UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF ADMINISTRATIVE LAW JUDGES

IN THE MATTER OF

Central Kitsap School District (WA) Docket No. 11-86-I

Federal Impact Aid Proceeding

Respondent

Appearances: Christopher L. Hirst, Esq. and Laura K. Clinton, Esq. of K&L Gates LLP, Seattle, Washington, for the Central Kitsap School District (WA)

Jane A. Hess, Esq. and Jill M. Eichner, Esq., Office of General Counsel, United States Department of Education for the Assistant Secretary for Elementary and Secondary Education

Before: Judge James G. Gilbert

INITIAL DECISION

This matter is before me on cross-motions for summary judgment.[1] At issue is whether the Assistant Secretary for Elementary and Secondary Education ("Department" or "Assistant Secretary") correctly determined that the Central Kitsap School District, Kitsap County, Washington ("District" or "Respondent") is ineligible for Heavy Impact Aid (HIA) for Fiscal Year 2010 (FY2010) under the provisions of Section 8003(b)(2) of Title VIII of the Elementary and Secondary Education Act of 1965 as amended (codified at 20 U.S.C. § 7703(b)(2)). The parties submitted twenty joint exhibits and comprehensive joint stipulations of fact that are accepted into the record.

[1] I preside by designation of the Office of Personnel Management and the Department of Education under the Administrative Law Judge Loan Program, 5 U.S.C. § 3344, its implementing regulations at 5 C.F.R. § 930.208, and a *Memorandum of Understanding* between the United States Postal Service (USPS) and the Department of Education (on file at the USPS Judicial Officer Department, Office of Administrative Law Judges, 2101 Wilson Blvd., Suite 600, Arlington, VA 22201) to hear this case under the Administrative Procedure Act, 5 U.S.C. §§ 551, *et seq.* and 34 C.F.R. § 222.153. *See Order of Assignment* dated June 13, 2013. The motions at issue in this matter were filed with the Department of Education in June 2012. This matter was referred to me in May 2013.

Background

Federal impact aid "provides financial assistance to local school districts whose ability to finance public school education is adversely affected by a federal presence." *Zuni Pub. Sch. Dist. No. 89 v. Dep't of Educ.*, 550 U.S. 81, 84 (2007). "Federal aid is available to districts, for example, where a significant amount of federal land is exempt from local property taxes, or where the federal presence is responsible for an increase in school-age children (say, of armed forces personnel) whom local schools must educate." *Id.* at 84-85. In addition to basic impact aid, in certain circumstances, a local education agency (LEA) may be eligible for additional impact aid if it is determined to be "heavily impacted" under the statute. 20 U.S.C. § 7703(b)(2). Respondent qualified as a "heavily impacted" LEA beginning in FY1998 and continuing through FY2009. *Joint Stipulation*, Part A, ¶1. As a heavily impacted LEA, Respondent received between $3,000,000 and $9,000,000 annually in HIA through FY2009. *Joint Stipulation*, Part A, ¶2. The District's continued eligibility for HIA in FY2010 is before me.

Respondent's eligibility for HIA for FY2010 is determined by four criteria: (1) whether the District received financing under Section 8003(f) for FY2000; (2) whether at least 35% of District students are federally connected; (3) whether the District's per-pupil expenditures are less than average for the state or all states; and (4) whether the District's tax rate for general fund purposes is not less than 95% of the average tax rate for all districts in the state or generally comparable districts in the state. *Joint Stipulation*, Part C, ¶5. The parties stipulate that Respondent met the first three criteria. *Joint Stipulation*, Part D, ¶1.

The fourth criterion is governed by the statutory language in Section 7703(b)(2)(G).

> (G) **Determination of average tax rates for general fund purposes**
> For the purpose of determining average tax rates for general fund purposes for local educational agencies in a State under this paragraph (except under subparagraph (C)(i)(II)(bb)), the Secretary shall use either--(i) the average tax rate for general fund purposes for comparable local educational agencies, as determined by the Secretary in regulations; or (ii) the average tax rate of all the local educational agencies in the State.
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> 20 U.S.C. § 7703(b)(2)(G).[2]

To determine its eligibility under subparagraph (i), the District sought and obtained data from the Washington State Office of the Superintendent of Public Instruction (OSPI) to define its group of generally comparable LEAs and their average tax rate. *Joint Stipulation*, Part D, ¶4. For this calculation, Respondent used data from 35 comparable LEAs. *Joint Stipulation*, Part D, ¶5. In determining the average tax rate, Respondent and OSPI took the total amount of levy certified

[2] To calculate its eligibility under the program, the District used 2006 tax year data to determine that under subparagraph (ii) its tax rate of $2.0129 (per $1,000) was less than 95% of all state districts. Thus, Respondent was not eligible for HIA under subparagraph (ii) of Section 7703(b)(2)(G). *Joint Stipulation*, Part D, ¶¶2, 3. The District does not dispute its ineligibility under subparagraph (ii) in this proceeding.

for the districts in their comparable LEA subgroup, divided that figure by the total assessed value within the subgroup, and divided by 1,000, reaching a subgroup average tax rate of $2.0410 (per $1,000). *Id.* Under this formula the District's tax rate of $2.0129 was 98.6% of the average tax rate for the defined comparable LEA subgroup, and, in accordance with subparagraph (i), the District qualified for HIA for FY2010. *Id.*[3]

Although the Department initially accepted the state supplied figures, it ultimately rejected the formula utilized by the District and OSPI to determine the average tax rate. *Joint Stipulation*, Part D, ¶9; *Joint Exhibit* 18. The Department concluded that the District's use of the "weighted" formula was inconsistent with its formula, which calculates an overall average tax rate without regard to assessed valuations. Given the Assistant Secretary's history of accepting the weighted average numbers based on assessed valuations provided by Respondent in prior fiscal years, combined with the absence of a regulation that addresses a specific formula for calculating average tax rate under Section 7703(b)(2)(G), Respondent argues that the Assistant Secretary's denial of HIA for FY2010 was improper.

The Assistant Secretary, to the contrary, asserts that the formula he adopted for the FY2010 calculation is part of a longstanding policy, and to the extent that he accepted another formula from the District in prior years, he did so in error. The Assistant Secretary further argues that his interpretation of the statutory term *average tax rate* is reasonable, and as the agency charged with enforcement of the statute, his interpretation is entitled to deference. *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984).[4]

Discussion

The Assistant Secretary contends that his interpretation of the term *average tax rate* in Section 7703(b)(2)(G)(i), as reflected by the formula adopted by the Assistant Secretary in this case, is entitled to deference under *Chevron* or other authority. The District argues that, in the absence of a properly promulgated regulation, any reasonable formula put forth by it, particularly one that was accepted by the Assistant Secretary for multiple years, cannot be rejected without issuing proper regulations under the Administrative Procedure Act, which the Assistant Secretary concedes he has not done. 5 U.S.C. §§ 551, *et seq*. In other words, the District argues that if the Assistant Secretary wishes to change the rules, he must do so by giving the affected parties an

[3] In Washington State, the property tax rate for an individual district or community is determined using the simple levy process. *Affidavit of Calvin Brodie*, ¶7 (Brodie Aff.). Under this process, the tax rate is established by dividing the community's budget (certified levy) by the total assessed value within the community and dividing by 1,000. Brodie Aff. ¶8. This results in a "weighted" average tax rate taking into consideration assessed valuation differences within the various LEAs. Individual districts in Washington State do not set their own tax rates, which rise and fall along with property values. *Id.*

[4] Section 7703(b)(2)(G)(i) states "the average tax rate for general fund purposes for comparable local educational agencies, *as determined by the Secretary in regulations*." (Emphasis added). Respondent argues that the phrase *as determined by the Secretary in regulations* compels the Secretary to issue a separate set of regulations addressing the calculations for average tax rate. The Department rejects Respondent's claim that the phrase was intended by Congress to require it adopt specific regulations governing the formula for calculation of average tax rate. For reasons later discussed, I need not address this argument to resolve the matter before me.

opportunity for notice and comment before applying the average tax rate formula to potentially eligible HIA districts.

Application of Chevron Deference to the Assistant Secretary's Interpretation of the Statutory Term "Average Tax Rate"

The operative phrase *average tax rate* is undefined in both the statute and in the implementing regulations.[5] Nevertheless, if the statutory term at issue is unambiguous, no further analysis is required. *Chevron*, 467 U.S. at 842-43 (1984). The Assistant Secretary argues that the term is clear, and that *average tax rate* means a simple average calculation. Under the Assistant Secretary's interpretation, the term *average tax rate* means the tax rates in the applicable category, added together, and divided by the number of districts composing the particular category. The District argues that the term *average tax rate* is ambiguous, and that its interpretation, in the absence of regulatory clarification, leaves the term open to numerous reasonable interpretations, including the one proffered by the District based on Washington's system of real property taxation.

Under *Chevron*, I must first determine whether Congress's intent is so clear and unambiguous that there is no further need for analysis. *Id*. I begin, as always, by looking to the plain language of the statute. *U.S. v. Ron Pair Enter., Inc.*, 489 U.S. 235, 241 (1989)(statutory interpretation "begins where all such inquiries must begin: with the language of the statute itself."). The parties do not dispute that the "tax rate" referenced in Section 7703(b)(2)(G)(i) represents real property tax, as that tax is generally the funding mechanism for most school districts in the United States, and is the tax that is the subject of various parts of Section 7703. Thus, the language suggests the calculation is for the average real property tax rate for the comparable LEAs. Beyond that basic assumption, the term *average tax rate* is susceptible to multiple meanings and presumably multiple calculations or formulas depending upon its particular application, including how an individual state calculates its property tax rates. *See supra* note 3.

Taxation is among the most heavily regulated areas of both state and federal law, and the complications involved in computing a tax rate keep the most qualified tax attorneys well employed. *See, e.g.*, Title 26, *Code of Federal Regulations*.[6] For example, the term *average tax rate* is often defined as "total taxes divided by taxable income." Campbell R. Harvey, *Yahoo Small Business Advisor*, http://smallbusiness.yahoo.com/advisor/business-tools/dictionary/term-average-tax-rate.html. The term *average tax rate* is also often discussed in the context of marginal tax rate. "Misunderstandings about two different types of tax rates often create confusion in discussions about taxes. A taxpayer's average tax rate (or effective tax rate) is the share of income that he or she pays in taxes. By contrast, a taxpayer's marginal tax rate is the tax rate imposed on his or her last dollar of income." *Policy Basics: Marginal and Average Tax*

[5] The implementing regulations relied upon by the Secretary are found at 34 C.F.R. §§ 222.39-222.41. They address "comparable LEAs" but do not define the term *average tax rate*.

[6] CCH publications, a comprehensive reporter of tax related information, reports that its original *Standard Federal Tax Reporter* published in 1913 was 400 pages, but that its 2012 version now numbered 73,608 pages. *See* http://www.cch.com/wbot2012/020TaxCode.asp.

Rates, Ctr. on Budget & Pol'y Policies (updated April 15, 2013) http://www.cbpp.org/cms/?fa=view&id=3764. *Black's Law Dictionary* defines the term *average tax rate* as "[a] taxpayer's tax liability divided by the amount of taxable income." *Black's Law Dictionary* 1475 (7th ed. 1999).

Further, the term *average tax rate* appears to be most frequently discussed in the context of income taxation. Yet, in the domain of real property taxation, *average tax rate* does not seem to be a frequently utilized term, and the commonly understood definitions in the field of income taxation discussed above have little to do with the concept of determining the *average tax rate* contemplated by Section 7703(b)(2)(G)(i). I could not find, and the parties did not cite, any authority that defines the term *average tax rate* in the context of real property taxation. Accordingly, the term demands further clarification within the meaning of Section 7703(b)(2)(G)(i) at least as it is used in the context of real property taxation. Thus, I cannot conclude, as the Assistant Secretary has done, that the term is unambiguous as applied in this statute.[7]

Having determined that the statutory term *average tax rate* is ambiguous; the second step of *Chevron* analysis requires me to determine whether "it appears that Congress delegated authority to the agency generally to make rules carrying the force of law, and that the agency interpretation claiming deference was promulgated in the exercise of that authority." *United States v. Mead Corp.*, 533 U.S. 218, 226-27 (2001). In a situation where the agency's interpretation is promulgated carrying the "force of law" *Chevron* is applied at the highest level of deference, in that the agency's exercise of the authority will be granted deference except in the most unusual circumstances. *Auer v. Robbins*, 519 U.S. 452, 457 (1997)("we must sustain the Secretary's approach so long as it is 'based on a permissible construction of the statute.'").

The Assistant Secretary takes the position that Section 7703(b)(2)(G)(i) does not require the agency to promulgate any rule or regulation defining the statutory term *average tax rate* and he has not done so.[8] *Chevron* contemplates that the agency has issued an interpretation of the statutory term in the form of a regulation or other means carrying the force of law by virtue of the authority delegated to it by Congress. Here, this is plainly not the case.

The current situation seems to align more closely with *Gonzales v. Oregon*, 546 U.S. 243 (2006), in which the Supreme Court determined that merely repeating statutory language in a

[7] The Secretary argues that the term "average" is well known, and when combined with the phrase "tax rate" the meaning of the phrase becomes clear. However, even the term "average" can take on several meanings depending upon the context in which it is used. Courts have struggled to determine how to define the term "average" when used as a modifier in a phrase. *See, e.g., United States v. Amoco Oil Co.*, 580 F. Supp. 1042, 1049 (W.D. Mo. 1984)("the term 'daily average' is, in the abstract, probably inherently ambiguous"); *Transitional Hosp. Corp. of Louisiana, Inc. v. Shalala*, 222 F.3d 1019, 1028 (D.C. Cir. 2000)(phrase "has an average inpatient length of stay (as determined by the Secretary) of greater than 25 days" is ambiguous); *Optopics Labs. Corp. v. Nicholas*, CIV. A. 96-8169, 1997 WL 256944 (E.D. Pa. May 13, 1997)(phrase "valued at the average of the high and low prices on NASDAQ of Nutramax shares on the date such recovery is actually received by the Surviving Corporation" is ambiguous); *Bosshard Bogs, LLP v. Cliffstar Corp.*, 02-C-0034-C, 2002 WL 32350544 (W.D. Wis. Oct. 23, 2002)(phrase "Ocean Spray's average pool price" is ambiguous.).

[8] See *supra* note 4.

regulation is not an interpretation of that language and is not entitled to deference. The Assistant Secretary does not define *average tax rate* in any rule, regulation, interpretive letter, or other publication. Rather, the Department repeats the phrase *average tax rate* in several areas of its regulations, but never explains its interpretation of the term. *See* 34 C.F.R. §§ 222.62, 222.70, 222.72, 222.73. "Simply put, the existence of a parroting regulation does not change the fact that the question here is not the meaning of the regulation but the meaning of the statute. An agency does not acquire special authority to interpret its own words when, instead of using its expertise and experience to formulate a regulation, it has elected merely to paraphrase the statutory language." *Gonzales v. Oregon*, 546 U.S. at 257.

Thus, without the benefit of a regulation defining the statutory term, the Department fails step two of *Chevron*, as it did not adopt its current interpretation as the result of the "exercise of authority" granted to it by Congress in a manner "carrying the force of law." *Mead Corp.*, 533 U.S. at 226-27. Accordingly, I find the Assistant Secretary's interpretation at issue is not entitled to *Chevron* deference.

B. Application of Skidmore Deference to the Assistant Secretary's Interpretation of the Statutory Term "Average Tax Rate"

Failure to be accorded the deference contemplated by *Chevron* invites a separate analysis under *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944), and its progeny.[9] *Skidmore* established a lesser level of deference than the Court later contemplated in *Chevron*. *Skidmore* places the level of deference entitled to an agency's interpretation on factors such as "the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking power to control." *Id.* at 140. Promulgation of a regulation or other formal rulemaking is less critical under *Skidmore* analysis.

On this record, it is difficult to establish the "thoroughness evident" in the agency's consideration of the term *average tax rate*. I note that the July 29, 2011 letter that operates as the denial of HIA for FY2010 certainly reflects a good faith effort by the agency to find a path toward HIA funding within the narrow confines of its interpretation of *average tax rate*. *Joint Exhibit* 18. However, the only evidence in the record pertaining to the adoption of that interpretation having been thoroughly considered is found in the *Affidavit of Catherine Schagh* (Schagh Aff.). Ms. Schagh states that "[w]e chose this method of calculating 'average tax rate for general fund purposes for comparable [LEAs]' – adding the rates and dividing by the number of districts – because it is the common-sense meaning of average." Schagh Aff. ¶34. She further states that the "[p]rogram never considered publishing a regulation to define 'average tax rate' because it is a commonly understood term." Id. at ¶35. Given that the Department freely admits

[9] Although *Skidmore* predates *Chevron*, subsequent case law suggests that when an agency interpretation is denied *Chevron* deference, a court must exercise a more detailed analysis under the lesser deference standards applied in *Skidmore* to determine if the interpretation is due any deference at all. *See, e.g., Christensen v. Harris County*, 529 U.S. 576, 587 (2000)(denying *Chevron* deference due to lack of regulation but recognizing "[i]nterpretations contained in formats such as opinion letters are 'entitled to respect' under our decision in *Skidmore v. Swift & Co.*, but only to the extent that those interpretations have the 'power to persuade'")(internal citations omitted)*; Mead Corp.*, 533 U.S. 218 (tariff classification ruling was not entitled to *Chevron* deference, but *Skidmore* applied).

that it never considered any other interpretation or formula, I can hardly conclude that its analysis to reach this interpretation was thorough.

Next I look to the validity of the reasoning behind the agency's interpretation. Here, the simple formula adopted by the Department for calculation of average tax rate is based on the Department's fundamental misunderstanding that all persons would intuitively understand that the ambiguous statutory term *average tax rate* must, by necessity, be calculated by its formula. The Department's insistence on the obviousness of its interpretation leads to its failure to consider the matter in more serious and thoughtful terms that might have revealed the ambiguity present had the Department pursued a more formal regulatory process.

I next review whether the Assistant Secretary's interpretation is consistent with past interpretations of the same term. Once again, I am confronted with the Assistant Secretary's insistence that this "longstanding policy" should be patently obvious from the undefined statutory term *average tax rate*. Given this insistence, based on my review of the record, the longstanding policy interpretation so intensely defended here was inexplicably of little interest to the Assistant Secretary prior to FY2010. By his own admission, the Assistant Secretary never bothered to check an individual state's calculation of average tax rate for anything other than to "ascertain if in fact the figure represents the average tax rate for general fund purposes, i.e., is consistent with the statutory definition of current expenditures in section 8103 of ESEA and does not include any significant changes[.]" *Id.* at ¶24. The Assistant Secretary admits that during the years leading up to FY2010, he would "typically accept" the state's calculation of average tax rate "without checking the math." *Id.* at ¶33. In doing so, the Assistant Secretary, by longstanding practice if not by policy, adopted the potentially varying formulas the states may have used in reaching their calculation for average tax rate, including Respondent's weighted average formula.

The District could not have known prior to FY2010 that it was "improperly" calculating average tax rate because the Assistant Secretary issued no guidance to inform the District, or any other applicant, of its internal interpretation.[10] Compounding this problem of application of an undisclosed internal interpretation is the fact that the Assistant Secretary failed to "check the math" of any district applying for HIA prior to FY2010. The Assistant Secretary's explanation for this lack of curiosity is that he cannot comprehend how anyone could possibly interpret the term *average tax rate* in any other manner than the Department's current interpretation; therefore further inquiry to the individual states was unnecessary. This is apparently the same reason why the Assistant Secretary failed to define the term *average tax rate* in a properly issued regulation under the Administrative Procedure Act (APA), or by some other means available to inform potential applicants for HIA.[11]

[10] The Secretary acknowledged that this longstanding interpretation appears nowhere in written form prior to the July 21, 2011 letter to the District. Schagh Aff. ¶36. Thus, there exist no rulings, interpretative letters, or other indicia of its existence prior to FY2010.

[11] The Secretary's argument that it did not substantively change regulations governing "comparable LEAs" because it was ordered by Congress not to do so has nothing to do with the lack of a regulatory definition for the term *average tax rate* under Section 7703(b)(2)(G)(i).

So now I must analyze whether the Assistant Secretary's interpretation, deficient in the foregoing elements, still maintains the "power to persuade, if lacking power to control." *Skidmore*, 323 U.S. at 140. This factor suggests that the power to persuade is inherent in the agency's ability to defend the correctness of its interpretation. Yet, when an agency fails to promulgate its interpretation through a formal rulemaking, it leaves behind little evidence of its own justifications for its interpretation. There is nothing in the record, absent the *Affidavit of Catherine Schagh*, that offers any explanation from the Assistant Secretary why his interpretation is more persuasive than the District's interpretation. The explanation provided is, at best, the result of circular reasoning, and lacks the power to persuade this Judge. Lamenting a similar lack of formal rulemaking, the Fourth Circuit found that the Department of Labor's (DOL) inclusion of Christmas tree farming as "forestry" was not entitled to deference because it lacked the power to persuade. *U.S. Dep't of Labor v. N. Carolina Growers Ass'n*, 377 F.3d 345, 354 (4th Cir. 2004)("Without an explanation of how the DOL came to its conclusion, it is impossible for us to be persuaded by the DOL's reasoning.") Similarly, I cannot conclude that the Assistant Secretary's interpretation of the statutory term *average tax rate* is persuasive in the absence of an understanding of the depth and breadth of his considered reasoning behind his interpretation.

For the reasons discussed, the Assistant Secretary's interpretation of the term *average tax rate* is not entitled to deference. As I find that *Skidmore* does not compel me to defer to the Assistant Secretary's internal interpretation of the statutory term *average tax rate*, I am left to decide whether the Assistant Secretary's decision to deny Respondent HIA in FY2010 is defensible on any other grounds.

C. Was the Assistant Secretary's Adoption of the Average Tax Rate Formula an Interpretive Rule under the APA?

It is certainly permissible for an agency charged with administration of a statute to change its position on a matter of statutory interpretation. *See Good Samaritan Hosp. v. Shalala*, 508 U.S. 402, 417 (1993)("The Secretary is not estopped from changing a view she believes to have been grounded upon a mistaken legal interpretation."). If the change is deemed "interpretive," prior notice or opportunity for comment is not required. 5 U.S.C. § 553(b)(3)(A).[12] The basis for this "interpretive rule" exception is that statutory interpretation is part of an agency's function, and a requirement that it proceed with formal rulemaking in every instance is an unnecessary roadblock to the efficiency of the agency. *Am. Hosp. Ass'n v. Bowen*, 834 F.2d 1037, 1045 (D.C. Cir. 1987)("[t]he function of § 553's first exemption, that for 'interpretive rules,' is to allow agencies to explain ambiguous terms in legislative enactments without having to undertake cumbersome proceedings.").[13] In the end, however, this case is less

[12] "Except when notice or hearing is required by statute, this subsection does not apply--(A) to *interpretative rules*, general statements of policy, or rules of agency organization, procedure, or practice; or (B) when the agency for good cause finds (and incorporates the finding and a brief statement of reasons therefor in the rules issued) that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest." 5 U.S.C. § 553(b)(emphasis added).

[13] Under the APA, the term rule is defined as "the whole or a part of an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy or describing the

about an agency's change in its interpretation of a statutory term than it is about an agency's change in its longstanding practice of accepting state-supplied average tax rate calculations.

Here, the practice at issue -- the acceptance of state calculated average tax rates -- was reversed in the context of a denial of HIA funding to the District as the result of the Assistant Secretary's adoption of a universal formula based on his interpretation of the statutory term *average tax rate*. The issue is not whether the Assistant Secretary has the authority to define the term *average tax rate*, or to adopt an appropriate formula for its calculation. Neither matter is in dispute here. The issue raised in this case is the procedure the Assistant Secretary used to reverse his longstanding practice. The Assistant Secretary reversed his longstanding practice, and adopted a formula for the calculation of *average tax rate*, in a decision to deny HIA funding to the District without the benefit of notice and comment from affected parties. Whether such an exercise of agency authority was proper requires an analysis of Section 553 of the APA. 5 U.S.C. § 553.

The general rule is that an agency's rulemaking must follow the notice and comment procedures set forth in the APA. *Miami-Dade Cnty. v. EPA*, 529 F.3d 1049, 1059 (11th Cir. 2008)(the purpose of notice and comment under the APA is "to allow an agency to reconsider, and sometimes change, its proposal based on the comments of affected persons." (quoting *Ass'n of Battery Recyclers v. EPA*, 208 F.3d 1047, 1058 (D.C.Cir.2000))). Yet, an agency's interpretation of a statute that it is charged with enforcement is generally determined to fall within the "interpretive rule" exception of Section 553 of the APA. 5 U.S.C. § 553(b)(3)(A). To uphold the importance of the APA's notice and comment requirements, the "interpretive rule" exception is narrowly construed. *Am. Hosp. Ass'n v. Bowen*, 834 F.2d at 1044 ("Congress intended the exceptions to § 553's notice and comment requirements to be narrow ones."); *see also, UPMC Mercy v. Sebelius*, 793 F. Supp. 2d 62, 69 (D.D.C. 2011). Nevertheless, if the decision of the Assistant Secretary is simply an interpretive rule, then the Assistant Secretary was not required to follow the notice and comment procedures of the APA. Therefore, I must determine if the "interpretive rule" exception applies. Proper application of the "interpretive rule" exception under Section 553 has been the subject of considerable litigation and academic debate.

Prior to the Supreme Court's ruling in *Vermont Yankee*, the "substantial impact" test was the predominant test used to decide whether an agency's action might fall under the "interpretive rule" exception. *Vermont Yankee Nuclear Power Corp. v. Natural Res. Def. Council, Inc.*, 435 U.S. 519, 543 (1978)("Absent constitutional constraints or extremely compelling circumstances 'the 'administrative agencies' should be free to fashion their own rules of procedure and to pursue methods of inquiry capable of permitting them to discharge their multitudinous duties.'")(citations omitted). After *Vermont Yankee*, several circuits abandoned the substantial impact test, and have since attempted to draw a brighter line for determining when the exception applies, with varying degrees of success. *Friedrich v. Sec'y of Health & Human Servs.*, 894 F.2d

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organization, procedure, or practice requirements of an agency and includes the approval or prescription for the future of rates, wages, corporate or financial structures or reorganizations thereof, prices, facilities, appliances, services or allowances therefor or of valuations, costs, or accounting, or practices bearing on any of the foregoing[.]" 5 U.S.C. § 551(4).

829, 834 (6th Cir. 1990)("[w]e have discovered no bright line that separates the two types of rules"); *White v. Bowen*, 636 F. Supp. 1235, 1241 (S.D.N.Y. 1986), *aff'd*, 835 F.2d 974 (2d Cir. 1987)("[i]n drawing the line between substantive and interpretative rules, the Second Circuit no longer looks to the impact of a rule, . . . but focuses instead upon the change in law effected by a rule"); *Donovan v. Red Star Marine Services, Inc.*, 739 F.2d 774, 783 (2d Cir.1984)("[o]nly rules that do not change 'existing rights and obligations' are considered interpretative"); *Alcaraz v. Block*, 746 F.2d 593, 613 (9th Cir. 1984)("[t]hus, we have rejected the argument that, for the purposes of imposing notice and comment requirements on the agency for a particular rule, we look to the 'substantial impact' of the rule."). Not surprisingly, and not unlike agency deference discussed *supra*, (and because the law, like nature, abhors a vacuum) in step a host of theories and tests that various courts apply to make this determination.

Yet, since *Vermont Yankee*, there has been little activity at the Supreme Court level to assist lower courts with their efforts to define the line between substantive and interpretive. I have reviewed numerous cases from various circuits, and can only conclude that a definitive test to determine whether an agency's action falls within the interpretive rule exception does not exist. In my opinion, the better-reasoned approaches balance the agencies' need to freely interpret (and reinterpret) their respective administering statute free from judicial interference, with the need of the affected parties to know their substantive rights and the rules they must follow to comply with the agencies' various directives. Where an agency fails to properly inform the affected parties of significant shifts in agency policy, these courts tend to be stricter in their application of the "interpretive rule" exception. In such cases, the courts are wary of an agency evading the formal procedures of the APA by issuing "interpretations" that are best addressed in a regulatory process. *See Appalachian Power Co. v. EPA*, 208 F.3d 1015, 1024 (D.C.Cir. 2000)("An agency may not escape ... notice and comment requirements ... by labeling a major substantive legal addition to a rule a mere interpretation."); *C.F. Communications Corp. v. FCC*, 128 F.3d 735, 739 (D.C.Cir. 1997)(holding that the FCC "may not bypass [the APA's notice-and-comment] procedure by rewriting its rules under the rubric of 'interpretation'")(citations omitted). These thoughtful opinions guide my judgment in this matter.

A number of courts have found that an interpretation resulting in a departure from a longstanding practice or policy will trigger the notice and comment requirements of the APA. *Ferguson v. Ashcroft*, 248 F. Supp. 2d 547, 564 (M.D. La. 2003)("although agency 'interpretations' are not typically subject to notice and comment procedures, when an interpretation departs from a longstanding agency practice, it too must be promulgated pursuant to the general APA notice and comment procedures."); *Shell Offshore Inc. v. Babbitt*, 238 F.3d 622, 630 (5th Cir. 2001)("If a new agency policy represents a significant departure from long established and consistent practice that substantially affects the regulated industry, the new policy is a new substantive rule and the agency is obliged, under the APA, to submit the change for notice and comment"); *see also*, *Nat'l Retired Teachers Ass'n v. U. S. Postal Serv.*, 430 F. Supp. 141, 148 (D.D.C. 1977) *aff'd*, 593 F.2d 1360 (D.C.Cir. 1979)("if the rule constitutes a change in prior agency position and has a substantial impact on the rights and obligations of [the parties], the rule would be invalid for failure to comply with the notice and comment requirements.").

Thus, when an agency adopts an interpretation that impacts affected parties in a substantive manner, or represents a change in agency practice or policy, or signifies a substantive change in an existing regulation, or results in a major substantive legal addition to an existing regulation, the "interpretation" may be deemed to be a substantive rule requiring compliance with the APA. *See, e.g., Shalala v. Guernsey Mem'l Hosp.*, 514 U.S. 87, 100 (1995)(when interpretation effects "a substantive change in the regulation" notice and comment are required)(citation omitted); *Sprint Corp. v. FCC*, 315 F.3d 369, 374 (D.C.Cir. 2003)("new rules that work substantive changes" to existing regulations require notice and comment); *Appalachian Power Co.*, 208 F.3d at 1024 (new rules that constitute "major substantive legal addition[s]" to a regulation require notice and comment); *American Mining Cong. v. Mine Safety & Health Admin.*, 995 F.2d 1106, 1112 (D.C.Cir. 1993)(a rule that "effectively amends a prior legislative rule" is "a legislative, not an interpretive rule" requiring Section 553 compliance).

The Assistant Secretary's departure from his longstanding practice to accept state calculated average tax rates resulted in a denial of FY2010 HIA funding to the District. Had there been no deviation from this longstanding practice, the District would have qualified for HIA funding for FY2010. It is hard to argue that such a departure from the Assistant Secretary's longstanding practice was not substantive. Certainly, the District's unanticipated loss of HIA funding for FY2010 was significant. I therefore conclude that the Department's decision to abandon its longstanding practice to accept state calculated average tax rates for the purposes of determining eligibility under Section 7703(b)(2)(G)(i), and the concurrent adoption of its interpretation of the term *average tax rate* reflected in the July 29, 2011 letter, constituted a substantive change to longstanding agency practice, and the "interpretive rule" exception under Section 553 does not apply. Thus, I find the Assistant Secretary's decision to adopt a universal formula for the calculation of average tax rates under Section 7703(b)(2)(G)(i) triggered the need for the Assistant Secretary to comply with the notice and comment provisions of Section 553. The Assistant Secretary's failure to have done so in this case violates 5 U.S.C. § 553.[14] For these reasons, the Assistant Secretary's denial of HIA for FY2010 to the Central Kitsap School District was improper.

Conclusion

The Assistant Secretary's *Motion for Summary Judgment* is **DENIED** and Respondent *Central Kitsap School District's Motion for Summary Judgment* is **GRANTED**.

[14] Having determined that the Secretary's interpretation is not entitled to deference, I decide this case solely on the grounds that the Secretary's failure to follow the requirements of 5 U.S.C. § 553 renders the denial of FY2010 HIA funding to the District invalid. I further note that even if the Secretary's interpretation met traditional deference standards, no deference is afforded an interpretation promulgated in violation of the APA. *Montefiore Med. Ctr. v. Leavitt*, 578 F. Supp. 2d 129, 133 (D.D.C. 2008)("The agency's action will not be accorded deference if it 'violates the APA because it constitutes a change in the Secretary's definitive interpretation made without following the required notice-and-comment procedures.'" (quoting *Mercy Med. Skilled Nursing Facility v. Thompson*, 2004 WL 3541332, at *2 (D.D.C. May 14, 2004))).

ORDER

The letter dated July 29, 2011, from the Director, Impact Aid Programs to the Executive Director of Business Operations, Central Kitsap School District informing the District that the FY2010 high impact aid payment is made pursuant to the hold harmless provisions of Section 8003(b)(2) is **VACATED**.

The Decision of the Assistant Secretary for Elementary and Secondary Education denying high impact aid to the Central Kitsap School District pursuant to 20 U.S.C. § 7703(b)(2)(G)(i) for FY2010 is **REVERSED**.

IT IS SO ORDERED.

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James G. Gilbert
Chief Administrative Law Judge
United States Postal Service

Dated: November 15, 2013