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Appeals Court Hears Arguments in Greenhouse Gas Cases

By James Holtkamp

On February 28 and 29, the District of Columbia Circuit Court of Appeals heard oral arguments in four consolidated challenges to EPA's greenhouse gas rulemaking. The EPA issued the various rulemaking actions in the wake of the decision of the United States Supreme Court in *Massachusetts v. EPA*, 549 U.S. 497 (2007), in which the Court ruled that greenhouse gases are a "pollutant" under the Clean Air Act and that section 202(a) of the CAA therefore requires EPA to determine whether GHGs from vehicles may pose an endangerment to public health and public welfare.

Notwithstanding the dozens, if not hundreds, of commentaries on the arguments (including this one), we will only know for sure how the court will rule after the court issues its decision. However, there are some important things that can be gleaned from the argument.

First, the *Massachusetts* decision is clearly going to be considered broadly by the courts, and a party who argues that its scope is limited has a fairly stiff burden to demonstrate that, for example, the decision only supports regulation of mobile source GHG emissions.

Secondly, the Clean Air Act is a highly complex and often internally inconsistent statute. As noted by the Second Circuit in a Clean Air Act case:

> With these considerations in mind we turn to the specific provisions of the statute-provisions, we might add, whose myriad complexity reminds us of Learned Hand's description of the Internal Revenue Code. The words of that act, he declared "tend to dance before [one's] eyes in a meaningless procession: cross-reference to cross-reference, exception upon exception-couched in abstract terms that offer no handle to seize hold of-leav[ing] only a confused sense of some vitally important, but successfully concealed purport ..."

State of Connecticut v. EPA 696 F.2d 147, 155 (2d Cir. 1982)

And that was before the 1990 Clean Air Act Amendments...

Rulemakings at Issue

On December 15, 2009, EPA published its "Endangerment Finding" in which it concluded that "six greenhouse gases taken in combination endanger both the public health and the public welfare of current and future generations." 74 Fed. Reg. 66496. The six greenhouse gases ("GHGs") addressed by the Endangerment Finding are carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons and sulfur hexafluoride. The primary scientific basis for the Endangerment Finding consists of the assessments by the U.S. Global Climate Research Program, the Intergovernmental Panel on Climate Change and the National Research Council. 74 Fed. Reg. at 66497.

The Endangerment Finding led to standards governing the emissions of GHGs from motor vehicles (the "Tailpipe Rule") issued jointly by EPA and the National Highway Traffic Administration. 75 Fed. Reg. 25324 (May 7, 2010).

Under an interpretation of the Clean Air Act set forth in a memorandum from Administrator Steven Johnson of the EPA on December 18, 2008 (the "Timing Rule"), the promulgation the Tailpipe Rule made GHGs (and CO2 in particular) "regulated pollutants" under the CAA, thereby triggering regulation under the New Source Review/Prevention of Significant Deterioration ("PSD"), Title V Operating Permit, and New Source Performance Standards provisions of the CAA, among others. According to the Timing Rule, as of January 2, 2011, the effective date of the Tailpipe Rule, GHGS become regulated uunder the other parts of the Clean Air Act.

The statutory thresholds for triggering major source PSD review are 100 tons per year ("tpy") of a regulated pollutant for proposed new sources within a category listed in the CAA, 250 tpy for a proposed new source not within a listed category, or a "significant" emissions increase resulting from a modification of an existing major source. Therefore, the Timing Rule would have swept into PSD review approximately 6 million sources of GHGs, including apartment complexes, office buildings, hospitals, schools and even large restaurants using the 100/250 tpy threshold in the statute.

As a result, on June 3, 2010, EPA promulgated the PSD Tailoring Rule, in which it set the thresholds for major source PSD review at 100,000 tpy of CO2 equivalent GHGs for new sources and an increase of 75,000 tpy of CO2e for modifications of existing sources. 75 Fed. Reg. 31514 (June 3, 2010). EPA cited the doctrines of "absurd results" and "administrative necessity" in setting thresholds for GHGs higher than those in the statute. EPA also indicated that it would be implementing PSD review for GHG emissions in phases or steps. Step 1 applied to new sources or modifications of existing sources between January 2, 2011 (the effective date of the GHG tailpipe rule) and July 1, 2011, and applied only to sources which would otherwise be major sources or modifications based on emissions other than GHGs and which had a potential to emit GHGs of

100,000 tpy or more of CO2e. Step 2 commenced July 1, 2011, and applies to any new source or modification of an existing source that commences construction after that date with a potential to emit of 100,000 tpy of CO2e for a new source or 75,000 tpy of CO2e for a modification.

The Arguments

Each of these rulemakings was challenged in the D.C. Circuit Court of Appeals, and the Court consolidated the four sets of challenges into one case. There are dozens of petitioners in the consolidated cases, led by the Coalition for Responsible Regulation, a client of Holland & Hart, which has taken a lead role in contesting the Endangerment Finding and the Tailoring Rule.

The cases have been briefed, and oral arguments were held in the D.C. Circuit on February 28 and 29. Eighteen lawyers presented arguments before a panel of three judges, Sentelle, Tatel an Rogers. The court heard the arguments on each of the four sets of challenges, beginning with the Endangerment Finding and the Tailpipe Rule on the 28th, and the Timing Rule and the Tailoriing Rule on the 29th. The line to get into the hearing room began to form the night before, and the proceedings were piped into other courtrooms in the building. There were dozens of lawyers representing the various parties in the courtroom.

The first lawyer to present arguments on the first day was Patrick Day, a partner at Holland & Hart, who spoke to the Endangerment Finding on behalf of the Coalition for Responsible Regulation. Mr. Day's arguments centered on the EPA's failure to consider the policy consequences of the Endangerment Finding. Mr. Day pointed out that in issuing the Tailpipe Rule, EPA did not address whether it will in fact reduce the risks that EPA determined to be present in the Endangerment Finding. Mr. Day fielded a number of questions from the court regarding the scope of the Massachusetts holding. As Mr. Day pointed out, the Supreme Court held that EPA was required to determine whether GHGs from mobile sources endangers health or welfare and that the Court did not require that EPA make a finding that there is in fact such endangerment.

The other lawyers for the petitioners who followed Mr. Day addressed the uncertainty in the record underlying the Endangerment Finding and EPA's failure to consider adaptation in making the Endangerment Finding.

The attorneys for EPA and state intervenors supporting EPA argued that the Endangerment Finding was based on peer-reviewed science and that EPA's role is not to be the "factfinder" but rather to make a judgment on the basis of the available science. Judge Sentelle aggressively questioned EPA as to why the Endangerment Finding addresses a suite of six GHGs when only four of them are emitted by mobile sources. The government responded that all six GHGs share common characteristics, a response that did not seem to satisfy Judge Sentelle..

The arguments then moved to the Tailpipe Rule. Counsel for a group of petitioners including the National Mining Association, the Farm Bureau and Peabody Coal Company argued that the Tailpipe Rule is unlawful because

of EPA's failure to consider the effect of issuing the Tailpipe Rule on major stationary sources and EPA's failure to tie the Endangerment Finding to the Tailpipe Rule. The government, supported by the State of California and the auto manufacturers, defended the rule, arguing that the Tailpipe Standards stand on their own and that the petitioners did not have standing because, among other things, they are not mobile source owners or manufacturers.

The second day was devoted to arguments on the Timing and Tailoring Rules. The Solicitor General of the State of Texas was first to argue, and was immediately met with a barrage of questions from the panel regarding the State's standing to bring a challenge to the Rules.

He was followed by industry counsel, who argued that the Tailoring Rule was not authorized by the Clean Air Act, and that the Timing Rule was based on a historical misinterpretation of the Clean Air Act. The *Massachusetts* decision only applies to mobile source emissions, and to impose a "one size fits all" requirement to regulate GHGs under all of the Clean Air programs simply because a GHG standard was set for mobile sources is not consistent with the differing purposes of each of the Act's various programs, including the PSD permitting requirements. In addition, the "absurd results" doctrine was applied prematurely by EPA, given that EPA could have (and should have) gone through the steps required by the Act before subjecting GHGs to regulation under the PSD permitting program, i.e., designating the pollutant as a "criteria pollutant," establishing a national ambient air quality standard for that pollutant, determining which areas are not in attainment with that standard, and then subjecting it to the permitting scheme designed to assure compliance with the ambient standard.

The Government responded that the agency indeed has broad latitude under interpretations of the Act going back decades, most notably in the D.C. Circuit's 1979 decision in *Alabama Power v. Costle*, 606 F.2d 1068 (D.C.Cir. 1979). That case addressed the validity of EPA's 1978 PSD regulations and made several key holdings that form the basis for current regulation and guidance by EPA on major source permitting.

A decision is expected in the next few months, and however it comes out, will most likely be the subject of one or more petitions for certiorari to the U.S. Supreme Court.

New Mexico Repeals Carbon Emissions Regulations

By Jeffrey Kendall, Santa Fe Law Clerk and Adam Rankin

As part of a significant change in New Mexico state policy under Governor Susana Martinez, the New Mexico Environmental Improvement Board voted unanimously on February 6 to repeal three regulations aimed at reducing greenhouse gas emissions that had been in effect since January 2011.[1] On March 16, the Board also repealed New Mexico's Greenhouse Gas Reduction Rule, which imposed emission reduction requirements for

facilities with carbon dioxide emissions in excess of 25,000 metric tons per year.[2]

Petitioners for the repeals included parties from the electric utilities and oil and gas industries, along with the City of Farmington.[3] The regulations repealed by the Board in February, included the Cap and Trade Rule[4], the Reporting Rule[5] , and the Verification Rule[6]. The objective of the Cap and Trade Rule was to establish requirements for participation in a greenhouse gas cap-and-trade market.[7] The Verification Rule and the Reporting Rule were adopted to support the Cap and Trade Rule by establishing uniform mandatory reporting of greenhouse gas emissions[8].

The Greenhouse Gas Reduction Rule would have required electric utilities and oil and gas developers to curb carbon dioxide emissions by 3 percent per year beginning in 2013 and had targeted a 25 percent reduction in emissions below 1990 levels by 2020[9]. The Cap and Trade Rule would have established an initial emissions cap, then would have required an effective annual cap reduction of 1.5 percent for the first year, and 2 percent per year for the following seven years[10].

The Board's primary motivation for repealing the rules was the disintegration of the Western Climate Initiative, which had served as the impetus for adopting the greenhouse gas regulations under Governor Bill Richardson's administration. Seven western states and four Canadian provinces formed the Western Climate Initiative with the objective of creating and cooperating in a regional cap-and-trade program.[11] By early 2012, however, only California and New Mexico remained in the initiative, and Quebec was the only Canadian Province scheduled to implement its program.[12] The original concept of a robust western regional cap-and-trade program supporting the carbon regulations was no longer a realistic prospect, and the lack of solidarity among the states and provinces comprising the initiative was a major consideration in the Board's decision to repeal the rules.[13]

The Board stated a number of additional reasons for repealing the rules: (1) the fact that the rules would have no-effect on climate change; (2) the potential for increased costs to New Mexico residents and commercial customers from increased electricity rates, lost income, lost jobs and lost revenues to local governments; (3) general disadvantages to New Mexico businesses competing with states without similar regulations; (4) the lack of available carbon dioxide-reduction technologies; (5) the change in policy position by the New Mexico Environment Department, which originally proposed the Cap and Trade Rule under Governor Richardson, before opposing it under the Governor Martinez.[14]

Counsel at the New Mexico Environment Department anticipate that environmental groups supporting the rules will likely appeal.[15] New Energy Economy, for example, has publicly stated that it intends to appeal the Board's decision to repeal the rules.[16] As of the time this update was written, however, no appeals had been filed.

[1]20.2.350 NMAC; 20.2.300 NMAC; 20.2.301 NMAC; http://www.nmenv.state.nm.us/eib/. (The repeal of Parts 350, 300, and 301 were filed with the State Records Center on Feb. 13, 2012.).
[2]20.2.100.6 and 7(M) NMAC. (As of the writing of this update, Part 100 had not been filed with the State Records Center.).
[3]EIB Order and Statement of Reasons for Repeal of 20.2.350 NMAC. No. EIB 11-15(R). Page 1. http://www.nmenv.state.nm.us/eib/documents/EIB11-15R-SOR.pdf.
[4]20.2.350 NMAC.
[5]20.2.300 NMAC.
[6]20.2.301 NMAC.
[7]20.2.350.6 NMAC.
[8]EIB Order and Statement of Reasons for Repeal of 10.2.300 and 20.2.301 NMAC. No. EIB 11-17(R). Page 9, Paragraph 8.
[9]20.2.100.8, 9(B) and 10(C) NMAC.
[10]20.2.350.11 NMAC.
[11]EIB Order and Statement of Reasons for Repeal of 20.2.350 NMAC. No. EIB 11-15(R). Page 35.
[12]EIB Order and Statement of Reasons for Repeal of 20.2.350 NMAC. No. EIB 11-15(R). Pages 36 and 37.
[13]EIB Order and Statement of Reasons for Repeal of 20.2.350 NMAC. No. EIB 11-15(R). Page 35.
[14]EIB Order and Statement of Reasons for Repeal of 20.2.350 NMAC. No. EIB 11-15(R).http://www.nmenv.state.nm.us/eib/documents/EIB11-15R-SOR.pdf.
[15]Conversation on March 26, 2012, with representatives of NMED.
[16]Simonich, Milan. "Pollution Rule Down the Tubes." El Paso Times. 16 March 2012.http://elpasotimes.typepad.com/newmexico/2012/03/pollution-rule-down-the-tubes.html#tp

Update From the Hill

By Nils Johnson

The main focus on the Green House Gas issue in DC has been U.S. EPA's proposal last week to reduce greenhouse gas emissions from new power plants effectively requiring all power plants to bring their emissions in line with those achieved by efficient natural gas power plants (1,000 pounds of carbon dioxide per megawatt-hour). As can be imagined the coal industry is very unhappy and the gas industry is ecstatic.

The proposed EPA rule exempts all existing plants, including plants that are already far along in the permitting process and due to begin construction in the next 12 months.

As a result of EPA's action the ranking member of the Senate Environment and Public Works Committee released a statement before EPA made its announcement accusing the Obama administration of introducing the largest energy tax in history just as the economy is struggling to get back on its feet. Senator Inhofe said he would offer a resolution under the Congressional Review Act that would strike down the rule once it is finalized (2012), and prevent EPA from crafting similar regulations in the future.

Any other action on a carbon cap remains very unlikely in this Congressional session that ends toward the end of this calendar year.

EPA Proposes to Limit GHG Permitting to Large Sources

Proposal Would Also Create Authority to Streamline GHG Permitting Process for Certain Sources
By Emily Schilling

On March 8, 2012, EPA published its proposal for Step 3 of the Prevention of Significant Deterioration ("PSD") and Title V Greenhouse Gas ("GHG") Tailoring Rule, which addresses permitting of GHG emissions from stationary sources under the Clean Air Act. Under the Step 3 proposal, EPA would not lower the permitting thresholds set forth in Steps 1 and 2 of the Tailoring Rule, which were issued by EPA on June 3, 2010, and would provide permitting authorities with additional flexibility to streamline permitting for sources that would otherwise be subject to the PSD program. 76 Fed. Reg. 14226 (March 8, 2012). A final rule is expected by July 2012, with an effective date of July 2013.

Under the Step 1 and Step 2 rulemakings, stationary sources with a potential to emit of more than 100,000 tons per year ("tpy") of CO2e and modifications of existing sources that total more than 75,000 tpy of CO2e must go through the PSD permitting process. As part of these earlier actions, EPA also committed to review the inclusion of smaller sources in the PSD permitting program and to propose streamlining provisions that would ease implementation of GHG permitting for both sources and state permitting authorities.

In its proposal, EPA refers to analyses demonstrating that reducing the 100,000 tpy threshold to 50,000 tpy would increase by 3,000 the number of sources that become major sources due to GHG emissions alone, while the number of modifications of existing sources triggered by a 50,000 tpy (as opposed to a 75,000 tpy) threshold would increase by more than 1,000. EPA also claims that lowering the thresholds would address only an additional three percent of GHG from stationary sources. EPA asserts that these statistics, coupled with the increased burden on permitting authorities, justify maintaining the thresholds set in Step 1 and Step 2 of the Tailoring Rule. EPA notes, however, that "a decision not to lower the thresholds in Step 3 does not foreclose a decision to lower them in Step 4." 76 Fed. Reg. at 14238. The Step 4 final rulemaking is not expected until April 30, 2016.

EPA also proposed two streamlining measures for GHG permitting: (1) creation of Plantwide Applicability Limits or "PALs" for GHG emissions; and (2) creation of a federal synthetic minor source permitting program for GHG.

A PAL is an emission limit that is applied to an entire source rather than individual emission limits. The PAL for GHG emissions would provide a source that is not major for any non-GHG pollutants with the flexibility to increase GHG emissions from individual units without triggering PSD permitting as long as it has accepted -and does not exceed- a source-wide limit on GHG.

A synthetic minor permit for GHG would allow a source that is not a major

source for non-GHG pollutants, but with a potential to emit ("PTE") above the regulatory thresholds for CO2e, to agree to an enforceable GHG emissions limit that is below the Tailoring Rule thresholds and therefore avoid PSD permitting. Although EPA asserts that many state permitting authorities already have this flexibility, the regulations for areas where EPA is the permitting authority must be amended to allow EPA to issue synthetic minor permits. This would include Indian Country and those states, including Wyoming, that do not yet have authority under their State Implementation Plans to regulate GHG.

In addition to these proposals, EPA seeks comment on a number of aspects of the GHG permitting program, including the impact of lowering the GHG thresholds for both PSD applicability and Title V, and various permit streamlining techniques such as general permits and the development of presumptive Best Available Control Technologies or "BACT" for GHG. EPA indicated that it does not intend to address any of these issues in the final rule, but may include these concepts in future rulemakings.

Comments must be received on or before April 20, 2012.

EPA Proposes High Hurdle for Construction of New Coal Power Plants

Rule Would Lead to Future Regulation of Existing Power Plants
By Chris Colclasure and Larry Volmert

On March 27, 2012, the U.S. EPA proposed to limit carbon dioxide emissions from fossil fuel-fired electric utility generating units ("EGUs"). New units above 25 megawatts would need to cap emissions at 1,000 pounds of CO2 per megawatt of gross output. This level is currently achievable by the latest natural gas combined cycle units but not by coal units. EPA anticipates that coal fired EGUs could comply with the proposed New Source Performance Standard ("NSPS") only through carbon capture and storage ("CCS"), which has not yet been applied to power plants on a commercial scale. EPA asserts that the proposal is "strictly limited to new sources," but buried within the proposal EPA admits that the NSPS "will also serve as a necessary predicate for the regulation of existing sources" and that EPA will be obligated to do so.

The proposed rule raises a number of legal and technical issues impacting both coal and gas fired EGUs. Several of these issues are identified below. Industry may submit comments for 60 days after publication of the proposed rule in the Federal Register.

Although the proposed rule is intended to "limit GHG emissions," EPA calculates that it will not reduce those emissions because EPA projects that few if any new coal EGUs would be built anyway. As Holland & Hart has argued in a pending challenge to EPA's GHG endangerment finding, regulations that do not advance their policy goals are irrational. EPA's statement strongly suggests that the rule's true purpose is to facilitate

regulation of existing coal and gas fired EGUs.

The proposed rule would effectively bar new coal power plants unless CCS is successful and cost effective. EPA has been inconsistent on CCS, stating here that it is feasible but stating in March 2011 that CCS would be technically infeasible in at least some cases. The proposed rule would allow new coal units that install CCS to show compliance using the 30-year average of their emissions. This would give additional time to install or optimize CCS. EPA is soliciting comment on this "unique" compliance option, and on the possibility of extending the averaging period to 50 years.

The EPA's authority to issue this NSPS is likely to be disputed. The proposed rule identifies three alternative legal theories. EPA proposes to base the rule on either its previous finding that GHGs endanger public health or welfare, a new finding that emissions from EGUs cause or contribute to endangerment, or a new finding that the large volume of emissions from EGUs provides a rational basis for the NSPS. EPA does not explain these alternative legal theories but they have the potential to expand its authority to regulate air emissions if EPA successfully relies upon these theories here.

Another likely area for dispute involves EPA's proposal to group all fossil fuel fired EGUs into the same "source category." EPA is declining to establish subcategories based on the fuel used at each facility. This approach would allow the agency to impose an emissions limit that coal EGUs cannot yet meet. The validity of this approach is debatable given the significant differences between coal and gas fired units.

The proposed rule would exempt 15 coal EGUs that have already received preconstruction permits, so long as those plants commence construction within 12 months. EPA refers to these units as "transitional sources." EPA seems to invite challenges to this aspect of the rule by stating that its approach "could raise the question of consistency."

EPA projects that the proposed rule will not impose any costs on industry because it assumes that there will be no construction of new coal EGUs without CCS under current market conditions. This cost projection is questionable in light of the transitional sources identified in the proposal.

Although by its terms the proposed NSPS applies only to new construction, the proposed rule could impact the Prevention of Significant Deterioration ("PSD") program for major modifications to existing sources. Major modifications under PSD must install the Best Available Control Technology ("BACT"), determined on a case-by-case basis. The control technology must be as stringent as any applicable NSPS. An important question is whether, either as a matter of law or a matter of case-by-case BACT evaluation, the proposed NSPS would result in BACT determinations for modifications to existing sources that require CCS for coal-fired power plants or even require the substitution of natural-gas fired turbines for coal-fired units. The latter would change EPA's historical position that companies are generally not required to install controls that redefine a source. Adoption of the proposed NSPS could result in more

stringent BACT determinations or, at a minimum, cause substantial uncertainty in the PSD program.

Industry should consider submitting comments on a number of other issues raised in the proposed rule. Industry might comment among other things on whether it is appropriate to select natural gas combined cycle technology as the "Best System of Emission Reduction;" whether all natural gas EGUs can meet the proposed NSPS; the level and form of the standard; or the monitoring, reporting, and performance test requirements.
