Legal Backgrounder

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EME HOMER CITY GENERATION, L.P. V. EPA: THE D.C. CIRCUIT'S RULING AND IMPLICATIONS FOR FUTURE RULEMAKING

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On August 21, 2012, the U.S. Court of Appeals for the D.C. Circuit struck down the Environmental Protection Agency's (EPA) Cross-State Air Pollution Rule (CSAPR) as unlawful and remanded it to EPA with instructions to promulgate a replacement rule. *EME Homer City Generation, L.P. v. EPA*, 2012 WL 3570721; slip op. at 59-60 & n.35. The court's decision represents a straightforward application of Supreme Court and D.C. Circuit precedent recognizing the limitations on EPA's authority under the Clean Air Act (CAA), and sets clear parameters for replacement rulemaking.

Background

CSAPR was published in the Federal Register on August 8, 2011, 76 Fed. Reg. 48,208. It represents EPA's attempt to redesign its Clean Air Interstate Rule (CAIR), which the D.C. Circuit remanded to EPA in 2008. *North Carolina v. EPA*, 531 F.3d 896 (D.C. Cir. 2008), *modified on petitions for reh'g*, 550 F.3d 1176 (D.C. Cir. 2008).

Like CAIR, CSAPR would have required reductions in emissions of sulfur dioxide (SO_2) and nitrogen oxides (NOx) from electric generating units, based on EPA's interpretation of CAA §110(a)(2)(D)(i)(I). That provision, which is sometimes referred to as the "good neighbor provision," requires, in relevant part, that each state's implementation plan (SIP) for attaining the national ambient air quality standards (NAAQS) "contain adequate provisions … prohibiting … any source or other type of emissions activity within the State from emitting any air pollutant in amounts which will… contribute significantly to nonattainment in, or interfere with maintenance by, any other State with respect to any [NAAQS]." CSAPR established an emissions cap-and-trade program and finalized a federal implementation plan (FIP) for each state covered by the rule. The first compliance period under CSAPR was to begin on January 1, 2012.

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Forty-five petitions for review of CSAPR were filed in the D.C. Circuit and consolidated. On December 30, 2011, the court issued a stay of CSAPR and directed EPA to keep CAIR in effect pending the court's resolution of the CSAPR litigation. The court ordered briefing on an accelerated schedule and heard oral argument on April 13, 2012.

The Court's Decision

The D.C. Circuit vacated CSAPR and the CSAPR FIPs in their entirety and remanded them to EPA with instructions to continue administering CAIR until EPA developed "a valid replacement." Slip op. at 60. The court held that EPA had "transgressed statutory boundaries" by committing two independent foundational errors, both of which were among the central arguments raised by petitioners: (1) EPA's impermissible definition of "significant contribution" in determining states' emission reduction requirements; and (2) EPA's issuance of CSAPR FIPs simultaneously with its determination of state-by-state emission reduction obligations. Slip op. at 7-8.

Issue 1: EPA's Definition of "Significant Contribution"

In CSAPR, EPA defined "significant contribution" in two stages. First, EPA deemed states whose emissions contribute to NAAQS nonattainment in a downwind state in an amount exceeding an EPA-defined percentage threshold to be "'significant contributor[s]' to the downwind State's air pollution problem." Slip op. at 15. In the second stage, "EPA abandoned the air quality thresholds" used in the first stage and "used a cost-based standard." Slip op. at 17. EPA then used modeling to develop "significant cost thresholds," slip op. at 19, which were in turn used to "determine[] the amount of SO_2 [or] NOx that each covered State could eliminate if its power plants installed all cost-effective emissions controls." Slip op. at 19-20. This analysis produced EPA-determined state emissions budgets.

The court's analysis of this issue is based squarely on its previous decisions in *North Carolina* and *Michigan v. EPA*, 213 F.3d 663 (D.C. Cir. 2000), the case involving challenges to EPA's 1998 NOx SIP Call Rule (another rule based on CAA §110(a)(2)(D)(i)(I)). The court explained "[a]lthough the statute grants EPA significant discretion to implement the good neighbor provision, the statute's text and this Court's decisions in *Michigan* and *North Carolina* establish several red lines that cabin EPA's authority" that "are central to our resolution of this case." Slip op. at 23. The court concluded that "EPA's reading of Section 110(a)(2)(D)(i)(I)—a narrow and limited provision—reaches far beyond what the [statutory] text will bear." Slip op. at 39.

The court identified "three independent but intertwined legal flaws in EPA's approach to the good neighbor provision." Slip op. at 31. First, CAA §110(a)(2)(D)(i)(I)'s focus on "amounts which will … contribute" to another state's nonattainment "is not a blank check for EPA to address interstate pollution on a regional basis without regard to an individual upwind State's actual contribution to downwind air quality." Slip op. at 23-24. In a reference to the first stage of EPA's "significant contribution" analysis in CSAPR, the court held that "once EPA reasonably designates some level of contribution as 'insignificant' under the statute, it may not force any upwind State to reduce more than its own contribution to that downwind State minus the insignificant amount." Slip op. at 24. The court confirmed that, consistent with its decisions in *Michigan* and *North Carolina*, "EPA may use cost considerations to require 'termination of only a subset of each state's contribution,'" and "may not use cost to force an upwind State to 'exceed the mark'" used to identify "significantly contributing" states in the first place. *See* slip op. at 35.

Second, the court explained that "the portion of an upwind State's contribution to a downwind State" is a relative determination, "meaning that each State's relative contribution to the downwind State's nonattainment must be considered." Slip op. at 24-25. This means that "the 'significance' of each upwind State's contribution cannot be measured in a vacuum, divorced from the impact of the other upwind States." Slip op. at 25. The court held that CSAPR "runs afoul of the statute's proportionality requirement" articulated in *North Carolina*, "because it made no attempt to calculate upwind States' required reductions on a proportional basis" and "failed to take into account the downwind State's own fair share of the amount by which it exceeds the NAAQS." Slip op. at 37-38.

Third, EPA must avoid obligations in upwind states that would "produce more than necessary 'over-control' in the downwind States—that is, [EPA must ensure] that the obligations do not go beyond what is necessary for the downwind States to achieve the NAAQS." Slip op. at 28. This limitation comes from the text of the statute, which "is not a free-standing tool for EPA to seek to achieve air quality levels in downwind States that are *well below* the NAAQS." Slip op. at 28. While "there may be some truly unavoidable over-control in some downwind States that occurs as a byproduct of the necessity of reducing upwind States' emissions enough to meet the NAAQS in other downwind States," slip op. at 29, the court found that in CSAPR, EPA "failed to ensure that the collective obligations of the various upwind States, when aggregated, did not produce unnecessary over-control in the downwind States." Slip op. at 38.

The court also briefly addressed the "interference with maintenance" clause of CAA §110(a)(2)(D)(i)(I), finding that this clause required an analysis of the impact of upwind emissions on specific maintenance areas, as directed in *North Carolina*. The court reiterated that EPA must "show some basis in evidence for believing that … 'amounts' from an upwind State, together with amounts from other upwind contributors, will reach a *specific* maintenance area in a downwind State and push that maintenance area back over the NAAQS *in the near future*." Slip op. at 39 n.25 (emphases added).

Issue 2: EPA's "FIP-First" Approach

After establishing state emission budgets under CSAPR, "EPA did not stop there and leave it to the States to implement the required reductions through new or revised [SIPs]." Slip op. at 20. Through EPA's simultaneous imposition of FIPs, it was "EPA, and not the States, that decide[d] how to distribute the allowances among the power plants in each State." Slip op. at 20. As the court found, this represented a significant departure from EPA's approach in previous rules implementing CAA §110(a)(2)(D)(i)(I). In both CAIR and the NOx SIP Call, EPA allowed covered states an opportunity to implement the standards defined in the rules before imposing FIPs.

Based on Supreme Court and D.C. Circuit decisions, including *Train v. Natural Resources Defense Council*, 421 U.S. 60 (1975), and *Virginia v. EPA*, 108 F.3d 1397 (D.C. Cir. 1997), the court described the CAA's cooperative federalism structure and its "strict" "statutory division of authority" between the federal government and the states. Slip op. at 41-42. Based on the statute and these precedents, the court found that EPA's simultaneous issuance of FIPs with CSAPR violated the CAA. Slip op. at 45. As the court explained, EPA was required to quantify the states' interstate significant contribution before any "SIP can be deficient for failing to implement the good neighbor obligation." Slip op. at 45. Because "the good neighbor obligation is not a clear numerical target … the upwind State's obligation remains impossible for the upwind State to determine *until EPA defines it*." Slip op. at 48.

Future Rulemaking

The court directed that EPA continue to implement CAIR pending remand rulemaking applying the statutory criteria. To assist in this remand rulemaking, the court described CSAPR's flaws in detail, often giving illustrative examples that leave little ambiguity regarding what EPA may and may not do on remand. *See, e.g.*, slip op. at 27 n.15, 28 n.16.

To comply with the court's decision, for example, EPA will need to ensure at a minimum that the emission reductions required of each state are no greater than the amount that EPA has identified as significant for that state, and then use the cost of emission reductions to *lower* (not increase) a state's emission reduction obligations. EPA will need to consider the proportionate contributions of all upwind states contributing to the same downwind areas to ensure that the replacement rule does not require any state to "share the burden" belonging to those other states. EPA must also avoid requiring upwind states to reduce their emissions by an amount more than necessary to allow downwind states to attain the NAAQS. Regarding maintenance areas, EPA will need to give independent meaning to the "interference with maintenance" clause of CAA §110(a)(2)(D)(i)(I). Finally, once EPA quantifies the emissions from each state that contribute significantly to downwind nonattainment or interfere with maintenance of the NAAQS in downwind states, it will need to allow the states an opportunity to develop SIPs achieving the emission reductions necessary to comply with the rule before promulgating FIPs. Failure on the part of EPA to fulfill these requirements will mean a continuation of the CAIR/CSAPR saga.

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