

Searching for certainty in uncertain air: NSR and the RMRR exclusion

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The New Source Review (NSR) program's Routine, Maintenance, Repair and Replacement (RMRR) exclusion has been the subject of much confusion and litigation for a number of years. RMRR excludes small projects from NSR that qualify as basic, routine maintenance of a facility. Since its inception in the late 1970s, the power industry has often used the exclusion for various projects in order to avoid NSR's permitting process.

But several environmental groups have alleged misuse, contending that many of these excluded projects were major modifications that increased emissions significantly. The Department of Justice (DOJ) joined the debate when it filed enforcement actions in 1999-2000 challenging the industry's use of the exclusion. The courts have been actively debating the issue ever since.

A number of opinions were issued in early 2006 that created uncertainty for industry. Utilities were handed a victory in February when a district court sided with their interpretation of what was encompassed by "routine maintenance," see *United States v. Cinergy*, No. 1:99-1693 (S.D. Ind. Feb. 16, 2006) (*Cinergy II*), but they suffered a defeat in March when the U.S. Court of Appeals for the D.C. Circuit vacated the Equipment Replacement Provision (ERP). See *New York v. EPA*, 443 F.3d 880 (D.C. Cir. 2006) (*New York II*).

ERP was a regulation promulgated by the Environmental Protection Agency (EPA) in 2003 that would have created an industry-friendly, bright-line RMRR exclusion of certain equipment-replacement projects from NSR. The victory in *Cinergy II* was significant, as it followed rulings that also sided with the industry's interpretation. But the defeat in *New York II* was just as significant, as it stymied EPA's efforts to enact a clearer rule.

Given these events, how should lawyers advise their clients in regard to the exclusion today? First, while *Cinergy II* was a significant win for industry, other courts have either been more favorable to industry or have sided with EPA's interpretation of RMRR. Thus, when assessing whether a modification triggers NSR, companies still need to explain how their activities fit within EPA's stricter interpretation.

But considering the courts' conflicting precedent and the vacatur of ERP, it would be wise for companies to avoid RMRR

altogether and focus more on the emissions increase element of NSR. Doing so will provide more certainty in seeing whether a prospective project triggers review.

Background

In 1977, Congress amended the Clean Air Act to introduce two programs that are collectively known as NSR—the Prevention of Significant Deterioration (PSD) and the Non-Attainment New Source Review (NNSR) programs. PSD and NNSR require new and existing sources to obtain permits prior to construction or major modification that provide for the installation of state-of-the-art, pollution-control technology. See 42 U.S.C. §§ 7475, 7503.

For existing sources, NSR is triggered when a company has engaged in a major modification that results in a "significant emissions increase." 40 C.F.R. 52.21(b)(2)(i). Because "modification" is defined as "any physical change," a strict interpretation of the statute would apply NSR to nearly all changes, even those that do not significantly increase emissions. As a result, EPA created RMRR, recognizing that Congress did not intend to subject every activity to the program.

While the courts have found the exclusion to be a reasonable provision, environmental groups have alleged that industry has misused RMRR by labeling as routine large-scale capital projects that require significant advance planning. For example, prior to 1999, Ohio Edison Co. undertook 11 construction projects to replace

major components at seven of its units—at a cost of approximately \$136.4 million—to increase the life and reliability of those units.

While the company contended that the projects were routine, critics asserted that these projects were too substantial to be considered ordinary upgrades. To the critics, these unregulated modifications—and the company's contention that the exclusion exempted these projects—personified the industry's approach to NSR. Similar disputes with other companies led DOJ to commence enforcement actions from 1999 to 2000 against several utilities across the country, including Ohio Edison. DOJ alleged these companies modified their facilities and significantly increased emissions without obtaining permits.

In its litigation, DOJ has contended that courts should interpret the exclusion narrowly—applying to projects that are routine at a particular unit. Under this definition, major repairs that occur only once in a facility's lifetime would not be considered routine. Industry, on the other hand, has advocated a broader interpretation—applying to projects that are routine within the industry. Here, major repairs at a facility would be considered



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routine if they also occurred at other facilities within the industry, even if the project occurred only once at the facility in question. Determining the proper standard for RMRR is important, as the industry's standard would render moot most of the enforcement actions DOJ has brought against industry.

While disagreeing about the proper interpretation, EPA and industry do agree that RMRR analysis requires a fact-intensive, case-by-case determination that takes into account numerous factors, including the project's nature, extent, frequency and cost. Industry has argued that this subjective analysis leads to uncertainty, thereby discouraging companies from modifying their facilities.

EPA promulgated ERP to attempt to provide clarity. The rule stated categorically that the replacement of components with identical or functionally equivalent components that did not exceed 20 percent of the replacement value of the unit and did not change the unit's basic-design parameters was not a modification and thus fell within the RMRR exclusion.

Thus, under ERP, an electric utility that operated a \$500 million generating unit could spend up to \$100 million a year on upgrades without being required to install new pollution-control equipment. Industry embraced the rule, but environmental groups cried foul. They alleged ERP created a gaping loophole in NSR that would allow facilities to replace entire units over multiple years without ever installing state-of-the-art technology.

Cinergy II* and *New York II

The debate over the proper interpretation of RMRR and the validity of ERP came to a head earlier this year. In February, the court in *Cinergy II* sided with industry, finding that its interpretation should prevail in determining whether a project qualified as routine. The court reasoned that precedent clearly showed that industry practices had to be considered when applying RMRR's multi-factor test. *Id.*

The ruling followed favorable rulings in two important cases in Alabama: *United States v. Alabama Power Co.*, 372 F. Supp. 2d 1283 (N.D. Ala. 2005) and *National Parks Conservation Association v. Tennessee Valley Authority*, No. 01-403 (N.D. Ala. Sep. 7, 2005). The courts there held decisively that the interpretation advanced by industry was the proper one to use in analyzing RMRR. *Cinergy II* provided additional precedent to these two cases.

A month after *Cinergy II*, however, utilities suffered a setback in *New York II* when the D.C. Circuit vacated ERP, holding in effect that the rule automatically excluded too many projects from NSR's permitting process. The decision turned on what Congress meant when it defined "modification" as "any physical change." *New York II*, 443 F.3d at 885. According to petitioners, including several states and environmental groups, the word "any" meant that the term "physical change" covered any activity that increased emissions at a source, including the replacement projects excluded by ERP. *Id.* EPA disagreed and argued the language was ambiguous. It said "physical change" was "susceptible to multiple meanings" and that its

interpretation of the term should be accorded deference. *Id.*

The court sided with the petitioners, explaining that Congress' use of the word "any" gave the term "physical change" an expansive scope that eliminated EPA's discretion to interpret it as written in ERP. *See id.* at 887. In a strongly worded rebuke, the court stated that only in a "Humpty Dumpty world" would EPA's interpretation of modification be valid. *Id.*

'Covering your bases' while seeking certainty

Lawyers and their clients can learn valuable lessons from these events.

First, despite the ruling in *Cinergy II*, industry must be careful in claiming complete victory. While the court sided with industry, it did not conclude that the interpretation advanced by industry was the sole, proper interpretation for RMRR analysis. In fact, the court held that EPA's interpretation was also relevant.

Cinergy II at 7. Moreover, *Cinergy II* is a less-decisive victory for industry when compared to the holdings in *Alabama Power*, *National Parks Conservation Association* and the recently decided *United States v. Alabama Power Co.*, No. 2:01-00152 (N.D. Ala. Aug. 14, 2006).

When one compares *Cinergy II* with the holding in *United States v. Ohio Edison Co.*, 276 F. Supp. 2d 829 (S.D. Ohio 2003) in which the court declared that EPA's narrow interpretation was justified and

reasonable, *Cinergy II* becomes just another decision in a long line of conflicting cases. Thus, to "cover one's bases" and defend its action, a company must be able to explain how a project fits within EPA's stricter interpretation. Simply relying on *Cinergy II* and the line of cases from the Northern District of Alabama may not be enough.

Second, the vacatur of ERP maintains the status quo and the subjective nature of the RMRR analysis. As a result, companies should consider another alternative when determining whether a prospective modification triggers NSR. Remember, NSR applies to major modifications that result in "a significant emissions increase." That means even if a company modifies its facility, NSR does not apply unless the modification significantly increases emissions.

More important, the emissions increase test provides clarity, as one can measure their emissions—both prior to and after the modification—and know if they are significant by comparing them to the pollutant-specific limits listed in the regulations. 40 CFR § 52.21(b)(23)(i). Of course, quantifying emissions for each project will be more expensive than simply contending that the modification is routine. This is especially so if a company complies with the recently upheld 2002 NSR reforms that require companies to monitor, report and keep records of post-modification emissions.

Focusing on the emissions increase prong rather than relying on the conflicting RMRR decisions will provide more certainty in determining whether one should pursue obtaining a pre-construction permit. Given today's NSR climate, a little certainty is a precious commodity.

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