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The U.S. Supreme Court Upholds EPA's Cross-State Air Pollution Rule in *EPA v. EME Homer City Generation, L.P.*, Paving the Way to Further Use of Cap-and-Trade Programs to Control Emissions of SO2 and NOx from Electric Power Plants.

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On April 24, the Supreme Court issued a 6-2 decision in EPA v. EME Homer City Generation, L.P.*, No. 12-1182, 356'ŴEv037: 6 (2014), upholding EPA's latest version of a regional cap-and-trade program under the federal Clean Air Act (CAA) to control those electric power plant emissions of sulfur dioxide (S02) and nitrogen oxides (NOx) that contribute to interstate formation of fine particle and ozone (smog) pollution. Of first importance, the Court removed the doubt haunting such programs for more than 15 years that EPA has power under the CAA to set the cap for such a program primarily on the basis of costs of control, an element of fairness vital to willing participation. By doing so, the Court largely cleared the path for EPA to use a regional cap-and-trade program to implement the revised National Ambient Air Quality Standard (NAAQS) for ozone that EPA is expected to issue before the end of the Obama Administration. In addition, the Court's decision gives insight into how it may resolve pending challenges to EPA's regulation of greenhouse gas (GHG) emissions through its Prevention of Significant Deterioration (PSD) permitting program.*

Background

Under the CAA, once EPA sets a NAAQS, each state has primary responsibility to fashion, and submit to EPA for approval, a State Implementation Plan (SIP) satisfying certain CAA design criteria. These criteria include so-called "Good Neighbor" measures aimed at keeping "emissions activity" within a particular state from generating "amounts" of air pollutants that "will *contribute significantly* to nonattainment in, or interfere with maintenance by, any [downwind] state" with respect to the particular NAAQS.[1] If a state fails to submit an approvable SIP in timely fashion, EPA must issue a Federal Implementation Plan (FIP) to fill the gap. While the CAA gives EPA two years to do that, it also authorizes EPA to issue the FIP "at any time" within that two-year period.[2]

In the early 1990s, eastern and midwestern states, spurred by almost 25 years of failure to attain the NAAQS for ozone and enabled by advances in computer modeling, undertook with EPA extensive analyses revealing the reality and extraordinary complexity of long-range transport of ozone and its precursors.[3] Those analyses, by contextualizing the CAA's Good Neighbor provision, spotlighted the difficulty of giving it practical meaning and efficacy. But the analyses, along with the then-growing success of the CAA's Acid Rain program, led EPA to establish, in close collaboration with the states, three multi-state cap-and-trade programs also aimed at electric power plants. These programs are:

> (1) the NOx SIP Call, promulgated in 1998 to help cure ozone nonattainment by limiting NOx emissions from such plants;[4]
>
> (2) the Clean Air Interstate Rule (CAIR) promulgated in 2005 to help cure ozone and fine particle (PM2.5) nonattainment by restricting SO2 and NOx emissions from such plants;[5] and
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> (3) the successor to CAIR, *i.e.*, the Cross-State Air Pollution Rule (CSAPR or Transport Rule), promulgated in 2011 to help cure ozone and PM2.5 nonattainment.[6]

In all three programs, EPA defined the contributory significance of a state's upwind emissions through a two part test: (1) whether the emissions prior to new control contribute appreciably to downwind nonattainment and (2) whether the emissions after control are at a level that would be achieved by the application of reasonably cost-effective measures, such as scrubbers for SO2 and selective catalytic reduction for NOx. Under that test, a neighbor state is obliged to reduce its appreciable contribution only to the extent affordable from the standpoint of national norms of cost-effectiveness. Because EPA had collaborated in each case so closely with states, that interpretation of the Good Neighbor provision enjoyed broad support among the states, enabling EPA to create a regional, generally voluntary system.

But was that interpretation authorized? Initially, the D.C. Circuit appeared to say "yes," in its review of the NOx SIP Call. *See Michigan v. EPA*, 213 F.3d 663, 674-80 (D.C. Cir. 2000). However, a strong dissent in that case by Judge Sentelle and vacillations by challengers, as depicted in detail by the *Michigan* majority, created doubt about the staying power of that "yes." *Id*. at 676-77. Subsequently, in the CAIR case, Judge Sentelle was a member of the three judge panel. He displayed during oral argument his unhappiness with the *Michigan* decision. The resulting *per curiam* decision, while purporting to honor *Michigan*, nonetheless

[1] *See* 42 U.S.C. §§7407(a), 7410(a), and 7410(a)(2)(D)(i)(I) (emphasis added).
[2] *Id*. §7410(c)(1).
[3] *See* ABA, *The Clean Air Act Handbook*, at 114-17 (2011).
[4] 63 Fed. Reg. 57356 (Oct. 27, 1998).
[5] 70 Fed. Reg. 25162 (May 12, 2005).
[6] 76 Fed. Reg. 48208 (Aug. 8, 2011).

found that CAIR's cap-and-trade system could allow a quantitatively significant contribution by one state to nonattainment in a downwind state to persist indefinitely, contrary to the panel's reading of the Good Neighbor provision. The court decided to vacate CAIR, saying: "In *Michigan*, we never passed on the lawfulness of the NOx SIP Call's trading program."[7] *North Carolina v. EPA*, 531 F.3d 896, 908 (D.C. Cir. 2008). When the Transport Rule came before the D.C. Circuit in 2011, industry petitioners thus had an opening to challenge that rule's definition of neighborliness – *i.e.*, the achievement of insignificant contributions by the application of cost-effective controls, as mediated by a regional cap-and-trade program. *See EME Homer City Generation, L.P. v. EPA*, 696 F.3d 7 (D.C. Cir. 2012). In response to that challenge, the majority in effect adopted Judge Sentelle's reading of the Good Neighbor provision in *Michigan*, interpreted EPA's virtual elimination of the two year grace period prior to FIP issuance as a violation of the CAA principle of cooperative federalism and vacated the Transport Rule, denying petitions for rehearing and allowing the court's mandate to issue.

Decision of the Supreme Court in *EME Homer City*

On writ of certiorari to the D.C. Circuit, the Supreme Court held that the term "significantly" in the Good Neighbor provision is ambiguous, particularly in the complex context of interstate transport, and that EPA's definition "is a permissible, workable, and equitable interpretation" of that provision, requiring deference by federal court under *Chevron's* analytical framework. *See* slip op. at 32; *Chevron U. S. A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U. S. 837 (1984). The Court warned, however, that EPA lacks authority to force a state to reduce its emissions beyond the threshold level of significant (appreciable) contribution, regardless of the cost-effectiveness of achieving such reduction, and that a state thus aggrieved would be able to bring "a particularized, as applied challenge" to the Transport Rule. *Id*. at 31; *see also*, *id*. at 29. The Court also upheld EPA's power to shorten the two-year, pre-FIP grace period as EPA sees fit. In view of those holdings, the Court reversed the judgment of the D.C. Circuit and remanded the cases for further proceedings.[8]

Immediate Implications of *EME Homer City*

On remand, the D.C. Circuit faces various unresolved challenges and housekeeping tasks. In *EME Homer City* (No. 11-1302 and consolidated cases), some states may reactivate their petitions claiming that EPA improperly changed prior SIP approvals into disapprovals in order to impose the Transport Rule. *See* slip op. at 14 n.12. States or power plants may petition the D.C. Circuit for review of the Transport Rule on an "as applied" basis, as suggested by the Supreme Court. It is unclear whether the interim stay issued by the D.C. Circuit in December 2011 of the effectiveness of the Transport Rule remains in effect despite the reversal by the Supreme Court. At stake is whether CAIR continues in effect, and EPA may move for clarification on this issue. Also, the D.C. Circuit and UARG, *et al*. will need to sort out whether to proceed with a technical claim (No. 11-1358) related to electronic reporting that was severed from the *EME Homer City* case and put on hold pending Supreme Court decision. Also, two states have petitioned the D.C. Circuit for review of EPA's disapproval of their particular interstate transport SIP provisions, namely: Kansas and Georgia.[9] Finally, the court will have to decide whether the environmental petitioners' challenge to guidance that EPA issued in response to the court's now-reversed decision in *EME Homer City* is moot. *See Sierra Club v. EPA*, No. 13-1014 (D.C. Cir.).

EPA also faces questions, which may be raised through petitions for reconsideration or rulemaking, about whether the Transport Rule needs adjustment. The rule's compliance deadlines have passed and, more

7 The court later decided only to remand CAIR, not vacate it. *See North Carolina v. EPA*, 550 F.3d 1176 (D.C. Cir. 2008).

8 That decision will not take effect for another couple of weeks to allow opportunity for petitions for rehearing.

9 *See Kansas v. EPA*, No. 12–1019 (D.C. Cir.); *Georgia v. EPA*, No. 11–1427 (D.C. Cir.). A similar challenge is pending in the Sixth Circuit: *Ohio v. EPA*, No. 11-3988 (6th Cir.).

generally, some of its premises have become outdated. For instance, the Transport Rule does not take into account the tighter ozone NAAQS that EPA issued in 2008.[10] Also, EPA separately has issued rules that have altered, or will soon alter, regional ozone and PM2.5 concentrations, including the Mercury and Air Toxics Standards (MATS) for electric power plants under section 112(d) of the CAA, Tier III vehicle and fuel standards, and several standards for GHG emissions from motor vehicles. EPA's decision to make adjustments to the Transport Rule could bear on the positions it would take on how the D.C. Circuit and other circuit courts should handle *EME Homer City* and related cases on remand, especially because such adjustments likely would require notice-and-comment rulemaking.[11]

Larger Significance of *EME Homer City*

However, the complexity of the matters now facing the D.C. Circuit and EPA should not obscure the larger significance of the Supreme Court's decision in *EME Homer City* in two areas: (1) continued use of regional cap-and-trade programs and (2) the upcoming decision of the Supreme Court in *UARG v. EPA* (No. 12-1146), testing whether EPA had authority to regulate GHG emissions from stationary sources through the CAA's PSD and Title V permit programs.[12]

First, in the increasingly important field of interstate transport of ozone and fine particles, the *EME Homer City* decision gives EPA a more secure legal foundation upon which to continue its practice of collaborating with states to create consensus and then deploying regional cap-and-trade programs in which most affected states want to participate. Now EPA is able confidently to define good neighborliness for purposes of section 110(a)(2)(D) of the CAA in terms of the level of emissions reduction achievable by the application of reasonably cost-effective controls, as mediated by a cap-and-trade program, and to manage the process of SIP disapproval and FIP issuance somewhat more flexibly. That legal foundation may prove to be vital in minimizing, through a regional cap-and-trade program, the costs of attaining a more stringent NAAQS for ozone.[13]

Second, the *EME Homer City* decision may foretell the outcome in *UARG v. EPA*, the GHG PSD case pending before the Court. A striking feature of the *EME Homer City* decision is that Chief Justice Roberts and Justice Kennedy joined the majority in rejecting the D.C. Circuit's determination, evidently persuaded that the phrase "significantly contribute" is sufficiently ambiguous in context to amount to a delegation of authority to EPA to undertake legislative rulemaking to fill the gap. At oral argument in *UARG v. EPA*, the liberal wing of the Court (Breyer, Ginsburg, Kagan, and Sotomayor) appeared to favor EPA's position, raising the prospect that EPA was only one vote away from vindication. At the core of the case is the tension in section 165(a) of the CAA between the program-limiting message behind the applicability thresholds of 100 and 250 tons per year of emissions of a particular pollutant and the program-expanding message behind the phrase "any pollutant subject to regulation under the [CAA]." Given the receptiveness of the Chief Justice and Justice Kennedy to the view that the phrase "significantly contribute" in section 110(a)(2)(D) is ambiguous, one or both of them may be inclined to see significant ambiguity also in the tension between the two messages in section 165(a).

[10] Recent press reports indicate that a coalition of about 30 states is gearing up to conduct the computer modeling needed to apportion additional ozone control burdens via a memorandum of understanding.

[11] Among such related cases are several that arise in the context of the CAA program for improving and protecting visibility in national parks and like areas, where EPA has posited that the Transport Rule constitutes Best Available Retrofit Technology (BART) for certain existing power plants.

[12] Oral argument in *UARG v. EPA* took place on February 24, 2014. A decision is expected by the end of June 2014.

[13] The federal district court for the Northern District of California recently decided to order EPA to complete the ozone NAAQS rulemaking by October 1, 2015. *See Sierra Club v. EPA*, No. 13-2809 (N.D. Cal.). EPA staff is recommending a level of stringency for the new NAAQS in the range of 60-70 ppb, in contrast to the level of 75 ppb as currently set in the 2008 ozone NAAQS.

Conclusion

EME Homer City is an important decision for air quality management under the CAA, more so for its larger significance than for its immediate impact. It gives EPA a firmer legal foundation for deploying regional cap-and-trade programs, a development of substantial importance for implementing at least cost an even more stringent ozone NAAQS. Further, the decision may provide insight into how the Supreme Court will resolve the pending challenges to EPA's GHG PSD program.

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