DHS filed an appeal to the Ninth Circuit, it later dismissed that appeal with prejudice.

Defendants now claim that they have completed the required RFA analysis mandated by this Court, and that the injunction should therefore be vacated and summary judgment entered. Defendants argue that as long as they can "demonstrate a reasonable, good-faith effort" to comply with the RFA, no more is required. 73 Fed. Reg. at 63850 (col. b), 63855 (col. b) (internal citations omitted). Using that logic, no matter how infirm that analysis may be, a court is obligated simply to accept it without any examination of the content or rationale of that analysis. The RFA contains no such "free pass." Defendants receive no deference for this interpretation of the RFA because DHS does not administer the RFA. *See Aeronautical Repair Station Ass'n v. FAA*, 494 F.3d 161, 176 (D.C. Cir. 2007); *American Trucking Ass'n v. EPA*, 175 F.3d 1027, 1044 (D.C. Cir. 1997) (same), *modified in other respects*, 195 F.3d 4 (D.C. Cir. 1999), *reversed on other grounds sub nom. Whitman v. Am. Trucking Ass'n*, 531 U.S. 457 (2001).

Judicial review is available to test whether an agency's "compliance with the requirements of sections 601, 604 [requiring and describing the final regulatory flexibility analysis], 605(b), 608(b), and 610 in accordance with chapter 7." 5 U.S.C. § 611(a)(1). Chapter 7, of course, requires a court to set aside agency action that is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law[.]" 5 U.S.C. § 706(2)(A). In determining whether Defendants complied in "good faith" with the RFA, a court is "not obligated to proceed myopically through the field of inconsistencies presented by the government's view of pertinent matters. Effective and informed judicial review is contemplated by the . . . the RFA." *Southern Offshore Fishing Ass'n v. Daley*, 55 F. Supp. 2d 1336, 1340 (M.D. Fla. 1999) (internal quotations and citations omitted).

Defendants' Final RFA analysis is "arbitrary and capricious" in four objective respects. First, it is not only internally inconsistent, but it is inconsistent with the analyses and forecasts of its own expert. Second, the analysis is incomplete. The Final RFA and the underlying analyses of its contractor, Econometrica, Inc., ignore the rule's impact on not-for-profit entities and on small local governmental entities, all of which qualify as small entities under the RFA and can be easily identified. The Final RFA analysis therefore only addresses one-third of the groups covered by the RFA—*i.e.*, small businesses. "In baseball, a batting average of" .333 "is enviable indeed. Judiciary wise, such an average sends one to the showers in a hurry." *Oregon Nat'l Res. Council v. Marsh*, 677 F. Supp. 1072, 1079 (D. Or. 1987); *see also Central Mfr'g, Inc. v. Brett*, 492 F.3d 876, 787 (7th Cir. 2007). Third, many of the assumptions underlying the Final RFA analysis are objectively incorrect and significantly understate the costs of complying with the Final Rule. And fourth, the Final RFA analysis was out of date when it was published; it failed to take into account the significant crisis in world credit markets that occurred nearly two months before the rule was issued on October 28, 2008. *See Paulson Announces "Troubled Asset Relief Program*,"

Bloomberg.com (Sept. 19, 2008) <http://www.bloomberg.com/apps/news?pid=20601087&sid=akDKPN1hzMZg&refer=home>. Using outdated assumptions, data, and analyses does not constitute a reasonable, good-faith effort: it is arbitrary and capricious.

STATEMENT OF THE ISSUE

Did the Defendants violate the RFA by failing to assess the Rule's impact on not-for-profit organizations, by presenting overall cost estimates that are inconsistent with the estimates of their experts, by under-estimating costs, and by ignoring the recent downturn in world credit markets?[1]

STATEMENT OF FACTS

1. Final Rule

On August 15, 2007, the Secretary of Homeland Security issued the Final No-Match Regulation, certifying under the RFA that the Rule "would not have a significant economic impact on a substantial number of small entities." 72 Fed. Reg. 45611, 45623 (col. a) (Aug. 15, 2007). The Secretary, however, provided no factual basis for this certification.

2. Plaintiff-Intervenors' Lawsuit

The Plaintiff-Intervenors ("Business Plaintiffs"), eight not-for-profit membership associations of businesses, filed suit alleging that the final rule was fatally infirm for three reasons. First, it exceeded the Secretary's statutory authority in a number of respects including that its definition of "knowingly" in the final rule was neither authorized by nor consistent with the organic legislation, and the obligations imposed on employers constituted a re-verification system in contravention of federal law. *See* Cause of Action Two, Business Plaintiffs' First Amended Compl. (doc. # 138) ("Compl.") at ¶¶ 63-64; 8 U.S.C. § 1324a; 5 U.S.C. § 706(2)(A) ("not in accordance with law") and § 706(3)(C) (in excess of agency's jurisdiction or authority). Second, the regulation was arbitrary and capricious in that it assumed a relationship between an employee's

[1] Whether the No-Match Rule is authorized by the organic legislation or whether it lacks a rational factual basis are addressed in the Union Plaintiffs' Brief, which legal arguments and relevant Statement of the Facts are adopted herein.

immigration status and a Social Security mismatch when in fact DHS did not know and still does not know the conditional probability that an employee is undocumented given that his or her name appears on a no-match letter. *See id.* at ¶ 65; 5 U.S.C. § 706(2)(A). Third, the Secretary violated the RFA by failing to present an RFA analysis. *See id*. at ¶¶ 58-62.

3. This Court's Decision

On October 10, 2007, this Court concluded that, among other defects in the No-Match Rule, Defendants had failed to justify the Secretary's certification under the RFA that the rule would not have a significant impact on substantial number of small businesses. *Chertoff*, 552 F. Supp. 2d at 1013. Defendants had argued that the rule was entirely voluntary and therefore imposed no new requirements and hence no new costs on employers. The Court rejected this argument as "wholly unavailing," finding "it likely that small businesses would incur significant costs associated with complying with the safe harbor rule[,]" (73 Fed. Reg. at 15951 (col. a), because "[t]he rule as good as mandates costly compliance with a new 90-day timeframe for resolving mismatches. "Accordingly, there are serious questions whether DHS violated the RFA by refusing to conduct a final flexibility analysis." *Id.* at 1013

The Court also concluded that two other claims raised by Plaintiffs presented serious issues justifying the imposition of an injunction. Specifically, the Court found that Plaintiffs had raised at least a serious question regarding whether DHS's action was arbitrary and capricious because the agency had changed its position regarding the significance of no-match letters without a reasoned analysis. 552 F. Supp. 2d at 1009-10. The Court further held that Plaintiffs had raised a serious question as to whether DHS had impermissibly exceeded its authority by interpreting IRCA's anti-discrimination provisions to preclude enforcement against employers who follow the "safe harbor" procedures of the new rule. *Id.* at 1010-11.

Following the Court decision, Defendants noticed an appeal and filed an opening brief with the Court of Appeals for the Ninth Circuit. Pursuant to Defendants' request, the appeal was dismissed.

4. Supplemental Rulemaking and Regulatory Flexibility Act Analysis

Following this Court's decision granting Plaintiffs' motions for a preliminary injunction, Defendants issued a Supplemental Proposed Rule on March 26, 2008. *See* 73 Fed. Reg. 15944 (March 26, 2008). The Proposed Rule contained a section entitled "Initial Regulatory Flexibility Act Analysis," which was ostensibly based on a Small Entity Impact Analysis ("SEIA") prepared by Econometrica, Inc., a government contractor. Econometrica issued two reports, an initial report on January 15, 2008, and a final report on August 25, 2008. *See* Econometrica, Inc. "Final Report--Small Entity Impact Analysis: Safe-Harbor Procedures for Employers Who Receive a No-Match Letter," ("Initial SEIA") Contr. No. GS-23F-0048P (Jan. 15, 2008), docketed as Document ICEB-2006-0004-0233, Supplemental Administrative Record ("SAR") at 1705. Defendants also inserted into the record a slightly modified rendition of that analysis that they claim to have used as the basis of their Final RFA analysis. *See* Econometrica, Inc. "Final Small Entity Impact Analysis: Safe-Harbor Procedures for Employers Who Receive a No-Match Letter," ("Final SEIA") Contr. No. GS-23F-0048P (Aug. 25, 2008), docketed as Document ICEB-2006-0004-0921, appearing at SAR at 3666.

In their Final RFA analysis the Defendants continue to argue that the Rule is voluntary and imposes no new costs on small entities. Defendants assert that if there are costs associated with the rule, those costs are less than $100 million per annum across the entire economy.

The Final Supplemental Rule of October 28, 2008, the Proposed Supplemental Rule of March 26, 2008, and the original Final Rule of August 15, 2007, are identical. The Proposed Supplemental Rule and the Final Supplemental Rule each presented a table from the SEIA setting

out Defendants' estimate of the costs incurred by various sized business to implement the rule. Those costs would vary, according to the preamble, based on the size of the business and the percentage of its workforce listed in no-match letters that was authorized. Both SEIAs then delineated seven classes of activities that employers would have to undertake to comply with the new regulation and assigned a cost to each, as follows: (1) Legal Costs; (2) Accounting Costs; (3) Human Resources Administrative Costs; (4) Cost of Lost Employee Time; (5) Miscellaneous Administrative Costs; (6) Costs of Research, Management and Internal Meetings; and (7) Employee Replacement Costs. *See* SAR at 3709. Each SEIA, also, assumed that two percent of authorized employees listed in no-match letters would be unable to resolve the mismatch within the 93-day window. Neither version of the SEIA presented any data to support this two-percent assumption.

ARGUMENT

I. Standards of Review

A. Regulatory Flexibility Act

Small entities are entitled to judicial review of an agency's Regulatory Flexibility Act analysis or an agency's certification that no such analysis is required. The standard is set forth in the Administrative Procedure Act § 10(e), 5 U.S.C. § 706(2), which provides, in part, that an agency action may be set aside if it is arbitrary, capricious or an abuse of discretion. *See* 5 U.S.C. § 611, *incorporating by reference* 5 U.S.C. § 706(2).

B. Motion for Summary Judgment

A movant is entitled to summary judgment under Fed. R. Civ. P. 56(a) where there are no genuine issues of material fact and the only issues before the court involve questions of law. *See James River Ins. v. Schenk*, 523 F.3d 915, 920 (9th Cir. 2008).

C. Motion to Vacate a Preliminary Injunction

In moving to dissolve the injunction, Defendants "bear[] the burden of establishing that a *significant* change in facts or law warrant[] revision or dissolution of the injunction." *Kontrabecki v. Oliner*, 318 B.R. 175, 180 (N.D. Cal. 2004) (quoting *Sharp v. Weston*, 233 F.3d 1166, 1170 (9th Cir. 2000)) (emphasis added); *see Rufo v. Inmates of Suffolk County Jail,* 502 U.S. 367 (1992). It is not enough that Defendants have responded in some way to the preliminary injunction. The court "will not presume that the [Defendants'] corrective action plan has succeeded;" rather, Defendants bear the burden of "show[ing] that the conditions warranting preliminary injunctive relief . . . have been remedied." *Reynolds v. Giuliani*, 118 F. Supp. 2d 352, 364 (S.D.N.Y. 2000). If the Defendants fail to carry their burden of demonstrating that the Court's prior conclusions are no longer warranted, the preliminary injunction should remain in force. *See Vaughn v. St. Helena Parish Police*, 261 F. Supp. 2d 553, 555 (M.D. La. 2002).

Here, Defendants' motion does not contend that the balance of hardships no longer tips heavily in Plaintiffs' favor. Rather, Defendants assert only that, in light of the analysis contained in the supplemental rulemaking, there are no longer serious questions with respect to the validity of the rule. As Business Plaintiffs demonstrate below, they are entitled to summary judgment and, therefore, Defendants have failed to meet their burden for dissolution of the injunction.

II. Summary Judgment in Plaintiffs' Favor is Appropriate For Defendants' Violation of the RFA

The RFA is an analytical tool, not a mechanical checklist. In enacting the RFA, 5 U.S.C. §§ 601-612, as amended in 1996 by the Small Business Regulatory Enforcement Fairness Act ("SBREFA"), Pub. L. No. 114-121, Title II, 110 Stat. 847, 857-74, §§ 201-253 (codified at 5 U.S.C. § 601-612 (1994 & Supp. II 1996)), Congress expressly recognized that agency rules frequently had a disproportionate adverse impact on small entities--small businesses, not-for-profit

organizations, and small governmental entities. Small entities, for example, face practical difficulties in complying with federal rules that differ significantly from those encountered by their larger counterparts, including "their limited access to capital," that "small concerns must borrow heavily to make modifications[,]" and that costs of complying cannot be easily absorbed or spread by small entities as they can by larger entities. Sen. Rep. No. 878, 96th Cong., 2d Sess. 4 (1980). Small entities lack access to the equity markets and "[e]ven if small businesses can afford additional debt, banks and other lenders are often reluctant to loan money for improvement purposes not related to productivity." *Id*. This lack of access to financing--whether debt or equity--became particularly acute starting in September 2008, and only worsened through October 28, the date of issuance of the instant final rule.

In light of this disparate impact, Congress in the RFA required agencies, as part of the rulemaking process, to conduct an initial and then final regulatory analysis. These analyses compel the agency to ascertain the economic impact that a proposed rule will have on small entities, to set out the less onerous alternatives considered by the agency and to discuss the agency's rationale for declining to adopt these less costly alternatives. *See* 5 U.S.C. §§ 603-604.

Defendants suggest that the RFA is procedural rather than substantive, and as such, simply imposes a to-do list of tasks. According to Defendants, once each item on the list has been checked-off, they have satisfied their obligations under the RFA. Whether one views an agency's obligations under the RFA as procedural or substantive, though, begs the real question: is the agency's analysis "arbitrary or capricious." *See* 5 U.S.C. § 611, incorporating 5 U.S.C. § 706. The RFA, like other economic-based law, focuses on "economic reality . . . rather than a mechanical checklist." *Tuazon v. R.J. Reynolds Tobacco Co*., 433 F.3d 1163, 1173 (9th Cir. 2006) (internal quotations and citations omitted) (evaluating minimum contacts for *in personam* jurisdiction).

A. Defendants' Final RFA Analysis Fails to Comply with the RFA's Specific Requirements

1. Defendants Ignored the Analysis of their Own Experts Creating an Unexplained $1 Billion Per Annum Discrepancy

The first step in any RFA analysis is determining the proposed rule's impact, if any, on small entities. The magnitude of the impact on small entities should focus the prophylactic steps an agency should consider and should influence whether the agency should adopt various options to mitigate that impact. Arguably, where the impact is small, an agency's responsibility to minimize untoward effects on small entities is small; where the impact is large so too is the agency's responsibility. Thus, the linchpin of any RFA analysis, as Defendants recognize, is "to measure and consider the regulatory impact of the rule to determine whether there will be a significant economic impact on a substantial number of small entities." 73 Fed. Reg. at 63850 n.5 (quoting Office of Advocacy, Small Business Administration, *A Guide for Government Agencies: How to Comply with the Regulatory Flexibility Act* (2003). The agency must undertake this analytical step in a rational manner, unfettered by improper considerations and uninfected by unreasonable data.

In that regard, an agency's decision-making is arbitrary and capricious if it "has relied on factors which Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise." *Motor Vehicle Mfrs. Ass'n of U.S. v. State Farm Mut. Auto. Ins. Co*., 463 U.S. 29, 43 (1983). An agency acts arbitrarily when it ignores the advice of its own experts.[2]

[2] There is a well developed body of scholarship in Information Theory that demonstrates how a decision-maker should integrate varying expert opinions to minimize the likelihood of drawing incorrect conclusions. *See* Alan R. Sampson and Robert L. Smith, *An Information Theory Model for the Evaluation of Circumstantial Evidence*, SMC-15 IEEE TRANSACTIONS ON SYSTEMS, MAN

See Pac. Coast Fed'n of Fishermen's Ass'ns, Inc. v. Nat'l Marine Fisheries Serv., 265 F.3d 1028, 1037-38 (9th Cir. 2001) (agency acted arbitrarily and capriciously by ignoring its own expert advice where no contrary recommendations existed in the record); *Ctr. For Biological Diversity v. Lohn*, 296 F. Supp. 2d 1223, 1239-40 (W.D. Wash. 2003) (finding that agency erred because it "ignored its experts' conclusions that the global taxon is inaccurate and that the best available science demonstrates that resident and transient killer whales do not belong to the same taxon"); *Northern Spotted Owl v. Hodel*, 716 F. Supp. 479, 483 (W.D.Wash. 1988); *see also Sierra Club v. United States Army Corps of Eng'rs*, 701 F.2d 1011, 1030 (2d Cir. 1983) (concluding that a reviewing court "may properly be skeptical as to whether an EIS's conclusions have a substantial basis in fact if the responsible agency has apparently ignored the conflicting views of other agencies having pertinent expertise.").[3] That is what has occurred here.

Here, the public was presented with two sets of measurements, one developed by Econometrica, Inc., under contract to Defendants, and the other reported by the Defendants. The two sets of measurements ought to be the same, but they are not and in fact, differ by more than an order of magnitude, *i.e.*, a factor of ten. Specifically, Defendants repeatedly state that the No-Match Rule will have an impact on the entire economy of less than $100 million per year. *See* 73 Fed. Reg. 63866 (col. c) (concluding that this "rule has not been found to be likely to result in an annual effect on the economy of $100 million or more."); *id*. ("OMB has determined that this rule will not have an effect on the economy of more than $100 million."); 73 Fed. Reg. 63866 (col. c).

AND CYBERNETICS 9-16 (1985); Alan R. Sampson and Robert L. Smith, *Assessing Risks Through the Determination of Rare Probabilities*, 8 OPERATIONS RESEARCH 839-866 (1982). Under no scenario is a rational decision supposed to ignore expert advice.

[3] Agencies may depart from expert advice from their consultants, employees or even an agency's prior expert views. However, when an agency does so, it must provide a "reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored." *Greater Boston Television Corp. v. Fed. Commc'ns Comm'n*, 444 F.2d 841, 852 (D.C. Cir. 1970); *see also Philadelphia Gas Works v. FERC*, 989 F.2d 1246, 1250-51 (D.C. Cir. 1993).

("[t]his rule will not result in the expenditure by State, local, and tribal governments, in the aggregate, or by the private sector, of $100 million or more in one year, and it would not significantly or uniquely affect small governments.").

The data presented by Econometrica reveal that the impact on small businesses alone, excluding not-for-profit entities and local governments, will likely exceed $1 billion per annum under favorable assumptions and considerably more under less favorable assumptions. Defendants make no attempt to reconcile this disparity between what they report in their preamble and what their experts say in the docket, but Defendants do not even acknowledge the disparity.

This is reminiscent of the so-called "malpractice rule" fiasco, where Medicare sought to alter the way in which it reimbursed hospitals for their malpractice insurance. The rule was based on a study commissioned by Medicare and performed by an outside contractor which had a limited scope. Medicare nonetheless used the study as the basis of regulation even though the study's authors cautioned that the study could not be generalized beyond its limits. Scores of district courts and seven circuits invalidated the rule as inherently arbitrary. *See, e.g., Cumberland Med. Ctr. v. Sec'y of HHS*, 781 F.2d 536 (6th Cir. 1986); *Bedford County Memorial Hosp. v. HHS*, 769 F.2d 1017 (4th Cir. 1985); *Menorah Med. Ctr. v. Heckler*, 768 F.2d 292 (8th Cir. 1985); *Desoto Gen. Hosp. v. Heckler*, 766 F.2d 182, *as amended at* 776 F.2d 115 (5th Cir. 1985); *Lloyd Noland Hosp. and Clinic v. Heckler*, 762 F.2d 1561 (11th Cir. 1985); *St. James Hosp. v. Heckler*, 760 F.2d 1460 (7th Cir.), *cert. denied*, 474 U.S. 902 (1985); *Humana of Aurora, Inc. v. Heckler*, 753 F.2d 1579 (10th Cir.), *cert. denied*, 474 U.S. 863 (1985); *Abington Memorial Hosp. v. Heckler*, 750 F.2d 242 (3d Cir. 1984), *cert. denied*, 474 U.S. 863 (1985). Ultimately the malpractice rule was withdrawn, and overtaken by new legislation. *See Georgetown Univ. Hosp. v. Bowen*, 862 F.2d 323 (D.C. Cir. 1988).

An agency, like a scientist, is not free to ignore data—especially when presented by their experts—that may conflict with the agency's preconceived notions. Defendants have sought to do just that in this case. Not only did Defendants fail to report on the overall magnitude of the rule's effect on small entities, but Defendants buried the information so that it was not easily accessible. This is "inconsistent with rational decisionmaking by an administrative agency." *Kent County, Delaware Levy Court v. EPA*, 963 F.2d 391 (D.C. Cir. 1992) (directing an agency to supplement the administrative record with the opinions of the agency's own experts). *See also American Radio Relay v. Fed. Commc'ns Comm'n*, 524 F.3d 227, 244 (D.C. Cir. 2008) (Tatel, J., concurring).

The Econometrica report presents two matrices—Exhibit 21 (*see* SAR 3709) estimates the costs of the rule under various assumptions for various size businesses and Exhibit 4 (*see* SAR at 1215, 3677) estimates the number of businesses in each size category. Multiplying the two matrices together and summing the results yields an overall annual estimate of the rule's impact on small businesses. This was never done and never discussed because the results—over one billion dollars per annum—were inconsistent with Defendants' determination that the rule's total impact to the entire economy would be less than $100 million per annum. *See* Comment by Richard Belzer to Initial SEIA ("Belzer Comment") at 4, SAR at 1473. Sweeping unwanted data under the rug is the hallmark of arbitrary agency action. *See Or. Nat'l Res. Council v. Lowe*, 109 F.3d 521, 526-27 (9th Cir. 1997).

2. Defendants Failed to Consider the Impact of the Rule on Small Organizations and Governments

As Defendants acknowledge, "the RFA requires agencies to analyze the impact of rulemaking on 'small entities.'" 72 Fed. Reg. at 63850. Small entities are not simply small businesses, although small businesses are included in the definition of "small entities." Instead, the RFA defines "small entities" as (i) businesses denoted by the Small Business Administration as

"small" (*see* 5 U.S.C. § 601(3)); (ii) not-for-profit enterprises, also referred to as "small organizations" (*see id*. at § 601(4)); and (iii) governmental entities with jurisdiction over a population that is no larger than 50,000 persons. *See* 5 U.S.C. § 601(6) (defining "small entity"). Thus, Defendants' analysis under the RFA must take into account all three classes of small entities and must estimate the total number of small entities effected by the rule, the costs of compliance, and in light of those costs, the alternatives considered. *See* 5 U.S.C. § 604(a). That is especially important here, where all eight of the Business Plaintiffs are not-for-profit entities, as opposed to small businesses.[4]

Despite the fact that the eight Business Plaintiffs are all "small organizations," as opposed to "small businesses," Defendants' Final RFA analysis failed to estimate the number of these small entities that would be affected by the rule, failed to estimate the impact of the rule on such entities, and failed to examine ways of minimizing the rule's compliance costs on these small organizations. Defendants' analysis was geared toward small businesses and ignored the other two classes of small entities--not-for-profits and small governmental entities.[5] The preamble consistently uses the term "small business" and not "small organization" or "small governmental jurisdiction." For example, when summarizing the effects of the rule, Defendants state that "[m]ost significantly,

[4] *See* First Amended Complaint in Intervention (Doc. # 138) at ¶ 6 (noting that Plaintiff-Intervenor San Francisco Chamber of Commerce is a not-for-profit organization), ¶ 7 (noting that Plaintiff-Intervenor Chamber of Commerce of the United States of America is a not-for-profit organization), ¶ 8 (noting that Plaintiff-Intervenor Golden Gate Restaurant Association is a not-for-profit organization), ¶ 9 (noting that Plaintiff-Intervenor National Roofing Contractors Association is a not-for-profit organization), ¶ 10(noting that Plaintiff-Intervenor United Fresh Produce Association is a not-for-profit organization), ¶ 11 (noting that Plaintiff-Intervenor American Nursery & Landscape Association), ¶ 12 (noting that Plaintiff-Intervenor International Franchise Association is a not-for-profit organization), and ¶ 13 (noting that Plaintiff-Intervenor California Landscape Contractors Association, Inc. is a not-for-profit organization).

[5] The preamble mentions not-for-profits when discussing the agency's inability to determine how many not-for-profits would affected by the rule. Instead, Defendants merely state that "[a]bsent some reason to believe small non-profits or small governmental jurisdictions might implement the rule's safe harbor procedures differently from private employers, the cost structure for such entities would be no different from small firms." 73 Fed. Reg. 63862 (col. b).

none of the alternatives for limiting or tailoring the applicability of the rule to specific industries or sectors would mitigate the rule's impact on small business." 73 Fed. Reg. at 63864 (col. a-b) (emphasis supplied).

This omission is not surprising given that the SEIA relied upon by Defendants did not address not-for-profits and made no effort to estimate the number of not-for-profits or the rule's impact on them. The SEIA is devoid of any information concerning not-for-profits and its entire focus is on businesses: "This section provides a brief description of the regulated community, with a particular emphasis on the small business entities that will be affected." SAR at 3672. This omission is particularly troubling given that while a small business must in fact be "small," a not-for-profit falls within the ambit of the RFA independent of its size. Some of the largest employers in cities and communities are not-for-profits. For example, Harvard University is the largest private employer in the Boston metropolitan area, as is The Johns Hopkins University in Baltimore, and Notre Dame in South Bend, Indiana. *See Interview with Samuel Thier*, 43 J. INVESTIG. MED. 10 (1995) (Boston); Mark Millspaugh, *Baltimore Employer Partnerships* (Dec. 2006)<www.sipr.org/PDF/Baltimore%20employer%20partnerships.pdf> (Baltimore); THE OBSERVER (April 29, 2008) <http://media.www.ndsmcobserver.com/media/storage/paper660/news/2008/04/29/Viewpoint/Living.Wage.Now-3354047.shtml> (South Bend, Indiana). These larger not-for-profits are not accounted for at all in the RFA analysis: the Defendants' highest projected cost per employer is $36,624 per annum for employers with more than 500 employees. *See* SAR at 3709. This makes no sense for large employers covered by the RFA, such as Harvard, Johns Hopkins or Notre Dame, all of which employ more than 10,000 employees. Indeed, Harvard and Johns Hopkins each employ more than 20,000 individuals. If we were to extrapolate the cost per employee from the 100-499 category to Harvard, the cost would be over

$1.6 million per annum which is hardly a paltry sum. Of course, we do not know what the actual cost would be because the Defendants never bothered to examine not-for-profits.

Nor are data unavailable. Other agencies have had no difficulty in counting the number of not-for-profits affected by their rules and therefore, it is difficult to understand how or why an entire sector was ignored by these Defendants. *See* 2008 Outpatient Prospective Payment System Final Rule, 72 Fed. Reg. 66580, 66902 (Nov. 27, 2007) (noting that for RFA purposes there are 2,141 not for profit hospitals and that 37% of the for-profit hospitals would qualify as small businesses with annual revenues of less than $31 million per annum).

More significantly, though, ignoring an entire sector is the hallmark of arbitrary action. This Circuit has consistently held that an agency's action is arbitrary or capricious

> if the agency relied on factors Congress did not intend it to consider, entirely failed to consider an important aspect of the problem, offered an explanation that ran counter to the evidence before the agency, or offered one that is so implausible that it could not be ascribed to a difference in view or the product of agency expertise.

Western Radio Servs. Co., Inc. v. Espy, 79 F.3d 896, 900 (9th Cir. 1996),

In this Circuit, satisfying one out of three statutory requirements is insufficient as a matter of law. In *Brower v. Evans*, 257 F.3d 1058, 1070 (9th Cir. 2001), for instance, the court vacated as arbitrary and capricious agency action where the agency had "fail[ed] to conduct two of the three statutorily-mandated studies." *Earth Island Inst. v. Hogarth,* 494 F.3d 757, 762 (9th Cir. 2007) (recounting agency's failure in *Brower*). Yet that is precisely what Defendants have done here: their Final RFA analysis and the SEIA on which it was based ignore the rule's impact on two of the three groups that the agency is required to consider. This shortcoming, like the shortcoming in *Brower* precludes enforcement of the rule.

3. Defendants' Analysis Understates the Costs of Compliance

The epitome of an arbitrary or capricious action is when there is a mismatch (or in Defendants' parlance, no-match) between the facts attested to by the agency and the conclusions reached by the agency. A conclusion reached in the admitted absence of data is arbitrary. *See Oxy USA, Inc. v. FERC*, 64 F.3d 679, 693 (D.C. Cir. 1995) (holding that FERC's position was arbitrary and capricious when it presented no data to support it, stating: "We find this reasoning arbitrary and capricious and thus conclude that, absent a more persuasive justification, FERC's method of valuing distillates violates the APA."); *Natural Resources Defense Council v. EPA*, 966 F.2d 1292, 1306 (9th Cir. 1992) (EPA's decision not to regulate construction sites smaller than five acres was arbitrary when EPA provided no data to justify the five-acre threshold and admitted that unregulated sites could have significant water quality impacts); *National Treasury Employees Union v. Horner*, 854 F.2d 490, 492 (D.C. Cir. 1988) ("Because OPM has presented no data to support its rationale for excepting the positions, we also affirm the district court's finding that the decision was arbitrary and capricious.")

That "no-match" is readily apparent in the Supplemental Final Rule. On at least three occasions, DHS admits that there are no data to support assumptions in its RFA analysis. *See e.g.*, 73 Fed. Reg. at 63855 ("Changes in the number of no-match letters sent to employers in a given year may change the aggregate costs incurred by all employers that choose to follow the safe harbor procedures, but DHS has no data . . . that would lead DHS to conclude that such variations would alter either the share of all no-match letters in a given year that would be received by small entities or the impact felt by a specific small entity that receives a no-match letter and decides to follow the safe harbor procedures."); *id.* at 63859 ("DHS understands that some businesses cannot, through planning, mitigate productivity losses attributed to employee absences to resolve

mismatches. No data is [sic] available that suggests how many businesses have the ability to schedule other employees to take the place of an absent employee, and therefore mitigate costs."); *id.* at 63862 ("Consequently, DHS does not have the data necessary to determine the precise number of small entities expected to receive a no-match letter."). The absence of supporting data renders the conclusions reached by DHS arbitrary.

As to other decisions for which DHS (or Econometrica) cites data, that data appear to be inaccurate. The net effect of the inaccuracies underestimates the costs imposed by the Supplemental Final Rule. For example, in assessing the costs of retaining a lawyer to advise firms who seek legal counsel if they receive a no-match letter, Econometrica assumed that the need for legal counsel would be a "start-up" cost, *i.e.*, a cost needed in the first year, but less likely to be necessary once measures have been put into place to comply with the safe harbor rulemaking. *See* SAR 1729. Econometrica estimates that counsel will spend eight to forty hours providing guidance. No basis for this assumption is provided. For purposes of its analysis, it assumed an average of twenty-four hours. *Id.* Again, no basis for this assumption is specified. Econometrica then assumes that not all firms will seek legal counsel, so it assumed that half would. Here too, Econometrica concedes that it "[l]ack[s] any tangible data on the topic." SAR 3692. Finally, in determining the costs of those twenty-four hours of legal counsel, Econometrica used weighted averages for states' wages from 2006. SAR 3758. In this way, Econometrica's analysis sidesteps the considerable hike in hourly rates that occurred after 2006, a hike that is a matter of public record. Thus based on the unsupported or incomplete assumptions, Econometrica assumed that the average "outsourced" lawyer billed at a rate of $137.50 per hour, whereas in-house lawyers cost $78.75 per hour. No support for these rates is provided. Further, assuming that 16% of small businesses turned to in-house lawyers (another assumption that lacks any data), Econometrica calculated a weighted hourly rate of $128.10. SAR at 3767.

In fact, there is abundant support in the published case law and elsewhere that demonstrates that few outside attorneys' hourly rates are as low as $137.50. *See B&G Min. Co. v. Director, OWCP*, 522 F.3d 657 (6th Cir. 2008) (affirming an administrative law judge's award based on a rate of $250.00 for work performed by a Pikeville, Kentucky lawyer prior to 2005); *Barfield v. N. Y. C. Health & Hosps*., No. 06-4137-cv (L), slip op. at 36 (2d Cir. Aug. 8, 2008) (finding that $350.00 per hour was a "reasonable hourly rate"); *United Steelworkers of Am. v. v. Retirement Income Plan for Hourly-Rated Employees of Asarco, Inc.,* 512 F.3d 555, 565 (9th Cir. 2008) (affirming district court's award of $300 per hour as a reasonable hourly rate for ERISA work); *Giovannoni v. Bidna*, No. 06-15640, slip op. at 4 (9th Cir. Nov. 7, 2007) (affirming district court's award of $300 per hour as a reasonable hourly rate for work under the Fair Debt Collection Practices Act, 15 U.S.C. § 1692 *et seq.*). Surveys from 2006, the year used by Econometrica for its hourly rates similarly fail to support the rates on which Econometrica's calculations are based. The ALTMAN WEIL SURVEY OF LAW FIRM ECONOMICS for 2006 discloses that the median hourly rate for attorneys practicing in New England, the Middle Atlantic and the South Atlantic ranged from $155 to $350 depending on their years of experience. The hourly rates for those in the Ninth Decile ranged from $203 to $463. *See* Altman Weil, Inc., THE 2006 SURVEY OF LAW FIRM ECONOMICS 86 (2006). In fact, the Altman Weil Survey discloses that hourly rates in 1997 were far above the numbers used by Econometrica for 2006. *See* Altman Weil Pensa Inc., SURVEY OF LAW FIRM ECONOMICS at II-5 (1997) (noting that the average billing rate for the top decile of partners in the Northeast was $295.00 per hour in 1997). The numbers used by Econometrica seem more than anything else to be "plucked from a hat." *Peabody Coal Co. v. McCandless*, 255 F.3d 465, 470 (7th Cir. 2001).

The analysis with respect to accountants discloses similar factual errors that understate the costs of the No-Match Rule. Econometrica uses hourly rates for "outsourced" accountants of

$72.50, and an average hourly rate for both in-house and outsourced accountants of $50.51. SAR 3767. This "wage rate" number is far below the rates approved by various courts as prevailing rates for accountants. *See*, *e.g., Cobell v. Norton*, 231 F. Supp. 2d 295 (D.D.C. 2002)("the Court deems $225 to be a reasonable hourly rate of compensation for services rendered by" a certified public accountant); *In Re Am. Bridge Prods. Inc.*, No. 96-16620-JNF, Adv. P. No. 00-1142 (Mass. 2005) (approving a $200/hour rate for accountant's services); *In re Garcia*, No. 03-06041-H7 (Bankr. S.D. Cal. Nov. 22, 2004) (relying on rates for bankers, consultants, accountants and other professionals in the case to arrive at the hourly rate of $400 per hour for the trustee).

Defendants understate the cost of the rule in yet another way. They argue in the preamble that turnover or replacement costs, *i.e.*, the cost to replace an employee who is terminated or resigns, only count where the employees are actually authorized. 73 Fed. Reg. 63863 (col a). They guessed that two percent of authorized employees will not be able to resolve a no-match within the 93-day time limit and therefore, will be terminated. First, the two percent figure has no basis in fact. Second, one cannot ignore the cost to replace an employee who was properly hired based on a proper review of what the employer believed to be proper identification. If that employee must be terminated or leaves as a result of a no-match letter, the employer incurs a cost to replace that employee. Defendants, however, argue that those costs are not legitimate because the employer had no business hiring the employee. *Id.* That rewrites the laws of immigration and economics.

According to the SEIA, the number of unauthorized employees could range from 393,229 to 3,145,830. *See* SAR at 3677 and 3689. Assuming Econometrica's figure of $5,000 per employee in turnover costs, these unaccounted costs range from $14,961 to $111,685 per firm or between $1.966 billion and $15.729 billion in the aggregate, not including the additional costs of compliance, *e.g.*, legal, accounting, human resource labor, miscellaneous administrative and research, management and internal costs.

4. Defendants' Final RFA Analysis Was An Anachronism When Issued

It is axiomatic that a rule speaks as of the date it is issued. *See Ogden v. United States*, 758 F.2d. 1168, 1183 n.11 (7th Cir. 1985); *Izaak Walton League of Am. v. Marsh*, 655 F.2d 346, 362 (D.C. Cir. 1981). If circumstances change between the time a rule is proposed and the time it is finalized, the agency is required to evaluate those changes to ensure that a rule's predicate still holds factual, legal, and logical sway. *See Certified Color Mfr'g Ass'n v. Mathews*, 543 F.2d 284 (D.C. Cir. 1976) (affirming agency's decision based on changed circumstances). Here, as this court aptly noted during the scheduling conference on December 5, 2008, there has been a major change in the economy since mid-September 2008, and those changes could affect the rule's economic impact. That fact alone should have been sufficient to galvanize Defendants into reevaluating the continued propriety of their August 2008 SEIA. Defendants, however, did not do this and as a result, the No-Match Rule ignores the economic changes that occurred during September and October 2008. Those changes are particularly pertinent with respect to small entities. One of the fundamental distinctions between large and small entities highlighted by Congress when it enacted the RFA was that small entities had "limited access to capital either through retained earnings or public sale of stock." Sen. Rep. No. 878, 96th Cong., 2d Sess. 4-5 (1980). Therefore, "small concerns traditionally must borrow heavily" and "[e]ven if small businesses can afford additional debt, banks and other lenders are often reluctant to loan money for improvement purposes not related to productivity," *i.e.*, regulatory compliance. *Id*. The hallmark, however, of the recent economic crisis is that banks and lenders are not making sufficient loans to drive the economy. The various stimulus packages that Congress is now considering are supposed to address these problems. The legislation has yet to be enacted and we have no idea whether—or when-- it will be effective. In the interim, debt financing is far more difficult to obtain than it was

in August 2008. Defendants acted arbitrarily by not revising their Final RFA analysis to address these significant, once in-a-generation economic changes.

B. The Court Should Enter Summary Judgment Against Defendants for Violating the RFA

Courts usually give agencies at least one opportunity to correct deficiencies in their rulemaking. However, courts are less tolerant when the response on remand remains inadequate and contrary to law. When that occurs this Circuit has authorized District Courts to invalidate the rule without a second remand. *See Earth Island Inst. v. Hogarth,* 494 F.3d at 769 ("We have already [remanded] once, to no avail, in *Brower II*. Having again failed to complete the studies, the government's brief gives no indication that the agency wants another chance to do what Congress asked it to do."). That should occur here. Defendants have had ample opportunity and four Federal Register issuances to conduct a reasonable good-faith RFA analysis. They have not done so and the matter should therefore come to end. That is especially so given that the Defendants do not believe that their rule is truly substantive and therefore, they would suffer little to no injury.

CONCLUSION

For the reasons set forth above and in the Union Plaintiffs' memorandum filed today, Defendants' motion for summary judgment should be denied. Rather, summary judgment should be entered against Defendants. Finally, the motion to vacate the preliminary injunction also should be denied.

Respectfully submitted

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CERTIFICATE OF SERVICE

I hereby certify that on January 9, 2009, I electronically filed the foregoing Plaintiff-Intervenors' Motion for Summary Judgment, Memorandum in Support of Plaintiffs' Motion for Summary Judgment and in Opposition to Defendants' Motions for Summary Judgment and to Vacate Preliminary Injunction and Proposed Order with the Clerk of the Court using the CM/ECF system which will send notification of such filing to the e-mail addresses denoted below:

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