

TEXAS ENVIRONMENTAL UPDATE



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TEXAS DEVELOPMENTS

EPA Issues 114s to Flexible Permit Holders and Asserts Jurisdiction to Issue Title V Permits

In news-making national press headlines, the Texas “SIP Gap” issues have taken a heightened political turn through two recent U.S. Environmental Protection Agency (“EPA”) initiatives. First, EPA has issued Clean Air Act (“CAA”) Section 114 information requests reportedly to all 150 Texas facilities with flexible permits. The information requests were issued in mid-May following prolonged and unsuccessful negotiations between the State of Texas and EPA regarding the state implementation plan (“SIP”) conformity of the Texas flexible permit program, the federal enforceability of flexible permits issued pursuant to that program, and how flexible permits can be “deflexed.” EPA’s move suggests that the Agency may be gearing up for enforcement actions against at least some of those facilities -- alleging that the flexible permit program has facilitated wide-scale circumvention of prevention of significant deterioration (“PSD”) requirements and avoidance of best available control technology (“BACT”) review and controls.

In a second move, on May 25, 2010, EPA took the bold step of calling in its first Title V permit application in Texas, claiming that the Texas Commission on Environmental Quality (“TCEQ”) had failed to respond to the Agency’s objections to the permit within the 90-day review period. EPA’s application call came one day after TCEQ submitted correspondence that outlined the difficulties the agencies had in resolving EPA’s objections. TCEQ Executive Director Mark Vickery concluded that “It seems that the only way EPA or TCEQ will be able to understand what is expected to alleviate any Title V programmatic objections is for EPA to issue a Title V permit.”

Even so, EPA warned in press releases that it is possible that it would make similar calls for the remaining 40 Title V permits to which it had submitted objections if TCEQ failed to respond to its objections. TCEQ officials decried the move, noting that EPA had approved the same Title V permit in the past without objection. Commissioner Carlos Rubinstein said,

Based on Dr. Armendariz’s statements and EPA actions, I do not believe the EPA is interested in serious negotiations to settle their objections to our permit program. EPA has not bothered to respond to letters and even stated they may not review proposed rules. It seems to me the outcome is predestined, regardless of any actions taken by the TCEQ. I have been involved in successful negotiations in the past. The process followed thus far by EPA is not one that allows for that. The time has come to end the double talk about our partnerships. Come to the table and negotiate in earnest.

EPA’s full statement is available at http://www.tceq.state.tx.us/comm_exec/communication/media/5-10flinthillsreact.

Other Texas SIP Activity

Although the ongoing controversy regarding Texas’ flexible permit program took center stage, a number of other Texas state implementation plan (“SIP”) developments occurred during May 2010. Among those developments were the following:

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- On May 21, 2010, TCEQ published notice that compliance with the following two contingency measures will be required in the Dallas-Forth Worth (“DFW”) ozone nonattainment area: (1) the requirements in 30 TAC Chapter 115, Subchapter F, Division 3, relating to degassing or cleaning of stationary, marine and transport vessels; and (2) the requirements in 30 TAC Chapter 115, Subchapter F, Division 4, relating to Petroleum Dry Cleaning Systems. These contingency rules are being implemented because the DFW area failed to attain the 1997 ozone national ambient air quality standard (“NAAQS”) by the June 15, 2010 attainment deadline. Affected owners or operators must comply with these contingency measures as soon as practicable, but no later than May 21, 2011. Additional information and a link to the publication (35 Tex. Reg. 4,268) are available at <http://www.tceq.state.tx.us/implementation/air/sip/dfw.html#New>.
- On May 18, 2010, EPA published final rules amending regulations to approve revisions to the Texas SIP regarding the discrete emission credit banking and trading program (75 Fed. Reg. 27644) and the emission credit banking and trading program (75 Fed. Reg. 27647). Texas submitted these SIP revisions for each of these programs on October 24, 2006 and August 16, 2007. The final rules, which will be effective on June 17, 2010, are available at http://www.access.gpo.gov/su_docs/fedreg/a100518c.html.
- On May 17, 2010, EPA published a rule proposal (75 Fed. Reg. 27,514) to approve a request to redesignate the Beaumont-Port Arthur nonattainment area to attainment status for the 1997 eight-hour ozone NAAQS and the one-hour ozone NAAQS. Comments on the proposal must be submitted to EPA by June 16, 2010. The publication, which also includes other proposals relating to the Beaumont-Port Arthur area SIP, is available at <http://www.regulations.gov/search/Regs/home.html#documentDetail?R=0900006480aef1c1>.
- At their May 14, 2010 work session the TCEQ Commissioners approved the Executive Director’s recommended request of the EPA to terminate the Federal Clean Air Act Section 185 fee program requirement for the Houston-Galveston-Brazoria (“HGB”) one-hour ozone nonattainment area. The request is based upon data from 2007-2009 showing that the HGB area is monitoring attainment of the 1997 eight-hour ozone NAAQS, and that such attainment is the result of permanent and enforceable emission reductions. Additional information, including the Executive Director’s recommended request, is available at <http://www.tceq.state.tx.us/implementation/air/sip/Hottop.html>.
- On May 13, 2010, EPA published a proposal to reject a portion of Texas the rules regarding emissions that occur during planned startup, shutdown and maintenance (“SSM”). Specifically, EPA proposed disapproval of provisions that provide for an affirmative defense against civil penalties for excess emissions from SSM activities. EPA distinguished between planned actions (such as planned SSM) and malfunctions or upsets beyond the facility’s control -- indicating that the Clean Air Act allows for application of an affirmative defense only to malfunctions or upsets. Comments must be submitted to EPA by June 14, 2010. The proposal (75 Fed. Reg. 26,892) is available at <http://edocket.access.gpo.gov/2010/pdf/2010-11429.pdf>.
- On May 4, 2010, TCEQ issued a statement indicating that EPA recently announced that it agrees with TCEQ that the Houston area is meeting the fine particulate matter (“PM2.5”) NAAQS. TCEQ credits compliance with that standard to marshalling the cooperation and assistance of the City of Houston, Harris County, the Port of Houston Authority, the Port Terminal Rail Authority, and local industry to reduce PM2.5 levels. The full text of TCEQ’s statement is available at http://www.tceq.state.tx.us/comm_exec/communication/media/5-10pm2.5.

TCEQ to Adopt Leak Detection Program Rules

On June 2, 2010, TCEQ’s Commissioners will consider adoption of two air quality rules

relating to leak detection. The first rulemaking involves the incorporation of an alternative work practice to use optical gas imaging instruments for leak detection and repair (“LDAR”) similar to the alternative work practice regulations recently adopted by EPA. See 73 Fed. Reg. 78199-78219 (December 23, 2008). The second rulemaking implements the provisions of House Bill 1526 (relating to incentives for the use of alternative leak detection technologies) adopted by the Texas legislature in 2007.

Specifically, under the first rulemaking, TCEQ will amend 30 TAC Chapter 115 to incorporate provisions of EPA’s alternative work practice regulations and add state-specific requirements. For example, TCEQ’s rules will include additional quality assurance and notification provisions. Under the second rulemaking, TCEQ will amend 30 TAC Chapter 101 to provide for the following incentives for the voluntary use of alternative leak detection technology: (i) compliance history-based penalty reductions; and (ii) conditional limits to enforcement actions if the leak or emission was detected by using alternative technology and it would not have been detected under TCEQ’s regulatory LDAR program. Additional information about both rulemakings is available at TCEQ’s website at <http://www.tceq.state.tx.us/rules/pendadopt.html#07040>.

TxDSHS Releases DISH, Texas Exposure Investigation Results

On May 12, 2010, the Texas Department of State Health Services (“TxDSHS”) reported its findings from an exposure investigation it conducted to measure various volatile organic compounds (“VOCs”) in the blood and urine of residents living in the DISH, Texas area. The TxDSHS concludes in its report that the information obtained from the investigation did not indicate that community-wide exposures were occurring in the sample population as a result of gas well or compressor station operations in the area.

TxDSHS conducted the investigation in response to a request by the mayor of DISH, who, along with residents in and around DISH, has expressed ongoing concern about exposure to contaminants from increased shale gas production activity in the area. TxDSHS collected blood and urine samples from 28 people living in and near DISH.

The blood samples were analyzed for VOCs to determine whether people living in and around DISH had higher levels of VOCs in their blood than 95% of the general U.S. population. Based on the findings, TxDSHS concluded that while a number of VOCs were detected in some of the blood samples, the pattern of VOC values was not consistent with a community-wide exposure to airborne contaminants. TxDSHS identified activities other than natural gas drilling operations as the likely source of exposure for the detected VOCs, including: cigarette smoking, ingestion of disinfectant by-products associated with chlorination of public drinking water systems, and the use of consumer products (e.g., moth balls, space deodorizers, metal cleaners, and lubricants).

In the urine samples, TxDSHS detected the urinary metabolite for benzene in three of the 28 people tested. TxDSHS determined the values in those three individuals were similar to those reported from other studies of smokers and non-smokers. TxDSHS also found that urinary results for the breakdown products of 1,2-butadiene and toluene and the urinary metabolite for N,N-dimethylformamide did not indicate community-wide exposures.

The TxDSHS report follows a January, 2010 TCEQ report of its findings regarding air emissions in the area. The TCEQ report covered the results of an intensive air monitoring effort covering 94 oil and gas monitoring sites in the Barnett Shale area. The study addressed multiple emission source types, including well-heads, condensate and product storage tank batteries, compressor stations, saltwater disposal wells, natural gas processing facilities, and operations associated with drilling and fracturing. TCEQ reported that at a majority of the monitoring sites chemicals were either not detected or were detected below levels of health concern. At two sites, TCEQ did find levels of benzene at a sufficient level to trigger facility repairs to reduce those emissions. At nineteen additional sites, benzene was measured at elevated levels that did not require immediate action.

The complete exposure investigation report is available at <http://www.dshs.state.tx.us/epitox/assess.shtm>.

Upcoming TCEQ Meetings and Events

- TCEQ's Air Quality Division will host a number of **public meetings regarding EPA's proposed 2010 ozone national ambient air quality standards** ("NAAQS"). The meetings will be held in select locations around the state from June 8 through July 20 to provide an opportunity to obtain information and offer comments on potential ozone nonattainment area boundaries and designations. Information regarding these meetings and submittal of written comments is available at <http://www.tceq.state.tx.us/implementation/air/aqps/eighthour.html>.
- TCEQ will host a **Dam Safety Workshop** in Tyler on June 10, 2010, and in Tomball on June 24, 2010. Information about these workshops is available at <http://www.tceq.state.tx.us/assistance/events/dam-safety.html>.
- TCEQ will host **Texas Emissions Reduction Plan ("TERP") Grant Application Workshops** and **TERP Dealer/Vendor Workshops** in select cities during June. Information about these workshops is available at <http://www.terpgrants.org>.

TCEQ Enforcement Orders

TCEQ announcements for enforcement orders adopted in May can be found on the TCEQ website at http://www.tceq.state.tx.us/comm_exec/communication/media/051910CommissionersAgenda.

Recent Texas Rules Updates

For information on recent TCEQ rule developments, please see the TCEQ website at <http://www.tceq.state.tx.us/rules/whatsnew.html>.

NATIONAL DEVELOPMENTS

EPA Explains Implementation of Greenhouse Gas Regulation With Issuance of Final "Tailoring Rule"

The Environmental Protection Agency ("EPA") has finalized its plan to regulate greenhouse gasses ("GHGs") under the existing Clean Air Act ("CAA"). While the debate in Congress continues over climate change legislation, on May 13, 2010, EPA released what is being called the final piece of the three-part puzzle for regulating GHGs beginning in early 2011. See Prevention of Significant Deterioration and Title V Greenhouse Gas Tailoring Rule (the "Tailoring Rule," available at <http://www.epa.gov/NSR/documents/20100413final.pdf>). The Tailoring Rule follows closely on the heels of two other GHG-related final rules issued by EPA within the last two months: the Johnson Memorandum and the Light Duty Vehicle Rule. While the previous two rules confirm that GHG emissions from stationary sources will be subject to regulation under the Clean Air Act beginning January 2, 2011, the Tailoring Rule establishes a phased implementation plan "tailoring" the stationary source permitting programs of the CAA to GHG emissions and limiting the number of sources affected by new GHG permitting requirements.

Background

EPA's Final Reconsideration of the "Johnson Memorandum"

The permitting requirements of the CAA's Prevention of Significant Deterioration ("PSD") program only apply to newly constructed or modified major sources that emit one or more pollutants "subject to regulation." See 40 C.F.R. 52.21(b)(50). Obtaining a PSD permit requires a source to install the best available control technology ("BACT") for those regulated pollutants that the source emits in quantities meeting or exceeding a threshold expressed in tons per year ("tpy"). EPA issued the Johnson Memorandum in 2008 in response to a

decision by the EPA Environmental Appeals Board, which remanded a PSD permit to EPA for a determination of whether GHG emissions were “subject to regulation,” thereby requiring application of BACT for GHG pollutants. See *In re Deseret Power Electric Cooperative*, PSD Appeal No. 07-03 (EAB 2008). In the Johnson Memorandum, EPA concluded that the PSD regulations apply only to those pollutants for which EPA had established actual emissions controls, which, at the time, did not include GHGs.

On March 29, 2010, EPA issued a final rule affirming the Johnson Memorandum’s interpretation that PSD permitting requirements are not triggered for a pollutant such as a GHG until a final nationwide rule requires actual control of emissions of the pollutant. See *Reconsideration of Interpretation of Regulations That Determine Pollutants Covered by the Clean Air Act Permitting Programs*; Final Rule, 75 Fed. Reg. 17,004 (April 2, 2010), available at <http://edocket.access.gpo.gov/2010/pdf/2010-7536.pdf>. In the final rule, EPA further refined its interpretation to establish that the triggering date is when the emissions control “takes effect,” not when the final rule is signed or published in the Federal Register. Finally, EPA expanded the Johnson Memorandum’s “subject to regulation” trigger to the Title V permitting program which requires major sources of air pollutants to obtain a permit incorporating in one document the myriad of requirements applicable to the individual facility. Thus, the final rule affirming the Johnson Memorandum established that PSD and Title V permitting requirements will apply to a newly regulated pollutant such as a GHG when and only when a regulatory control on emissions of that pollutant “takes effect.”

The Light Duty Vehicle Rule

Released on April 1, 2010, just three days after the rule affirming the Johnson Memorandum, the Light Duty Vehicle Rule (“LDVR”) is EPA’s first national emissions standard to control GHG emissions from passenger cars and light duty trucks. See *Light-Duty Vehicle Greenhouse Gas Emission Standards and Corporate Average Fuel Economy Standards*; Final Rule, 75 Fed. Reg. 25324 (May 7, 2010), available at <http://edocket.access.gpo.gov/2010/pdf/2010-8159.pdf>. The first GHG standards under the LDVR take effect when the 2012 model year begins, which is no earlier than January 2, 2011. On that day, the LDVR will make GHGs “regulated pollutants” under EPA’s interpretation, which, according to the Johnson Memorandum, will trigger PSD and Title V permitting requirements for all GHG-emitting stationary sources.

The PSD and Title V Greenhouse Gas Tailoring Rule

According to EPA, the final tailoring rule (available at <http://www.epa.gov/NSR/documents/20100413final.pdf>) is intended to reduce what is expected to be a massive permitting burden on previously unregulated sources when the LDVR takes effect and GHGs become a regulated pollutant under EPA’s interpretation of the Clean Air Act. To reduce the burden, the Tailoring Rule increases the threshold level of GHG emissions that will trigger the permitting requirements. Under the CAA, new or modified major sources must obtain PSD permits and implement BACT if the source emits at least 100 or 250 tpy (depending on the type of source) of a regulated pollutant. Likewise, Title V permitting requirements apply to sources that emit at least 100 tpy of a regulated pollutant. According to EPA, while the statutory thresholds are appropriate for criteria pollutants, such as lead and sulfur dioxide, they are not feasible for GHGs, which are emitted in much higher volumes. Applying the statutory thresholds to GHG emissions would sweep thousands of new or modified sources into the PSD program, and subject millions of sources to the requirements of Title V.

The Tailoring Rule seeks to reduce the permitting burden by “tailoring” the requirements of the PSD and Title V permitting programs to cover only the largest GHG-emitting sources. The rule establishes a schedule to phase in the permitting requirements for GHGs in two initial steps:

Step 1: (January 2, 2011 – June 30, 2011)

- During the first six-months, no sources would be subject to permitting requirements due solely to GHG emissions.
- Only sources that would be otherwise subject to PSD requirements (*i.e.*, sources that are newly constructed or modified in a way that significantly increases

emissions of a pollutant other than GHGs) may be subject to permitting requirements for their GHG emissions. Further, these sources would only need to go through a GHG BACT analysis if their GHG emissions increase by 75,000 tpy or more.

- Similarly, only sources currently subject to Title V (i.e., major sources for a pollutant other than GHGs) will be subject to Title V requirements for GHGs.

Step 2: (July 1, 2011 – June 30, 2013)

- PSD requirements will apply to modifications at existing facilities if the modification increases GHG emissions by at least 75,000 tpy, even if the modification does not exceed the significance threshold of any other pollutant. New construction projects will trigger permitting requirements if the facility will emit at least 100,000 tpy of GHGs, even if the project does not exceed the permitting threshold for any other pollutant.
- Title V operating permits will apply to facilities that emit at least 100,000 tpy of GHGs, even if the source does not exceed the significance threshold for any other pollutant.

Outline of the Future

The final Tailoring Rule also outlines a third step for implementing requirements between June 30, 2013 and April 30, 2016. The third step will be preceded by an additional rulemaking action set to begin in 2011 and conclude no later than July 1, 2012. According to EPA, the Step 3 rulemaking will consider reducing the GHG emission threshold to a level not lower than 50,000 tpy, and will consider the possibility of permanently exempting smaller sources from permitting requirements and other “streamlining options” designed to reduce regulatory burdens. EPA will not require permits for smaller sources in step three until at least April 30, 2016.

Other Noteworthy Points

- The thresholds that will trigger GHG permitting requirements under the final Tailoring Rule are significantly higher than the 25,000 tpy threshold originally proposed in the rule’s October 27, 2009 proposal. See Prevention of Significant Deterioration and Title V Greenhouse Gas Tailoring Rule; Proposed Rule, 74 Fed. Reg. 55,292 (Oct. 27, 2009). The increase is due in part to comments from state permitting agencies that expressed concern over the administrative burdens of a lower threshold.
- According to EPA, the new GHG emissions thresholds will also take effect in state, local, and tribal programs that administer their own CAA permitting requirements under EPA approval (i.e., state implementation plans or “SIPs”). The final rule asks states to inform EPA whether they must make rule changes to implement the new GHG emissions thresholds, and if so, when such changes will be adopted. If a state is unable to implement the new thresholds, EPA will “take appropriate action to ensure that the existing CAA permitting rules do not apply to sources excluded” by the Tailoring Rule.
- The final rule applies to six GHGs: Carbon dioxide (CO₂), Methane (CH₄), Nitrous oxide (N₂O), Hydrofluorocarbons (HFCs), Perfluorocarbons (PFCs), and Sulfur hexafluoride (SF₆). Because some GHGs have greater potential to effect climate than others, the GHG thresholds express GHG emissions in “carbon dioxide equivalents” (CO₂e). The CO₂e metric translates emissions of gases other than CO₂ into CO₂e by using the gases’ climate change potential. Total GHG emissions will be calculated by summing the CO₂e emissions of all six regulated GHGs.
- EPA plans to develop supporting guidance to assist permitting authorities, including guidance on identifying BACT for GHGs.

Conclusion

Issuance of the final Tailoring Rule is the most significant step to date toward regulation of GHG emissions. The rule eases the implementation of CAA permitting requirements that would otherwise apply to a multitude of GHG-emitting sources beginning January 2, 2011, when the LDVR takes effect and, according to EPA, makes GHGs “subject to regulation” under the PSD and Title V permitting programs. Nevertheless, stakeholders can continue to expect new developments on all fronts of the GHG issue, including proposed legislation and additional regulatory developments and guidance. There is a high likelihood the Tailoring Rule will be challenged in court given the arguably questionable bases EPA has to alter by rule the emissions thresholds set forth in the CAA, delay implementation of GHG permitting requirements, and order the Tailoring Rule to take effect even in SIP-approved state permitting programs. If the Tailoring Rule is rejected by a federal court, it could impose burdensome permitting requirements on a massive amount of small GHG sources and create a regulatory clog difficult to address without Congressional intervention. For now, large emitters of GHGs should watch the issue closely and be sure to understand the permitting obligations scheduled to take effect in 2011.

For additional information or questions regarding this final rule and its relation to other EPA rules regarding GHGs, please contact David Friedland at dfriedland@bdlaw.com, (202) 789-6047, Amy Lincoln at alincoln@bdlaw.com, (415) 262-4029, Laura LaValle at lavalle@bdlaw.com, (512) 391-8020, or Graham St. Michel at gstmichel@bdlaw.com, (202) 789-6039.

EPA Looks to Expand Mandatory GHG Emissions Reporting Program

The Mandatory Greenhouse Gas (“GHG”) Reporting Program is less than a year old, and already EPA is looking to expand the program’s scope. Four proposed amendments published on April 12, 2010, would add to the information already being reported under the program and bring new facilities within the program’s purview. Specifically, annual reports submitted under the program would have to include information on the reporting entity’s U.S. parent company(ies), applicable North American Industry Classification System (“NAICS”) codes, and whether any of the GHG emissions being reported are from cogeneration (i.e., producing both electric and useful thermal energy) activities. See 75 Fed. Reg. 18455 (April 12, 2010). New source categories proposed to be added to the program include electronics manufacturing, fluorinated gas production, the injection and sequestration of carbon dioxide, and certain segments of the petroleum and natural gas industries. See 75 Fed. Reg. 18652; 18576; 18608 (April 12, 2010).

In addition to the April 12 proposals, the Agency has sent a draft final rule to the White House that would add four more source categories to the program: industrial landfills, wastewater treatment facilities, underground coal mines, and magnesium production. The proposals and draft rule are discussed in more detail below.

I. Proposed new reporting requirements.

The additional reporting requirements proposed April 12 would apply to all facilities meeting the applicability criteria of the GHG emissions reporting program (found at 40 CFR part 98, subpart A), and would require facilities to submit the following information as part of their annual GHG emissions reports: (1) the name, address, and ownership status of U.S. parent company(ies)¹; (2) primary and other applicable NAICS code(s); and (3) whether any reported GHG emissions are from cogeneration units. See 75 Fed. Reg. at 18457-64.

According to EPA’s statements in the proposed rulemaking, the parent company and NAICS information will assist the Agency in aggregating comprehensive corporate-level and sector-level GHG emissions, *id.* at 18461-62, while information on cogeneration units is intended to assist in the development of future GHG-mitigation strategies. *Id.* at 18463.

A complete copy of the proposed rule amendment as published in the Federal Register on April 12, 2010, is available at <http://www.bdlaw.com/assets/attachments/75%20Fed.%20Reg.%2018455.pdf>. Comments on the proposal are due June 11, 2010.

II. Proposed mandatory GHG reporting for additional source categories.

A. Five source categories re-proposed for inclusion in the reporting program.

A second proposed rulemaking issued April 12 proposes to add five more source categories to the GHG reporting program: electronics manufacturing; production of fluorinated gases; use of electrical transmission and distribution equipment; manufacture or refurbishment of electrical equipment; and import and export of pre-charged equipment and closed cell foams. See 75 Fed. Reg. at 18652. All five of these categories were part of EPA's original GHG reporting program, as it was proposed in April, 2009, but were among several categories EPA elected not to include when finalizing the reporting program in October, 2009 based on concerns raised in public comments about costs and technical feasibility. *Id.* at 18654; see 74 Fed. Reg. 16448 (April 10, 2009).

The re-proposal includes changes to the categories' scope and applicable requirements designed to address these concerns. For example, based on public comments, EPA has proposed to clarify the affected source category for electric power transmission and distribution system equipment by defining a "facility" in this category as an "electric power system." 75 Fed. Reg. at 18681. "Electric power system" would be defined as the collection of SF₆- and PFC-insulated equipment that is linked through electric power transmission or distribution lines and operated as an integrated unit by one entity. SF₆- and PFC-insulated equipment includes gas-insulated substations, circuit breakers and other switchgear, gas-insulated lines, and power transformers containing SF₆ and PFCs. Equipment also includes gas containers such as pressurized cylinders, gas carts, new equipment owned but not yet installed, or other containers. *Id.* EPA is soliciting comments on further clarification of "facility" in this context and whether the Agency should incorporate the definition of a transmission/distribution entity used by the Regional Greenhouse Gas Initiative ("RGGI"). *Id.* at 18681.

With respect to electronics manufacturing facilities (e.g., facilities that manufacture semiconductors, liquid crystal displays, micro-electro-mechanical systems, and photovoltaic cells ("PV" cells)), the Agency has proposed new methods for estimating facility emissions and for reporting controlled emissions from abatement systems. See *id.* at 18655-69. Facilities under the electronics manufacturing subpart would have to report annual emissions from the production and transformation of fluorinated gas and destruction of fluorinated GHGs. *Id.* at 18670. EPA seeks comments on whether it should require reporting processes where GHGs are generated as by-products or intermediaries, and where fluorinated gas transformation is not co-located with fluorinated gas production facilities. *Id.*

For importers and exporters of pre-charged or closed-cell foams, reporting would include the type, charge sizes, and total pieces of equipment imported or exported. *Id.* at 18683. Foam importers would further report on the volume and fluorinated GHG density of the foam imported. *Id.* EPA seeks comments on the distribution of imports and exports, and the likely coverage at the proposed 25,000 mtCO₂e threshold. *Id.* at 18685.

Lastly, with respect to the manufacture and refurbishment of electrical equipment, the proposal is aimed specifically at SF₆ or PFC-insulated closed pressure equipment and sealed-pressure equipment, such as gas-insulated substations, circuit breakers and other switchgear, gas-insulated lines, or power transformers. *Id.* at 18686. The proposed reporting threshold is total annual purchases of SF₆ and PFCs exceeding 23,000 pounds. *Id.* EPA is seeking comment on whether transformers that use PFCs are manufactured in the United States, and whether PFC emissions occur at the same rate as SF₆ emissions.

Facilities in all five of these re-proposed categories would have to report emissions of fluorinated GHGs (e.g., perfluorocarbons (PFCs), hydrofluorocarbons (HFCs), sulfur hexafluoride (SF₆), and nitrogen trifluoride (NF₃)). Data collection requirements for affected facilities would begin in 2011, with the first reports due to EPA March 21, 2012. *Id.* at 18655.

A copy of the proposed rule is available at <http://www.bdlaw.com/assets/attachments/75%20Fed.%20Reg.%2018652.pdf>. Comments are due June 11, 2010.

B. Supplemental proposal to require reporting on injection and sequestration of carbon dioxide.

Another proposed amendment to the GHG reporting program would require monitoring and reporting on carbon dioxide (CO₂) injection and geologic sequestration (“GS”). See 75 Fed. Reg. at 18576. CO₂ injection facilities would be required to report CO₂ transferred onsite, the source of the CO₂, and CO₂ injected. *Id.* at 18579. GS facilities would be required to calculate CO₂ sequestered, factoring in leakages, fugitive, vented, or other CO₂ emissions. *Id.* The proposal includes an amendment to the reporting programs general provisions to apply the program to CO₂ injection and sequestration on and under the Outer Continental Shelf. *Id.* at 18580. EPA states in the proposal that it’s seeking information on CO₂ injection and GS to aid in the Agency’s evaluation of GHG mitigation technology and relevant policy options. *Id.*

Comments on the proposal must be received by June 11, 2010. A copy of the proposed rule is available at <http://www.bdlaw.com/assets/attachments/75%20Fed.%20Reg.%2018576.pdf>.

C. Supplemental proposal to require GHG emissions reporting from petroleum and natural gas systems.

In the fourth proposed rule issued on April 12, 2010, EPA proposed to create 40 CFR part 98, subpart W, which would require certain facilities within the petroleum and natural gas industry to report if they emit 25,000 metric tons or more of CO₂e through vented, fugitive, or flare combustion sources. See 75 Fed. Reg. at 18610-11. These facilities would include: offshore petroleum and natural gas production facilities; onshore petroleum and natural gas production facilities (including enhanced oil recovery); onshore natural gas processing plants; onshore natural gas transmission compression facilities; onshore natural gas storage facilities; liquefied natural gas (“LNG”) storage; LNG import and export facilities; and natural gas distribution facilities owned or operated by local distribution companies. *Id.* at 18611. The Agency proposes the use of direct GHG emissions monitoring only for the most significant sources, and where other monitoring options are unavailable. *Id.* Component count and emissions factors are proposed methodologies for smaller sources. *Id.* Data collection at these source would begin in 2011, with the first report due to EPA in 2012. *Id.* at 18612. To ease the burden on sources, EPA opted not to propose the use of best available monitoring methods for the first year of data collection, but seeks comments on that decision. *Id.* Comments are due on or before June 11, 2010. A copy of the proposed rule is available at <http://www.bdlaw.com/assets/attachments/75%20Fed.%20Reg.%2018608.pdf>.

III. Draft final rule to require four more sectors to report GHG emissions.

In addition to the proposed rulemakings published on April 12, EPA has also sent to the White House for review a draft final rule that would extend the GHG reporting program to cover four more industry source categories: industrial landfills; wastewater treatment facilities; underground coal mines; and magnesium production. These four sectors were among the source categories originally proposed for inclusion in the program in April, 2009, but deferred when the final reporting program rule was issued later that year. According to the summary of the rule on the White House Office of Management and Budget’s website, EPA has concluded, after review of the relevant public comments, that the four categories do not need to be re-proposed. Rather, EPA has addressed the comments and is prepared to issue a final rulemaking incorporating the source categories into the reporting program. The draft final rule was submitted to the White House on April 30 for final interagency review. No publication date has been set. The status of the rulemaking is available on www.reginfo.gov under RIN 2060-AQ03.

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¹ Among the issues open for comment is whether EPA should require only the highest-level U.S. parent company for each facility or a list of all U.S. parent companies. See 75 Fed. Reg. at 18457 n.3.

Senators Kerry and Lieberman Unveil Comprehensive Energy and Climate Bill

I. Summary

On May 12, 2010, Senators John Kerry (D-MA) and Joseph Lieberman (I-CT) unveiled a “discussion draft” of their long-awaited climate change and energy bill, the American Power Act. Key features of the bill include economy-wide targets for greenhouse gas (“GHG”) emission reductions, a cap-and-trade program extending to electric utilities, manufacturing facilities, and natural gas distributors, and a fee imposed on fuel refiners in the form of a requirement to purchase and retire allowances. The bill also would provide numerous incentives and concessions, including loan guarantees for nuclear plant operators, expansion of offshore drilling, consumer rebates, and assistance for trade-exposed industries.

The bill emerges after nearly eight months of negotiations and numerous setbacks, most notably, the abrupt departure of sponsor Lindsey Graham (R-SC), who was expected to secure critical bipartisan support for the bill. Despite the optimism of Senators Kerry and Lieberman, prospects for the bill’s passage appear slim given the difficult political climate and renewed concerns regarding offshore drilling, a key concession in the bill.

The discussion draft of the 987-page bill is available at <http://kerry.senate.gov/americanpoweract/pdf/APAbill.pdf>.

II. GHG Emissions Limitations for Targeted Sectors

The bill would set nationwide GHG reduction targets to be achieved primarily through the bill’s central feature, a cap-and-trade program for the electricity and manufacturing sectors. In addition, petroleum refiners would be required to purchase allowances (to cover the emissions associated with the use of fuels they produce), but would not be permitted to trade these allowances. Specific provisions relating to the bill’s GHG emissions limitations are summarized below.

- *GHGs Covered:* The bill would apply to emissions of the “Kyoto six” GHGs — carbon dioxide (CO₂), methane (CH₄), nitrous oxide (N₂O), hydrofluorocarbons (HFCs), perfluorocarbons (PFCs), and sulfur hexafluoride (SF₆) — plus nitrogen trifluoride (NF₃). The U.S. Environmental Protection Agency (“EPA”) would have the authority to designate additional GHGs through rulemaking.
- *Overall Targets:* The bill would require a 4.75 percent reduction in GHG emissions below 2005 levels by 2013; a 17 percent reduction by 2020; a 42 percent reduction by 2030; and an 83 percent reduction by 2050.
- *Which Sectors Are Covered?* The bill would require “covered entities” to match their GHG emissions with allowances, which are issued on an economy-wide basis annually, and which decrease over time. Electric utilities would be covered entities beginning in 2013, while natural gas distributors and manufacturing facilities — including industrial gas producers and importers, nitrogen trifluoride sources, and various other industries (e.g., lime manufacturing, cement production) — would be phased-in as covered entities beginning in 2016. Petroleum refiners and importers would be required to purchase and immediately retire allowances on a quarterly basis beginning in 2013 to account for emissions associated with the use of covered fuels.
- *Threshold for Coverage:* The bill sets an emissions threshold of 25,000 metric tons of carbon dioxide equivalent per year for most categories of manufacturing facilities (although several categories of manufacturers are included as covered entities without reference to an emissions threshold, e.g., titanium dioxide and adipic acid production). Natural gas distributors would be covered entities if they deliver 460 million cubic feet or more of natural gas per year. Electric utilities and refiners that meet the definitions in the bill are covered irrespective of total emissions. Approximately 7,500 entities are expected to be regulated under the bill.
- *Allowance Allocation:* Covered entities (excluding refiners) subject to the cap-and-trade program initially would receive a certain percentage of allowances distributed

free of charge, with the percentage of auctioned allowances gradually increasing to 100 percent by 2030. Allocations to electric utilities would be based 75 percent on historic GHG emissions and 25 percent on retail sales. (This differs from the House-approved Waxman-Markey bill, which proposed an allocation based 50 percent on historic emissions and 50 percent on retail sales.) Refiners would be required to purchase allowances directly from EPA, and EPA would guarantee the availability of these allowances at the most recent auction price.

- *Offsets:* The bill would authorize up to two billion tons of offset credits per year for use toward compliance with emissions reduction obligations, 500,000 of which can be international offsets. Domestic offset credits could be used on a one-to-one basis (i.e., domestic offsets and allowances would “count” equally toward compliance obligations), while international offset credits would be discounted at a rate of 25 percent. Emitters may use offsets to meet a portion of their allowance requirements; that portion is equal the emitter’s percentage share of the total GHG emissions by covered entities times two billion. (In other words, they get a share of the pool of allowed offsets equal to their share of the covered entities total GHG emissions. As those numbers are not set yet, it is difficult to assess how restrictive this quantitative limit will be in practice.)

EPA and the Department of Agriculture (“USDA”) would be required to establish a domestic offsets program and to consider a specific list of eligible project categories, including: fugitive methane emissions (from coal mines, landfills, and oil and gas distribution facilities); agricultural, grassland, and rangeland sequestration and management; afforestation and reforestation; land use and forestry; and carbon capture and sequestration. A “positive list” of presumptively approved offset project types is included; EPA and USDA can add to it over time. The eligibility date for offset projects is set at January 1, 2009 (Waxman-Markey set it at January 1, 2001), though the bill does provide a means for the approval of offsets generated by projects dating back to 2001. Section 740 provides that “regulatory or voluntary greenhouse gas emission offset program may apply to [EPA and the USDA] for approval as a qualified early offset program.” The USDA would administer agriculture and forestry offsets and EPA would administer all others. The bill does not list eligible project categories for international offsets, but would establish a mechanism for generating international offset credits from reduced deforestation (“REDD”) activities.

- *Linkage:* The bill would permit EPA, in conjunction with the Department of State, to authorize the use of international allowances or credits toward compliance with the bill’s GHG emission limitations. In addition, EPA would be required within one year of the bill’s enactment to develop regulations allowing individuals or entities to exchange state allowances for federal emission allowances.

III. Cost Containment Mechanisms

In addition to the offsets provisions, the bill includes a significant cost containment mechanism that Waxman-Markey did not: a “hard” “price collar” to keep the price of carbon between \$12 and \$25 per ton. The price floor is set at \$12 in 2013 plus 3% + CPI in subsequent years; the price ceiling is set at \$25 in 2013 plus 5% + CPI in subsequent years. Note that the ceiling thus will increase at a faster rate than the floor. In addition to containing the cost of compliance, the price collar provides a great deal of cost certainty by limiting market fluctuation. Some commentators have warned that fixing such parameters at the outset can cause market distortions later, as conditions change.

IV. Market Oversight

Covered entities (except for refiners that have purchased allowances directly from EPA) would be able to trade allowances on a national GHG emissions market. However, participation in the primary market would be limited to entities that are subject to the bill’s compliance obligations or that are registered with the Commodity Futures Trading Commission (“CFTC”) as “regulated greenhouse gas market participants.” The CFTC, in conjunction with EPA, appears to have broad authority under the bill to permit or deny access to the primary market based on a determination as to whether “additional participants

are necessary for a liquid and well-functioning market” The bill would require derivatives sold on the secondary market to be cleared by a CFTC-approved “greenhouse gas clearing organization.” The bill also includes numerous provisions designed to prohibit fraud and manipulation with respect to GHG instruments, and the CFTC is authorized to limit excessive speculation.

V. Preemption of State and EPA Authority to Regulate GHGs

The bill would permanently preempt state authority to regulate GHGs through sub-national cap-and-trade programs. To mitigate the impact, the bill provides for some limited recognition of offsets generated under these programs. It also allows and in some cases requires EPA to incorporate registries and work done by state and voluntary organizations. For example, Section 733(b)(1) allows the EPA to “establish a registry (or expand an established emission allowance registry) for use in issuing and recording credits approved and issued.” Section 735(c) states that EPA, when establishing offset methodologies, “shall give due consideration to methodologies for offset projects existing as of the date of enactment of the Act.” Thus, EPA is given the flexibility to build on what NGOs, state governments such as California, and regional initiatives such as the Regional Greenhouse Gas Initiative (“RGGI”) and the Western Climate Initiative (“WCI”) have done.

While states’ cap-and-trade programs would be preempted, the bill would not prevent the states from continuing to develop GHG control programs or establish state-wide GHG emissions limits or energy efficiency measures.

The bill also would partially preempt EPA authority to regulate GHGs under certain programs. For example, it would prohibit EPA from regulating GHGs pursuant to the National Ambient Air Quality Standards, New Source Review, and Title V permitting authorities under the Clean Air Act. EPA would, however, retain authority under the bill to regulate existing power plants under Section 111(d) of the Clean Air Act. Moreover, EPA could continue to develop New Source Performance Standards for sources that are not covered entities (except those eligible to receive offset credits) and could potentially regulate GHGs under other federal statutes (e.g., the Clean Water Act).

VI. Other Key Provisions

- *Offshore Drilling:* The bill contains provisions to expand domestic oil drilling, including revenue sharing for states that allow increased production off their shores. However, the bill would also allow a state to prohibit drilling within 75 miles of the state’s shores.
- *International Competitiveness:* The bill would establish a border adjustment mechanism to take effect in 2025, which would essentially require importers to buy carbon allowances for commodities such as steel, aluminum, or cement from countries that do not have GHG reduction programs. In addition, the bill would establish an international reserve for the provision of allowance rebates to eligible sectors that are trade sensitive (determined by EPA through rulemaking).
- *Performance Standards for New Coal-Fired Power Plants:* Coal-fired power plants permitted after January 2020 would be required to reduce CO₂ emissions by at least 65 percent. New plants permitted between 2009 and 2015 would be required to reduce CO₂ emissions by at least 50 percent within four years from the date on which certain carbon capture and storage commercialization targets are met.
- *Consumer Rebates:* Two-thirds of revenues generated by the bill would be rebated to consumers through energy bill discounts and direct rebates. Additional rebates would be available for families that are disproportionately affected by increased energy costs.

VII. Next Steps

Despite the bill’s initial introduction as a “discussion draft,” pressure is mounting from environmental groups for formal introduction into the Senate. The bill is currently undergoing economic review at EPA, and results of this review are expected in late June. Meanwhile,

Senate Majority Leader Harry Reid (D-NV) is scheduled to confer with committee chairs in May to evaluate support for the bill and determine the timing of floor debate. If the bill passes the Senate, it would need to be reconciled with the Waxman-Markey bill that was approved by the House last June.

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Senate Passes Conflict Minerals Legislation

The Senate has passed legislation that would expand Securities and Exchange Commission (“SEC”) reporting and public disclosure obligations for a wide range of companies using certain “conflict minerals” and their derivatives. On May 18, 2010, the Senate amended its version of financial reform legislation with a provision, introduced by Senator Brownback (R-KS), that would require annual disclosures to the Securities and Exchange Commission relating to columbite-tantalite, cassiterite, gold, and wolframite originating in the Democratic Republic of Congo (“DRC”) or adjoining countries. The Senate passed the underlying financial reform legislation, H.R. 4173, the Wall Street Reform and Consumer Protection Act, on May 20, 2010. The House has already passed its version of H.R. 4173, which did not contain any conflict minerals provisions. A House-Senate conference committee will work to reconcile the two versions of the bill in the coming weeks. It seems likely that some version of the conflict minerals provision in the Senate bill will be included in the legislation delivered to the President.

The Brownback amendment requires the SEC to promulgate rules within 180 days mandating specified annual disclosures to the SEC by certain entities that manufacture a product, the functionality or production of which relies on certain “conflict minerals” and their derivatives. The covered minerals are columbite-tantalite, cassiterite, gold, and wolframite. The rules would apply to entities subject to the SEC’s quarterly and annual reporting obligations under Section 13(a)(2) of the Securities Exchange Act. Under the Senate provision, entities covered by the new rules would be required to:

- disclose annually whether any of the conflict minerals or derivatives came or may have come from the DRC or an adjoining country;
- describe the due diligence exercised on the source and chain of custody of the minerals or derivatives to ensure that the covered entity’s activities that involve the minerals or derivatives did not directly or indirectly benefit armed groups in DRC or an adjoining country; and
- make the information in its disclosures available to the public on the entity’s website.

The Brownback amendment (available at www.bdlaw.com/assets/attachments/2010-05-18%20Conflict%20Minerals%20Amendment.pdf) is similar to S. 891, the Congo Conflict Minerals Act of 2009, that Senators Brownback, Durbin (D-IL), and Feingold (D-WI) introduced earlier this session. Both proposals include the SEC disclosure model, which differs from the import declaration process proposed in legislation introduced in the House by Representative McDermott (D-WA). For further background on S. 891, see <http://www.bdlaw.com/news-575.html>.

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EPA Settles With Pep Boys in Largest Engine Importation Case in Clean Air Act History

On May 10, 2010, EPA announced a settlement with Pep Boys – Manny, Moe & Jack (“Pep Boys”) and Baja, Inc. (“Baja”), resolving violations by both companies under Title II of the Clean Air Act, which establishes emissions standards for mobile sources. In the settlement,

Pep Boys agreed to a \$5 million penalty and an estimated \$5 million in injunctive relief for its role in the sale of vehicles and engines that failed to comply with U.S. emissions standards. Baja agreed to pay \$25,000 for its role in importing the noncompliant engines that were ultimately sold in Pep Boys' 580 U.S. stores. EPA describes the settlement as the largest vehicle and engine importation case brought to date under the Clean Air Act, both in terms of the number of vehicles and engines imported and the penalty paid.

At issue in the case were 250,000 highway motorcycles, recreational vehicles, and generators manufactured in China and which failed to meet the emissions standards of Title II of the CAA and 40 C.F.R. Parts 86, 90, 1051, and 1068. The vehicles and engines were imported and sold between 2004 and 2009 from some 35 Chinese manufacturers and, according to EPA, led to excess emissions of more than 620 tons of hydrocarbons and nitrogen oxides, and more than 6,520 tons of carbon monoxide.

A complete copy of the consent decree is available at <http://www.epa.gov/compliance/resources/decrees/civil/caa/pepboys-cd.pdf>. Under the decree, Pep Boys has agreed to:

- Implement EPA mandated corporate compliance plans;
- Adhere to reporting and inspection requirements;
- Extend emissions-related warranties for certain vehicle and generator models;
- Establish a customer hotline and employee training program;
- Export or destroy over 1,300 noncompliant vehicles and generators; and
- Purchase emission credits and develop offset projects (including a program for consumers to exchange gas-powered lawn mowers for electric-powered mowers) to mitigate the emissions caused by their violations.

Imported vehicles and engines have become a top enforcement priority at EPA in recent years, as the Agency seeks to enforce the more stringent emissions standards that now apply to a wide variety of on-road and off-road vehicles and engines that are commonly sold in auto parts, home improvement, and discount warehouse stores across the country. (See EPA's September 2006 Enforcement Alert, available at <http://www.epa.gov/compliance/resources/newsletters/civil/enfalert/nonroadengines-0609.pdf>; see also EPA's 2007 Vehicle and Engine Imports Clean Air Act Information Sheet, available at <http://www.epa.gov/compliance/resources/cases/civil/caa/2007imports-infosht.pdf>.) The Agency's enforcement efforts used to focus primarily on the importers and distributors involved, but, as demonstrated by the Pep Boys settlement, that focus has shifted to retailers, who now bear the responsibility of ensuring that products on their shelves meet all Clean Air Act standards.

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Green Chemistry Developments at the Federal and State Levels

Green Chemistry at the Federal Level

Green Chemistry is gaining prominence as an approach to enhance the design and development of chemicals. At the federal level, recently proposed legislation to overhaul the Toxic Substances and Control Act incorporates Green Chemistry principles in a section entitled "Safer Alternatives and Green Chemistry and Engineering." The Environmental Protection Agency also already implements several programs that promote Green Chemistry, and the United States Senate recently confirmed Paul Anastas, the "founding father" of Green Chemistry, as Assistant Administrator for the Office of Research and Development at EPA.

In light of these activities, this Client Alert provides a detailed look at Green Chemistry and describes current Green Chemistry efforts at the federal level. Understanding Green Chemistry is important because the role of Green Chemistry is expected to amplify as the United States continues to manage and regulate chemical use into the future.

To read the full article on developments in federal Green Chemistry, please go to <http://www.bdlaw.com/assets/attachments/05-05-10%20BD%20Client%20Alert%20-%20Federal%20Green%20Chemistry.pdf>.

Green Chemistry at the State Level

In April 2010, California released proposed draft regulations for the implementation of the State's foundational Green Chemistry legislation. Viewed by many as a potential national model for chemical reform, California's legislation is considered to be one of the nation's first comprehensive, state-level efforts to find safer alternatives to hazardous chemicals, a core principle of Green Chemistry. The impact of the legislation and similar laws emerging throughout the states is potentially far-reaching for manufacturers and industry, which may face a number of new obligations, such as the full disclosure of product ingredients, and new restrictions, such as outright chemical bans. Given this significance, this Client Alert provides a detailed look at the ongoing development of Green Chemistry in California, as well as an overview of Green Chemistry efforts underway in several other states.

For the full article on developments in Green Chemistry at the state level, please go to <http://www.bdlaw.com/assets/attachments/05-05-10%20BD%20Client%20Alert%20-%20State%20Green%20Chemistry.pdf>.

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