

Power & Utilities Spotlight

CSAPR Vacated by Court of Appeals

EPA to Reconsider Which Way the Winds Blow

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The Bottom Line

The court has instructed the EPA to draft regulations to replace the CSAPR, which may take years to finalize, and to retain the CAIR until a replacement to the CSAPR has been finalized.

- On August 21, 2012, a federal appeals court vacated the U.S. Environmental Protection Agency's (EPA's) Cross-State Air Pollution Rule (CSAPR), which would have set limits on emissions from power plants in 28 states in the eastern half of the United States via a new cap-and-trade program.
- The court has instructed the EPA to draft regulations to replace the CSAPR, which may take years to finalize, and to retain the Clean Air Interstate Rule (CAIR) until a replacement to the CSAPR has been finalized.
- U.S. power and utility (P&U) companies should continue to evaluate different strategies to reduce power plant emissions to comply with state and EPA air-quality guidelines. Current regulations include the CAIR, the mercury and air toxics standards (the MATS rule), the National Ambient Air Quality Standards (NAAQS), and regional haze rules.

Beyond the Bottom Line

This *Power & Utilities Spotlight* discusses (1) the background of the CSAPR, (2) the federal appeals court's decision to vacate it, and (3) the overall effect of the court's decision on companies that own or manage power plants in the United States.

CSAPR in a Nutshell

Background

On July 6, 2011, the EPA issued the CSAPR, which would have required more than 1,050 coal-, natural gas-, and oil-fired electric power plants in 28 states in the eastern half of the United States to reduce sulfur dioxide (SO₂) and nitrous oxide (NO_x) emissions via a new cap-and-trade¹ program for emission allowances. The rule would have also required every affected state to adopt federal implementation plans (FIPs). The CSAPR was to have ultimately replaced the CAIR, which the EPA issued in 2005. According to the EPA, the CSAPR's overall purpose was to protect the health of American citizens by reducing air pollution that damages the ozone and results in the emission of fine particles. Effectively, the new rule would have been a means to enforce the requirements of the NAAQS.²

Legislative History

Congress enacted the Clean Air Act (CAA) in 1963 to research and regulate the effects of air pollution nationally. In 1970 and 1977, Congress greatly expanded the CAA to require the development of both federal and state regulations on industrial and mobile pollution (i.e., pollution caused by vehicle engine emissions). In 1990, amendments to the CAA required governments to establish regulations addressing pollution related to acid rain, ozone depletion, and toxic air pollution. These amendments also (1) increased enforcement authority, (2) established a national permit program for stationary sources,³ and (3) established new auto gasoline reformulation requirements.

The "good neighbor provision"⁴ in the CAA requires every state to operate its emissions policies responsibly and limit the adverse impact of pollution on neighboring states. Under this provision, states must institute a state implementation plan (SIP) that would:

[C]ontain adequate provisions [that would prohibit] 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 such national primary or secondary ambient air quality standard . . .

The CSAPR was designed to implement the good neighbor provision for the regulation of SO₂ and NO_x and would have required certain upwind states to establish measures to prevent the emission of pollution across state lines that would "contribute significantly to nonattainment" of the NAAQS by neighboring states. (See the [appendix](#) for details on states that would have been affected.) The rule's overall goal was to reduce SO₂ and NO_x emissions and pollution in downwind states. Certain aspects of the rule were to take effect January 1, 2012, with full implementation by 2014.

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¹ "Cap and trade" is a market-based approach to controlling pollution in participating areas by providing economic incentives for achieving reductions in the emissions of pollutants. Under this approach, a state or government body sets a limit or "cap" on the amount of pollutant that may be emitted and this cap is allocated or sold to companies in the form of emissions permits (known as allowances or carbon credits) representing the right to emit a specific volume. Companies are required to hold a number of allowances equivalent to their emissions and can buy additional allowances from other companies when their emissions volume exceeds the number of allowances they hold.

² NAAQS, as established by the EPA under the Clean Air Act, include both (1) primary standards designed to protect the health and well-being of the general population, with special focus on children, the elderly, and individuals suffering from respiratory diseases, and (2) secondary standards designed to protect the general public from any "known or anticipated adverse effects of a pollutant."

³ The EPA defines a [stationary source](#) as a "place or object from which pollutants are released and which does not move around. Stationary sources include power plants, gas stations, incinerators, houses etc."

⁴ Section 110(a)(2)(D)(i)(I) of the CAA is also commonly referred to as the "good neighbor provision."

In response to the court's decision to vacate the CSAPR, some electric power producers that had previously decided to abandon, or that may have temporarily idled, a power plant pending the outcome of the CSAPR ruling are reconsidering those plans.

Court Challenges

After its issuance, the CSAPR's legality was challenged for numerous reasons by various stakeholders, including states, local governments, industry groups, and labor organizations. On December 30, 2011, just days before the rule was to take effect, the CSAPR was stayed by the U.S. Court of Appeals for the D.C. Circuit to give the judges more time to consider its merits. On August 21, 2012, the court ruled 2–1 to vacate it.

While it addressed numerous points, the majority opinion cited two primary reasons for vacating the rule:

- The EPA exceeded its authority under the CAA by mandating that a state reduce its emissions beyond its level of significant contribution. The CSAPR does not properly account for an upwind state's proportional contribution to a downwind state's nonattainment of the NAAQS because it does not take into consideration (1) contributions by other upwind states or (2) the downwind state's independent contribution to its own nonattainment.
- The EPA overstepped its authority by imposing FIPs on states that were identified as upwind states. Upon its adoption of any EPA emissions standard, a state must be given the opportunity to initiate and execute a SIP before the EPA mandates a FIP. Under the CSAPR, however, the EPA executed a FIP when it implemented the rule, thereby violating the CAA.

What's Next

The court has instructed the EPA to act "expeditiously" in drafting and finalizing a rule to replace the CSAPR. In addition, the court has directed the EPA to retain the CAIR until a replacement rule has been enacted. The EPA has 45 days from the date of the opinion to petition for a rehearing or appeal to the U.S. Supreme Court.

Issued by the EPA in April 2005, the CAIR regulates emissions of SO₂ and NO_x from power plants, seeking to limit particles that drift from one state to another. The CAIR's cap-and-trade system, which covers 27 eastern states and the District of Columbia, allows the states to meet their individual emissions budgets by employing either of two compliance options: (1) requiring power plants to participate in an EPA-administered interstate cap-and-trade system that caps emissions in two stages or (2) undertaking measures of their own choosing.

Immediately after the court vacated the CSAPR, the trading prices for SO₂ and NO_x allowances for the CAIR program increased slightly (although allowance prices remain low relative to those of several years ago). CAIR SO₂ allowances in particular are plentiful and are trading at low prices. As a practical matter, the cost for a power producer to comply with the CAIR SO₂ emission requirements is not expected to be significant.

Impact on Electric Power Producers

Reconsideration of CSAPR Implications

In response to the court's decision to vacate the CSAPR, some electric power producers that had previously decided to abandon, or that may have temporarily idled, a power plant pending the outcome of the CSAPR ruling are reconsidering those plans.⁵ In addition, some power producers are considering delaying the implementation of certain SO₂ and NO_x emission control solutions that had been planned in response to the CSAPR requirements until those controls are needed for MATS rule compliance or until the EPA issues a replacement rule.

⁵ The plan to "unabandon" power plants might be temporary since, in many cases, companies might need to close down some of these same plants to comply with the MATS or other relevant regulations.

Power and utility companies should continue to evaluate different strategies to reduce emissions (including SO₂ and NO_x) to comply with state and EPA air-quality guidelines, including the MATS rule.

Compliance With Other Federal and State Regulations

Even though the CSAPR has been vacated, other federal and state regulations, including the CAIR, the MATS rule, the NAAQS, and regional haze rules, still curtail excessive emissions and air pollution. U.S. companies, including electric power plants, should familiarize themselves with changes to such regulations.

The EPA issued the MATS rule on December 16, 2011, to set a national standard for mercury emissions and to regulate power plant emissions of mercury, acid gases, and nonmercury metallic toxic pollutants. The MATS rule is intended to (1) prevent emission into the air of about 90 percent of the mercury in coal burned in power plants, (2) reduce acid gas emissions from power plants by 88 percent, and (3) reduce SO₂ emissions from power plants by 41 percent. Unlike the CSAPR or CAIR, the MATS rule is not a cap-and-trade program; no emissions allowances are involved. If a specific plant emits more mercury or other toxics than are permitted, that plant is not allowed to operate.

Under the MATS rule, reductions are to be achieved starting in the first quarter of 2015. Power producers are expected to employ available technologies to reach the prescribed mercury targets, including selective catalytic reduction (SCR) with flue-gas desulfurization, activated carbon injection (ACI), ACI with fabric filter, and electrostatic precipitators. For more information on the MATS rule, including information on targets, penalties, and technologies expected to be used to address other toxics, see the [EPA's Web site](#).

Thinking Ahead

Power and utility companies should continue to evaluate different strategies to reduce emissions (including SO₂ and NO_x) to comply with state and EPA air-quality guidelines, including the MATS rule. These strategies should take into account national gas prices as well as other economic factors, and they could potentially include (1) early retirement of certain plants, (2) retrofitting of existing plants with emissions reduction equipment, (3) changing the fuel mix of generating units, (4) temporarily idling plants, or (5) designing flexible dispatch plans. Although the industry is expected to achieve reductions of certain toxins without too much difficulty and, in many cases, with existing equipment (as would be the case with NO_x), the reduction of other toxins (e.g., SO₂) might present greater challenges.

The EPA is certain to continue monitoring air pollution nationally and to issue rules as needed to reduce toxic emissions in states where power plants are located as well as neighboring states. Deloitte's Power & Utilities industry team will (1) host live industry seminars, (2) conduct quarterly accounting update webcasts, (3) and host industry Spotlights as developments warrant. In addition, watch for Deloitte's annual *Energy & Resources Accounting, Financial Reporting, and Tax Update*, which will be published this winter.

Other Deloitte Resources

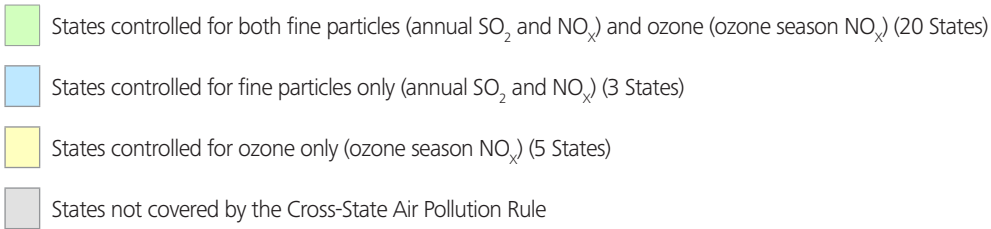
- [September 26, 2012, "Energy & Resources Quarterly Accounting Update Webcast — Q3 2012."](#)
- [Energy & Resources — Accounting, Financial Reporting, and Tax Update \(January 2012\).](#)

Appendix — States Included in the CSAPR

The table and map below are reproduced from the [EPA's Web site](#).

State	Required to Reduce Emissions of NO _x during the Ozone Season (1997 Ozone NAAQS)	Required to Reduce Annual Emissions of SO ₂ and NO _x (1997 Annual PM2.5 NAAQS)	Required to Reduce Annual Emissions of SO ₂ and NO _x (2006 24-Hour PM2.5 NAAQS)	*SO ₂ Group
Alabama	X	X	X	2
Arkansas	X			
Florida	X			
Georgia	X	X	X	2
Illinois	X	X	X	1
Indiana	X	X	X	1
Iowa	X	X	X	1
Kansas			X	2
Kentucky	X	X	X	1
Louisiana	X			
Maryland	X	X	X	1
Michigan	X	X	X	1
Minnesota			X	2
Mississippi	X			
Missouri	X	X	X	1
Nebraska			X	2
New Jersey	X		X	1
New York	X	X	X	1
North Carolina	X	X	X	1
Ohio	X	X	X	1
Oklahoma	X			
Pennsylvania	X	X	X	1
South Carolina	X	X		2
Tennessee	X	X	X	1
Texas	X	X		2
Virginia	X		X	1
West Virginia	X	X	X	1
Wisconsin	X	X	X	1
Number of States	25	18	21	

* The final CSAPR divides the states required to reduce SO₂ into two groups. Both groups must reduce their SO₂ emissions beginning in 2012. Group 1 states must make significant additional reductions in SO₂ emissions by 2014 in order to eliminate their significant contribution to air quality problems in downwind areas.



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