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UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
Washington, D.C. 20460

MEMORANDUM

Subject: Emissions Trades in Nonattainment Areas
Needing but Lacking a Demonstration of Attainment

Date: August 6, 1984

From: Joseph A. Cannon
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for Air and Radiation

To: Milton Russell
Assistant Administrator
for Policy, Planning, and Evaluation

This memorandum reflects my position on emissions trading in nonattainment areas without adequate attainment demonstrations. It supplements the memorandum I sent you on March 6.

As you know, a central goal of the air program is to improve air quality so as to bring nonattainment areas into attainment expeditiously. The emissions grading policy that the Agency adopts should play a role in achieving this expeditious attainment, rather than impede progress toward that goal. Consistent with this principle, our policy on trading in nonattainment areas without adequate demonstrations must permit approval of only those trades that would produce real progress in the plan and in the air. We should neither approve nor encourage trades that represent a relaxation from what would have occurred absent the trading opportunity.

We agreed in our meetings that a workable "but-for" test is the appropriate way to accomplish this result. As I said in my March 6 memorandum, we should establish a set of criteria or indicators that the Agency would use to answer the question whether the emissions reduction yielding credit for a trade would have occurred absent the trading opportunity.

This memorandum reflects our agreement on how to define the "economic benefit" indicator. It also sets forth the other indicators that I believe should be components of the but-for test, a summary description of the baseline that should apply in these areas, a description of the "significant improvement" test, and a list of the geographic areas in which we should apply the but-for test.

I. But-For Indicators

EPA should state in the Final Emissions Trading Policy Statement that it will consider the following factors in deciding whether an emissions reduction would have occurred absent the trading opportunity:

Credit for Reductions Achieved by RACT

States often establish RACT emission limits at a level achievable by control technology or process changes under worst-case conditions. This means that in many individual applications the technology will actually reduce emissions well below RACT limits. These reductions result merely from the expected performance of the technology the State and EPA have identified as RACT. They do not result from extra or innovative control attributable to the trading opportunity. Therefore, where the facts on their face show that a trade relies on reductions resulting merely from application of RACT, we should not approve the trade. In contrast, where it is not obvious that the trade uses such reductions, we should presume that the reductions are creditable, provided they are consistent with the other guidelines described in this memorandum.

Standard Industry Practice

In some cases, the control technology that produces the emission reduction relied on for credit is different from the technology EPA previously approved as RACT, but is no different from what sources would apply under current standard industry practice. This may occur where the previous RACT determination is outdated, and the company proposing the trade has developed and used new, more efficient control techniques not because of the trading opportunity but because it is the standard industry practice to do so. Where it is obvious that the trade involves this type of emissions, reduction, we should presume that the reduction is not creditable.

Economic Benefit

EPA should not credit reductions that were motivated solely by economic benefit that would accrue independently of the trade. These reductions would have occurred anyway. However, where the desire for credit was a factor significantly contributing to the decision to make the reduction, we should presume that the reduction would not have occurred anyway, provided it is consistent with the other guidelines described in this memorandum.

Timing

An emission reduction that took place prior to submittal of an application for a trade can generally be presumed not to be creditable since it most likely would have happened anyway. The applicant may attempt to rebut this presumption. However, regardless of the timing of the reduction and the bubble application, the reduction would still need to be consistent with the other guidelines described in this memorandum.

II. Baseline

Emission reduction credit can only be given from reductions below the emission levels calculated using 1) the lowest of the State Implementation Plan (SIP) allowable or RACT¹ emission rates, and 2) the actual level of capacity utilization over the two-year period preceding application for the trade.

III. Significant Air Quality Improvement

The trade should produce an air quality improvement beyond that of the baseline. As a surrogate for determining a net air quality improvement, all trades must show a significant net emissions reduction (at least 20 percent). For trades where Level II modeling is required, there can be no increase in concentration at any site above the Level II significance range (basic Level II requirement).

IV. Applicability

Trades in the following areas are to be subject to the "but-for" test:²

- Areas that are nonattainment under Section 107 for the pollutant involved in the trade and that failed to submit a 1979 Part D attainment demonstration or that submitted one that has not yet received full EPA approval. This includes total suspended particulate (TSP) nonattainment areas that submitted a SIP that did not include an actual demonstration of attainment but still received EPA approval (e.g., a "RACT plus studies" SIP). The test does not apply in areas that have failed to get a secondary particulate plan approved.

- Extension nonattainment areas that failed to submit a 1982 SIP demonstration, or that submitted one that has not yet received EPA approval. Also included are those ozone areas that are unable to demonstrate attainment by 1987.

- Attainment and nonattainment areas that received either a 1) Section 110(a)(2)(H) notice of deficiency based on failure to attain or maintain the primary NAAQS (in the form of a SIP call or a new Section 107 or 171(2) nonattainment designation) or 2) a notice of failure to implement an approved SIP.

¹ Consistent with the first two paragraphs under Section I of this memorandum, we should use "standard industry practice" or "expected (or realized) RACT" emission rates where those rates are below the generic RACT rate and are easily identifiable.

² Of course, trades that are submitted together with a fully approvable attainment demonstration will not be subject to the "but-for" test.

□ Nonattainment areas that received notice from EPA that they have failed to meet conditions in their EPA-approved SIP's, including commitments to adopt particular regulations by specified dates. As an exception, if an area with an adequate demonstration of attainment has failed to enact or implement a required inspection and maintenance (I/M) program but has adopted all required volatile organic compound (VOC) stationary controls, the test will not apply.

³

Any area that does not have an EPA-approved demonstration for lead (or any other non-Section 107 pollutant).

I will soon send you a more detailed description of the tests we would use to identify the emission reductions that achieve progress in the plan and in the air. These criteria will be consistent with this memorandum.

Also, I must conclude that this reasoning applies even when the deficiency in the SIP relates to a single source not involved in the trade. Even in that event EPA has no assurance that the State will not need eventually to adjust the existing requirements for sources involved in the trade.

Finally, our treatment of I/M is consistent with not creating a germaneness exemption. The I/M exemption discussed above applies only to areas that, although failing to enact the statutorily required I/M program, did demonstrate that the existing control requirements with the projected I/M program will be adequate to assure attainment. Thus, we know that the existing control requirements will need no further adjustment if the State merely complies with the Act's I/M requirement.

³ We should not create a general exemption from the but-for test based on whether the deficiency in the SIP is "germane" to the sources involved in the trade. Until a State has shown that it has adopted or entered into an enforceable commitment to adopt new measures that would provide for attainment of the standards, EPA has no assurance that the stationary source controls that the State has already adopted will need no further adjustment. For that reason, in these areas we cannot safely assume that trades achieving mere equivalence to the existing stationary source requirements will serve the Act's attainment goal.