

Alert 10-166



EPA Proposes Transport Rule to Replace CAIR: New Rule Governs Air Emission from Utilities Only

In two previous Client Alerts, we have reported the vacation of the Clean Air Interstate Rule ("CAIR") by the Circuit Court for the District of Columbia in *North Carolina v. EPA*, 531 F.3d 896 (2008) (*North Carolina I*) and CAIR's subsequent, temporary resuscitation by the Circuit Court, *North Carolina v. EPA*, 550 F.3d 1176 (2008) (*North Carolina II*), pending the drafting of a replacement rule by EPA. On July 6, 2010, the EPA released its draft of the proposed replacement, the Transport Rule. This article summarizes the new rule and highlights issues for which the EPA is expressly soliciting public comments.

The Transport Rule is specifically directed at emissions from electric generating units ("EGUs") in classes 2211, 2212 and 2213 of the North American Industry Classification System (NAICS). Like CAIR, the Transport Rule is intended to help downwind states achieve EPA's National Ambient Air Quality Standards ("NAAQS") for fine particulate matter (pM_{2.5}) and ozone (O₃). Also like CAIR, the Transport Rule actually regulates sulfur dioxide (SO₂)—a chemical precursor of pM_{2.5}—and nitrogen oxides (NO_x)—a chemical precursor of both pM_{2.5} and O₃— generated by upwind states.

By 2014, the EPA estimates that the proposed Transport Rule will reduce emissions of SO₂ by 6.3 million tons per year from covered states compared with emissions in 2005, the last year before CAIR came into effect. Emissions will thus be capped at 2.6 million tons in the states covered by the rule, which represents a 71 percent reduction from 2005. The corresponding figures for NO_x are a reduction of 1.4 million tons to the new cap of 1.3 million tons, which represents a 52 percent reduction. Less stringent reductions (5 million tons of SO₂, 700,000 tons of NO_x) will be required by 2012.¹

The EPA believes that the 2012 targets can be met using controls that are already in place, but that the 2014 targets will require additional controls. EPA estimates that the cost to utilities of the new rule will be \$2.8 million, but that the savings in annual health benefits will be between \$120 billion to \$290 billion.

Under the proposed rule, the 31 states and the District of Columbia that are to be the subject of regulation will be divided among four control regions, depending on which pollutant is being regulated. The states (including the District of Columbia) that are in each of the control regions are shown on the map reached by the following link to the EPA's information page: <http://www.epa.gov/airtransport/>. One control region is for annual NO_x emissions, a second is for NO_x emissions in the ozone season, a third is for SO₂ emissions subject to a low emission budget, and the fourth is for states with a less stringent SO₂ emission budget. In the control regions, each state (including the District of Columbia) will have its own emission budget. The budgets are directly linked to each state's significant contribution to downwind states' nonattainment of NAAQS and its interference with downwind states' maintenance of NAAQS.

The EPA has proposed that the initial allocation of emission allowances to existing utilities in 2012 should be based on the unit's emissions in 2009 or its 2012 base case emission projection, whichever is lower. Emission allowances for new units will be issued from a 3 percent set-aside in every state's emissions budget. How allowances for new units should be allocated is, however, one of the many issues for which the EPA has expressly solicited comments.

In its preferred version of the Transport Rule, EPA is proposing that emissions trading will be permissible intrastate, and, with some limits, interstate. The EPA is also soliciting comments on two alternative approaches, in the first of which only intrastate trading of allowances will be allowed, and in the second of which the EPA will establish emissions budgets for individual power plants with no trading allowed. The restricted nature of the emissions trading under each of these

alternatives was forced on EPA by the D.C. Circuit Court's decision in *North Carolina I* which struck down the regional trading approach of CAIR.

In addition, the EPA has expressed interest in developing a trading scheme using trading ratios that take into account differences in cumulative downwind impact of emissions from different upwind states. For instance, if emission reductions from State A were twice as effective in reducing downwind impact as emissions from State B, the trading ratio between States A and B would be 2:1. EPA has requested comments on whether such a scheme would be compatible with *North Carolina I* and section 110(a)(2)(D) of the Clean Air Act.

Finally, larger fossil fuel-fired electrical utilities fall within the scope of the acid rain provisions of Title IV of the Clean Air Act. CAIR provided for the conversion of Title IV SO₂ allowances to SO₂ allowances under CAIR, and the mandatory retirement of Title IV allowances. In *North Carolina I*, the court found this approach to be incompatible with the statute. Accordingly, under the proposed Transport Rule, SO₂ allowances under the new rule and SO₂ allowances under Title IV are not exchangeable, and the two programs will operate independently.

If you are the representative of an electric utility that will be affected by the Transport Rule, it may be in your company's interest to provide comments to the EPA. The comment period will run for 60 days from the date that the proposed rule is published in the *Federal Register*. Reed Smith is experienced in submitting comments on proposed legislation, and you may wish to contact one of the following attorneys to discuss the preparation of your submission.

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1. It may be noted that in *North Carolina I*, one reason that CAIR was vacated was that the 2015 compliance deadline for upwind states to meet their emission targets under CAIR was not coordinated with the statutory 2010 date by which downwind states had to achieve NAAQS for ozone. Clearly, at this late date, no interstate emission transport rule could take effect in time to significantly ease the ability of a downwind state to meet a 2010 deadline. Presumably EPA will take the absence of a timely implemented rule into account when determining the consequences of a downwind state's failure to reach its NAAQS target.

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