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Will Pa. Businesses Benefit From New Source Review Reform?

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Special to the Legal

Among the myriad of complex legal standards imposed under the federal Clean Air Act, the New Source Review (NSR) program has achieved the ignominious distinction as the most controversial — and despised — regulatory program, at least from the perspective of regulated industry.

The Clean Air Act requires the Environmental Protection Agency to identify an appropriate ambient concentration, termed the National Ambient Air Quality Standard or NAAQS, for each “criteria” air pollutant identified in the statute. Based upon ambient air quality monitoring data, the EPA then designates each air quality control region as attaining the NAAQS (attainment areas), failing to attain the NAAQS (non-attainment areas) or unclassifiable based upon existing information.

The NSR program is then intended to balance economic development with air quality protection by ensuring that increased emissions associated with new economic activity does not interfere with the necessary air quality improvement in non-attainment areas and the preservation of air quality in attainment or unclassifiable areas. In order to accomplish this balancing, NSR is divided into two programs - the prevention of significant deterioration (PSD) program for attainment areas and non-attainment NSR (NSR-NA) for non-attainment areas.

A source subject to NSR must satisfy stringent emission control technology standards — best available control technology

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(BACT) under PSD, and lowest achievable emission rate (LAER) under NSR-NA, perform more extensive air emission analyses, and undergo greater scrutiny of permit applications. In addition, emissions from a new or modified source subject to NSR-NA must be offset by emission reductions from existing sources at a ratio greater than 1:1; the precise ratio is prescribed by the regulation; depending upon the severity of the non-attainment status. Numerous disputes have arisen concerning the appropriate determination of BACT and LAER technology, and permit applicants routinely complain about the extended permit application review timeframe under NSR/PSD.

More significantly, the application of NSR/PSD to modifications of existing sources has been the subject of numerous legal disputes, multibillion-dollar EPA enforcement initiatives and a recent decision of the U.S. Supreme Court. The Clean Air Act includes a definition of “modification” that extends to “any physical change in, or change in the method of operation of,” a source. The EPA concedes that this broad definition would extend to virtually any activity involving an existing source, and therefore also promulgated exceptions to this definition, notably including an exception for routine maintenance, repair and replacement activity.

The greatest source of controversy under

NSR is the evaluation of whether proposed maintenance, repair or replacement activity at an existing source is properly characterized as “routine.” The EPA’s multibillion-dollar enforcement initiatives against the electric utility sector and petroleum refining industry rest primarily on the question of whether maintenance and repair activities conducted by virtually every company within each industry sector were properly characterized as “routine,” or rather should have been subjected to NSR/PSD permit review.

The EPA attempted to provide industry with greater clarity concerning the scope of the routine maintenance, repair and replacement exception. Specifically, the EPA promulgated a regulation establishing that the replacement of existing components with identical or functionally equivalent equipment would qualify as an exemption to the definition of “modification,” if certain criteria were satisfied.

However, as with all activity concerning NSR, certain parties were not happy with the EPA’s proposed changes. In particular, northeastern states, including Pennsylvania, and national environmental groups challenged the rule. The petitioners contended that the EPA did not have the authority under the Clean Air Act to implement these sweeping changes to NSR.

On March 17, 2006, the D.C. Circuit Court vacated the EPA’s equipment replacement rule. The court held that the relevant statutory language prevented the EPA from exempting maintenance activity without consideration of the emission impact resulting from such activity. On April 30, 2007, the Supreme Court rejected the EPA’s peti-

tion for certiorari.

Not all modifications trigger NSR/PSD applicability, but rather only “major modifications.” A modification is major if it results in a “significant net emission increase.” Regulated industry, states, the EPA and environmental groups have disagreed over the appropriate calculation methods for this analysis. In response to these inconsistent interpretations and other controversies, the EPA promulgated significant changes to the NSR program (the NSR Reform Rule). Once again, states and environmental groups immediately filed a legal challenge to the EPA’s reform efforts.

In this case, the D.C. Circuit generally upheld the NSR Reform Rule with respect to three significant elements: a new baseline emission rate calculation, a new alternative “past actual to projected actual” test for calculating net emission increases from modifications, and the use of plant-wide applicability limits (PALs), pursuant to which a facility can establish an emission cap for all sources at the facility, and avoid NSR/PSD by maintaining emissions below the PAL cap.

However, this case did not end the controversy over the calculation of net emission increases for NSR purposes. In addition to the EPA’s NSR/PSD regulations, the EPA has also promulgated regulations under the Clean Air Act that establish new source performance standards (NSPS) for sources within specific operational categories. Like NSR, NSPS requirements extend to the construction of new sources or modification of existing sources.

In addition, the EPA relies on the same statutory definition of “modification” under the Clean Air Act for both the NSPS and NSR/PSD programs. Nonetheless, in evaluating whether a modification triggers regulatory applicability, the EPA has directed that permit applicants should evaluate the resulting increase in annual emissions for purposes of NSR/PSD, while requiring consideration of the increase in the source’s hourly emission rate under NSPS.

Industry sources contended that the EPA could not use the identical statutory definition to justify two distinct regulatory evaluations. In *United States v. Duke Energy Corp.*, the 4th U.S. Circuit Court of Appeals agreed with this industry contention. Only nine days later, however, the D.C. Circuit reached the contrary conclusion in *New York v. EPA*. The Supreme Court granted certiorari in the *Duke*

Energy case to resolve these inconsistent determinations by the circuit courts.

In a unanimous determination, the Supreme Court vacated the decision in *Duke Energy* on April 2. The court ruled that the 4th Circuit’s decision in *Duke Energy* effectively constituted a determination that the relevant NSR/PSD regulatory applicability provisions are invalid in the face of the statute; any challenge to the validity of the regulations must have been raised immediately following promulgation. Accordingly, the Supreme Court did not reject the EPA’s interpretation that the determination of a net emission increase resulting from a modification is evaluated under NSR on an annual basis.

As if the turmoil on the federal NSR landscape is not sufficient, matters of state implementation also contribute to the complexity. Pursuant to the Clean Air Act, states are charged with implementing the NSR/PSD programs within their borders. The federal PSD program applies in most states, including Pennsylvania.

By contrast, many states, including Pennsylvania, have promulgated a state-specific NSR-NA regulatory program. In response to the NSR Reform Rule, Pennsylvania is poised to publish its final revised state-specific NSR-NA program. Few industrial sources will regard the changes as beneficial. First, Pennsylvania has adopted an actual-to-future actual emission test option for evaluating emission increases resulting from modifications. Previously, Pennsylvania evaluated emission increases from a modified source by comparing the potential to emit of the source prior to the change to the potential to emit of the source subsequent to the change.

Under this evaluation, a modified source would not trigger NSR-NA if it did not cause emissions to exceed existing permit limits. Many source operators regarded this provision of the Pennsylvania rules as the lone oasis of sanity in the NSR program, since it allowed facilities to make changes to existing equipment without triggering the burdensome NSR program as long as the emissions from the source would remain within allowable permit rates.

Under the new Pennsylvania NSR-NA rule, a source must generally evaluate the expected emission rate resulting from a modification by comparing actual emission rates before the change with projected actual rates

after the change. Therefore, a modification to an existing Pennsylvania source may now trigger NSR even if the post-modification emission rate remains below prior permit limits.

Moreover, Pennsylvania’s revised regulation arguably does not even allow the source to rely on the projected actual emission rate in the calculation. In contrast to the NSR Reform Rule, Pennsylvania’s NSR applicability analysis for modified sources requires that the projected “actual” emission rate must be translated into a permit condition. The intended benefit of the actual-to-future actual test relative to the actual-to-potential test is that the source need not accept permit-based emission restrictions to avoid NSR when the proposed modification will not actually cause a significant emission increase; that benefit is not available under the new Pennsylvania NSR-NA regulations.

Further, the Pennsylvania regulation provides less flexibility than the NSR Reform Rule in the calculation of the baseline actual emission rate used for calculating emission increases resulting from modifications. While the NSR Reform Rule allows an applicant to select any 24-month period during the past 10 years for the baseline emission rate of a pollutant, and select different periods for different pollutants, Pennsylvania’s program generally limits the consideration to the most recent five years, and requires that the same 24-month period be used for all pollutants.

In addition, in contrast to the federal program, Pennsylvania has maintained its requirement that fugitive emissions be included in the emission calculus for all sources. Further, all sources performing an NSR evaluation must aggregate all emission increases and decreases during the most recent 10 years to determine whether the net emission increase exceeds NSR thresholds. Under the federal program, a source may elect to perform such netting, but is not required to do so.

CONCLUSION

In short, following several EPA rulemaking efforts, numerous court challenges, and distinct state regulatory development, the NSR/PSD landscape remains highly uncertain and controversial. The proponent of any new source, and more importantly any modification to an existing source, must carefully consider the implications of the current

regulatory standards for NSR and PSD in designing a proposed project and preparing a permit application.

Applicability of NSR/PSD to a proposed

project can result in significant additional costs, and will almost certainly result in additional time required for review of the permit application. However, the source owner that

fails to properly address NSR/PSD applicability faces the potential for significant liability for noncompliance with state and/or federal regulatory requirements. •