ORAL ARGUMENT HELD March 25, 2008
PANEL DECISION ISSUED JULY 11, 2008

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 05-1244 and consolidated cases

STATE OF NORTH CAROLINA, et al.,

Petitioners,

v.

UNITED STATES ENVIRONMENTAL PROTECTION AGENCY,

Respondent.

On Petition for Review of Final Action of the
United States Environmental Protection Agency

PETITION FOR REHEARING OR REHEARING EN BANC

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September 24, 2008

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UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

STATE OF NORTH CAROLINA, et al. Petitioners, v. UNITED STATES ENVIRONMENTAL PROTECTION AGENCY, Respondent.	)	Docket No. 05-1244 (and consolidated cases)

CERTIFICATE OF PARTIES

Pursuant to Circuit Rule 35(c), counsel for respondent United States Environmental Protection Agency ("EPA") submits this certificate as to parties.

(I) Parties, Intervenors, and Amici Who Appeared in the District Court

These cases are consolidated petitions for review of final agency actions, not appeals from the ruling of a district court.

(II) Parties to These Cases

Petitioners:

AES Corp. and its United States subsidiaries; AES Beaver Valley, LLC; AES Warrior Run, LLC; and Constellation Energy Group, Inc. (Nos. 05-1259 and 06-1226)

ARIPPA (Nos. 05-1249, 06-1242, and 06-1243)

City of Amarillo, Texas; Occidental Permian, Ltd.; and Southwestern Public Service Co. d/b/a Xcel Energy (Nos. 05-1260, 06-1228, and 06-1230)

Duke Energy Corp. (No. 05-1262)

Duke Power Co. LLC, d/b/a Duke Energy Carolinas, LLC (No. 06-1217)

Entergy Corp. (Nos. 05-1251, 06-1227, and 06-1229)

Florida Association of Electric Utilities (Nos. 05-1252 and 06-1235)

FPL Group, Inc. (Nos. 05-1253, 06-1240, and 06-1241)

Inter-Power/AhlCon Partners (No. 06-1245)

Minnesota Power, a Division of ALLETE, Inc. (Nos. 05-1246 and 06-1238)

Northern Indiana Public Service Co. (No. 05-1254)

South Carolina Electric & Gas Co. (Nos. 05-1256, 06-1222, and 06-1224)

South Carolina Public Service Authority and JEA (Nos. 05-1250, 06-1236, and 06-1237)

State of North Carolina (Nos. 05-1244, 06-1232, and 06-1233)

Respondent:

United States Environmental Protection Agency (all cases)

Amici:

States of Connecticut, New York, New Jersey, Delaware, Illinois, Massachusetts, Maryland, New Hampshire, New Mexico, and Rhode Island, and Washington, D.C.

Commonwealth of Pennsylvania

Tennessee Valley Authority

Intervenors for Respondent:

Environmental Defense

Midwest Generation, LLC

National Mining Association

Natural Resources Defense Council, Inc.

Ohio Environmental Council

U.S. Public Interest Research Group

Utility Air Regulatory Group

Alabama Power Company

There are no Intervenors for Petitioners.

Respectfully submitted,

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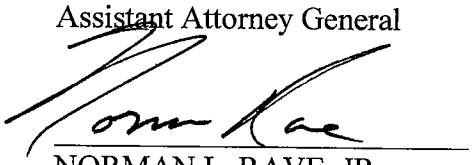

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INTRODUCTION

Respondent United States Environmental Protection Agency ("EPA") seeks rehearing *en banc*, or in the alternative, Panel rehearing of the Panel's vacatur of the Clean Air Interstate Rule ("CAIR") and its associated Federal Implementation Plans. (Decision attached as Attachment 1). EPA is not seeking further review of the Panel's holdings with regard to "interference with maintenance," the 2015 date for full implementation of CAIR, or inclusion of Minnesota in CAIR.[1] Thus, EPA recognizes that a remand of CAIR is required. However, EPA seeks rehearing or rehearing *en banc* of the Panel's holding that CAIR must be vacated. The issue of remedy was not addressed in the briefs; thus the Panel did not have the opportunity to consider the public health, environmental, and economic harms that will result from vacatur of CAIR, including tens of thousands of premature deaths, heart attacks, emergency room visits, and lost school and work days. Furthermore, the Panel's holding is based on the apparent belief that CAIR's regional trading approach was significantly different from the one upheld by this Court in Michigan v. EPA, 213 F.3d 663 (D.C. Cir. 2000). The Panel's decision turns primarily on the fundamental legality of using an interstate trading program to address the requirements of Clean Air Act section 110(a)(2)(D)(i), 42 U.S.C. § 7401(a)(2)(D)(i), an issue no party contested. Thus the issue was not addressed in EPA's brief. As a result, there is significant information in the record not presented to the Panel demonstrating that the CAIR trading program used the same fundamental approach approved by Michigan. EPA also seeks rehearing *en banc* of the Panel's holding that EPA lacks authority to require sources to surrender allowances created under CAA Title IV to comply with the requirements of CAIR.

En banc consideration is merited under Rule 35. Alternatively, panel rehearing is merited under Rule 40. Consideration of the full record demonstrates that the Panel's decision is

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[1] As discussed below, these issues can be addressed by EPA on remand while CAIR is being implemented. With regard to the 2015 date for the second phase of CAIR, EPA believes that, upon reconsideration, it may be able to present additional information sufficient to demonstrate that CAIR would eliminate significant contribution as expeditiously as practicable. Slip Op. at 59. For example, because of the incentives created by a cap-and-trade program, the second phase of CAIR will achieve significant additional emission reductions that contribute to attainment *prior* to 2015. This issue was not briefed and thus not considered by the Panel.

inconsistent with a prior decision of the Court. The petition also presents questions of exceptional importance. Vacatur will eliminate substantial emission reductions that would have been achieved by CAIR wiping out the accompanying public health benefits of decreases in illness and premature death and significantly disrupting efforts by eastern States to meet national ambient air quality standards. The Panel's decision has also upended the settled expectations upon which substantial investment in control equipment and allowances has already been made, resulting in losses of billions of dollars to regulated companies. The Panel's decision also hamstrings EPA's ability to utilize trading programs to deal with broad-scale regional pollution problems, which prevents EPA from getting the greatest emissions reductions because trading programs get such reductions in the most efficient, least costly manner.

BACKGROUND

I. STATUTORY AND REGULATORY BACKGROUND

EPA promulgated CAIR to address the interstate transport of pollutants that significantly contribute to nonattainment of the National Ambient Air Quality Standards ("NAAQS") for ozone and particulate matter ("PM") in downwind States. The statutory authority for CAIR is section 110(a)(2)(D)(i) of the Clean Air Act (42 U.S.C. § 7410(a)(2)(D)(i)), which provides that States must include in their State Implementation Plans ("SIPs") provisions:

> (i) prohibiting . . . any source or other type of emissions activity within the State from emitting any air pollutant in amounts which will -- (I) contribute significantly to nonattainment in, or interfere with maintenance by, any other State with respect to any such national primary or secondary [NAAQS].

In determining whether emissions from one State "contribute significantly" to nonattainment in another State, EPA considers whether emissions from one State contribute to nonattainment concentrations of pollutants in another State by amounts that meet or exceed specific criteria and then determines how much those emissions can be reduced by the application of highly cost-effective controls. EPA's use of economic factors in determining what contribution must be eliminated was upheld by this Court in reviewing the "NOx SIP Call,"

which like CAIR established a regional trading program to eliminate the significant contributions of upwind States to nonattainment in downwind States. Michigan, 213 F.3d 663.

In CAIR, EPA determined that impacts of emissions from 29 jurisdictions in the eastern United States exceeded the air quality criteria for a finding of significant contribution. The Agency determined the emissions reductions that could be achieved for sulfur dioxide ("SO_2") (a PM precursor) and nitrogen oxides ("NOx") (a PM and ozone precursor) using controls determined to be highly cost-effective, assuming the existence of an emissions trading program for these pollutants among the States subject to CAIR.

In establishing the CAIR trading program for SO_2, EPA utilized the existing SO_2 allowances created and allocated to sources in each State by Title IV of the Clean Air Act. In States subject to CAIR, covered electric generating units ("EGUs") would have to surrender two Title IV SO_2 allowances (which under Title IV authorize the emission of one ton of SO_2) for each ton of SO_2 emitted during the years 2010 to 2014 and surrender 2.86 Title IV SO_2 allowances for each ton of SO_2 emitted thereafter. In establishing new trading programs for annual and ozone-season NOx emissions, EPA developed state budgets based on each State's share of regionwide recent historic heat input to EGUs, multiplying each source's heat input by a fuel factor (1.0 for coal, 0.6 for oil, and 0.4 for natural gas) to better reflect actual emissions.

II. SUMMARY OF THE PANEL DECISION

The Panel held that CAIR's unrestricted trading program is unlawful because it does not adequately address the requirement that States eliminate significant contribution to nonattainment in or interference with maintenance by other States from sources "within the State." Slip Op. at 16. It also held that EPA's method for allocating SO_2 allowances is unlawful because (1) EPA's decision to use existing allowances to preserve the Title IV program is based on a factor that is unrelated to the amount by which upwind States significantly contribute to downwind nonattainment, and (2) EPA has no legal authority under section 110(a)(2)(D) to require the surrender of Title IV allowances for compliance with a Title I requirement. Id. at

33-37, 42-45. Similarly, the Panel held that EPA's method for determining State NOx budgets (i.e., adjusting allowances for each State based on the fuel mix used by utilities in the State) is unlawful. Equity between types of sources is unrelated to the amount by which upwind States significantly contribute to downwind nonattainment and so is an improper factor to consider. Id. at 37-42.

The Panel also held that EPA improperly failed to consider North Carolina's claim that additional States should be included in CAIR to prevent interference with maintenance of the ozone standard in North Carolina, Slip Op. at 18-22, that EPA improperly used 2015 as the date for requiring full compliance with CAIR, id. at 22-25, and that EPA did not adequately address claims by Minnesota utilities that EPA had overestimated emissions from Minnesota. Id. at 52-56. The Panel held that EPA properly used 2010 as the relevant date for considering which upwind States made a significant contribution to downwind nonattainment, id. at 27-29. The Court also rejected a challenge to EPA's decision to move the first phase of the NOx requirements to 2009, id. at 56-57, and rejected challenges to EPA's criteria for determining which upwind States should be subject to CAIR requirements. It rejected claims by Texas and Florida that CAIR should apply to only a portion of those States. Id. at 29-32, 46-52.

Finally, the Panel held that CAIR must be vacated, rather than remanded, because the rule is "fundamentally flawed" and "very little will survive[ ] remand in anything approaching recognizable form." Slip Op. at 58-59.

STANDARD FOR *EN BANC* REVIEW

The Federal Rules of Appellate Procedure provide that rehearing *en banc* may be ordered where: "(1) *En banc* consideration is necessary to secure or maintain uniformity of the court's decisions; or (2) The proceeding involves a question of exceptional importance." Fed. R. App. P. 35(a). Panel rehearing or rehearing *en banc* is warranted here because vacatur of CAIR will result in significant environmental and economic harm and will seriously impede EPA's ability to implement the requirements of the Clean Air Act, because the decision is in conflict with the

Court's prior decision in Michigan, and because the Panel did not entertain argument on a number of significant issues it resolved.

ARGUMENT

I. THE PANEL ERRED IN DETERMINING THAT CAIR MUST BE VACATED

In determining to vacate, rather than remand, CAIR, the Panel relied on the two-part test of Allied-Signal, Inc. v. U.S. Nuclear Regulatory Comm'n, 988 F.2d 146, 150-51 (D.C. Cir. 1993), that such a decision "depends on the 'seriousness of the order's deficiencies (and thus the extent of doubt whether the agency chose correctly) and the disruptive consequences of an interim change.'" Slip Op. at 58. Rehearing is required on the Panel's application of both prongs of this test. The Panel's determination that CAIR is "fundamentally flawed," Slip Op. at 59, is based on an incomplete view of the record, which resulted in a fundamental misunderstanding of the similarities between CAIR and the very similar NOx SIP Call Rule that the Court upheld in Michigan. The "disruptive consequences" of vacating CAIR are extreme, compromising public health and state air pollution control efforts, and yet were not briefed by any party.

A. The Panel Erred In Holding That CAIR Is "Fundamentally Flawed."

In Michigan, this Court upheld the NOx SIP Call, a regional approach to addressing interstate contributions to nonattainment implemented through an emissions trading program. In the NOx SIP Call, EPA determined that reducing emissions from all contributing States collectively would satisfy each State's requirement to eliminate its significant contribution to nonattainment in other States. Thus, EPA developed a region-wide emissions budget based on the amount of emission reductions that could be achieved through the application of highly cost-effective controls. Each covered State's portion of that budget was based on EGU heat input adjusted by a growth factor. On review, this Court generally upheld the NOx SIP Call, rejecting claims that it was invalid because it used economic considerations in determining what constituted "significant contribution" or because it did not correlate the level of emission

reductions required from each State to that State's impact on downwind nonattainment. 213 F.3d at 674-80.

EPA took a similar regional approach in CAIR. The Agency determined that region-wide reductions in emissions of SO_2 and NOx would eliminate the significant contribution of all States in the CAIR region to nonattainment in downwind States. EPA then determined a region-wide budget based on the application of highly cost-effective controls and allocated that budget to the States. No party in this case challenged EPA's authority to use a trading program to address significant contribution to downwind nonattainment. While the State of North Carolina challenged the lack of any limitations on trading, it specifically stated that "North Carolina does not submit that any trading is *per se* unlawful." NC Br. at 33. Thus, because no petitioner challenged EPA's authority to utilize a trading program, and because that issue had been favorably resolved in Michigan, EPA did not address the question in its briefs but limited its discussion to the narrow issue presented by petitioner, i.e., whether some limitation on the amount of trading that can occur (such as the limits on the use of banked allowances in the NOx SIP Call) was necessary. Because the fundamental basis of the Panel's decision is an issue that was not raised by petitioners and not briefed by EPA, rehearing is necessary to give EPA an opportunity to present both the legal and the factual basis for EPA's determination that the CAIR regional trading program already addresses the significant contribution of each State in the region to nonattainment in other States. For example, the record contains data demonstrating that emissions from all States in the CAIR region affect ozone and PM concentrations in States throughout the region. The record also contains data not considered by the Panel demonstrating the air quality benefits in reduced ambient pollution concentrations anticipated throughout the region from the emission reductions required by CAIR.

The Panel's attempt to distinguish Michigan appears to be based on a misunderstanding of either the NOx SIP Call, CAIR, or both. The Panel asserts that "the similarities with the NOx SIP Call are only superficial." Slip Op. at 59. However, EPA used the same fundamental

approach – a regional emissions cap and a trading program to address upwind States' significant contribution to downwind nonattainment – in both rules. Further, the Panel places inappropriate emphasis on the Michigan Court's statement that it was "able to assume the existence of EPA's allowance trading program only because no one has challenged its adoption." Slip Op. at 17, quoting Michigan, 213 F.3d at 676. In fact, the Michigan Court considered and rejected arguments that the NOx SIP Call's trading program was inconsistent with the section 110(a)(2)(D) requirement to eliminate each individual State's significant contribution. See Michigan, Brief of Petitioning States at 43 ("EPA's position that the NOx emissions budget for each of the 23 States represents those emission reductions 'necessary' to remedy the State's alleged significant contribution to regional ozone transport is also contradicted by the 23-State NOx trading program contained within the same rule."). Of direct relevance to the Panel's decision, petitioners in Michigan argued that EPA lacked authority to create a cap-and-trade program, that the trading program would allow sources to trade allowances regardless of the resulting impact of their emissions on concentrations of ambient ozone throughout the region, and that several of the States were expected to "exceed their supposedly 'necessary' emissions cap." Id. at 43 n.19, 45.

The Michigan Court rejected these arguments, recognizing and approving EPA's regional approach to emission reductions and its use of a trading program that would allow some States to exceed their budgets. 213 F.3d at 686-87. In upholding the NOx SIP Call against these challenges, the Court thus necessarily decided and rejected petitioners' challenges to interstate trading. American Iron & Steel Inst. v. EPA, 886 F.2d 390, 397 (D.C. Cir. 1989) ("[T]he outcome of the case . . . necessarily constituted a rejection of the claims [in the briefs].") Because the Michigan court necessarily considered and rejected claims that EPA lacks authority to allow States to eliminate their significant contribution to downwind nonattainment by participation in a trading program, the Panel's vacatur of CAIR on that ground is inconsistent, and rehearing "is necessary to secure or maintain uniformity of the court's decisions."

The Panel's reliance on the reference in section 110(a)(2)(D)(i) to sources "within the State" as the basis for its holding that CAIR is unlawful, Slip Op. at 16, is similarly misplaced. Section 110 is directed to States and contains the requirements that States must include in their implementation plans. Section 110(a)(2)(D) contains the specific requirement that in developing its plan, a State must ensure that sources do not significantly contribute to nonattainment or interfere with maintenance in another State. The language "within the State" is included for clarity to contrast with the phrase "any other State" in subsections (I) and (II). Given this straightforward grammatical construction, there is no basis to conclude that Congress intended the phrase to preclude EPA from adopting a trading program to deal collectively with upwind States' significant contribution. Moreover, the Panel's reading of the phrase is inconsistent with the Court's holding in Michigan that EPA may take a regional approach to addressing significant contribution and need not tie each State's budgets directly to its impact on downwind States.

Furthermore, section 110(a)(2)(D)(i)(I) requires States to have adequate provisions in their implementation plans prohibiting sources within the State from emitting pollutants in amounts that will significantly contribute to nonattainment or interfere with maintenance in another State. Where EPA has determined that participation in a regional trading program will eliminate the significant contribution of States in the program to nonattainment in other States, each such State complies with the statutory requirement by ensuring that all covered sources within the State hold allowances equal to their emissions, which requires the sources to either reduce their emissions or to acquire allowances from other sources within the region that result from emission reductions at those sources. In either event, the significant contribution to downwind nonattainment coming from within the participating States has been eliminated.[2/]

[2/] The Panel also based its holding on a concern that CAIR would eliminate a State's ability to seek further relief under CAA section 126 if necessary. Slip Op. at 17. This concern is based on a misunderstanding of EPA's position. Although EPA denied a petition by North Carolina that was based on the level of contribution shown in the CAIR record, EPA has made clear that post-CAIR developments can be the basis for a section 126 petition, giving as an example a Section 126 Petition presenting information showing that there is a different level of contribution

(continued...)

With the exception of the issue discussed below concerning EPA's legal authority to terminate or limit Title IV allowances in implementing a program under Title I, the Panel's holdings concerning EPA's methodologies for determining State SO_2 and NOx budgets are derived from its holding that participation in a cap-and-trade program does not meet the State's obligations under section 110(a)(2)(D)(i). Specifically, because the Panel held that EPA must require each State to achieve emission reductions "within the State," the Panel held that a method of determining State budgets on any other basis is unlawful. As demonstrated above, rehearing is required on the Panel's vacatur of CAIR because its central holding is based on issues that EPA did not have an opportunity to address and because that holding conflicts with this Court's opinion in Michigan. Because that central holding must be reconsidered, the Panel's subsidiary holdings on allowance allocations must be reconsidered as well.

The record clearly demonstrates the appropriateness of the CAIR State budget distribution schemes. The Panel questions "how the quantitative number of allowances created by 1990 legislation to address one substance, acid rain, could be relevant to 2015 levels of an air pollutant, $PM_{2.5}$." Slip Op. at 35. However, no one in this litigation disputed that regulating SO_2, a $PM_{2.5}$ precursor, is appropriate. In addition, the record demonstrates that there is a close relationship between the current allocation of Title IV allowances among States and actual SO_2 emissions (without CAIR) in each State. Thus, the allocation of Title IV allowances is a reasonable starting point for calculating the required emissions reductions. Moreover, the record demonstrates that the differences between alternative methods for allocating SO_2 allowances are not very substantial. Thus, even if the Court were to determine, after rehearing, that the allocation method is arbitrary or capricious, any inequity resulting from leaving it in place during remand is outweighed by the significant harms resulting from vacatur of CAIR described below.

[2/](...continued)
than EPA analyzed in CAIR. 71 Fed. Reg. 25, 328, 25,335 n.6 (Apr. 28, 2006).

The same is true of the methodology used to establish State NOx budgets. While the Panel focuses on the differential cost of controlling different types of EGUs, the Panel does not appear to have considered the fact that the fuel factors represent the relative emissions of NOx from facilities fired with different types of fuel. Thus, the allowance methodology utilized in CAIR more closely approximates emissions of NOx – and thus each State's significant contribution – than an allocation methodology based only on heat input, such as that utilized in the NOx SIP Call. The record further demonstrates that differences in initial allocations resulting from different allocation schemes are relatively minor for most States. Thus, even if the Court believes further explanation or revision is required, the methodology should remain in place on remand to allow EPA to make any necessary modifications while avoiding the very serious near term health and air quality problems resulting from vacatur. In addition, the SO_2, annual NOx and ozone season NOx trading programs are severable from each other, and vacatur of one need not lead to vacatur of all three programs.

That EPA is not seeking rehearing on all issues does not require vacatur of CAIR. If EPA, after consideration of the Panel's holdings on "interference with maintenance" and of the 2015 date for the final CAIR requirements, Slip Op. at 18-25, determines either that more States should be added to CAIR or that greater emission reductions are required, the program could be modified to incorporate those changes, and there is no reason not to obtain the significant benefits of the existing CAIR program in the interim. With regard to inclusion of Minnesota in CAIR, vacatur is not necessary because the Panel remanded for further explanation. Id. at 56.

B. Vacatur Of CAIR Will Result In Significant Harms.

The issue of remedy was not briefed in this case. Therefore, the Panel did not have before it an analysis of the environmental benefits of CAIR and the extremely disruptive consequences of vacatur. Most significantly, vacatur will jeopardize the massive emission reductions that were being achieved and expected to be achieved with CAIR and the accompanying improvements in public health. EPA has estimated that CAIR would prevent

13,000 deaths annually by 2010 and 17,000 premature deaths annually by 2015. CAIR would reduce annual SO2 emissions by 4.3 million tons, or 45% from 2003 levels, by 2010, and annual NOx emissions by 1.7 million tons or 53% from 2003 levels by 2009. Additional reductions would be achieved by 2015. Vacatur of CAIR will likely cause these significant emission reductions to be delayed or foregone, causing thousands of cases of illness or premature death. Declaration of Brian McLean (Attachment 2). Vacatur will also significantly disrupt state efforts to achieve the requirements of the Clean Air Act related to regional haze and ambient levels of ozone and $PM_{2.5}$. Declaration of William Harnett (Attachment 3).

The Panel's suggestion that the negative environmental consequences of vacatur might be offset by the continuation of the NOx Budget Trading program under the NOx SIP Call fails to recognize that the vast majority (about 90%) of the health benefits from CAIR arise from reductions in SO_2, which are not addressed by the NOx SIP Call. Nor does the NOx SIP Call address winter NOx emissions. Moreover, the NOx SIP Call trading program requirements have been eliminated in many States by State regulation, meaning the program cannot automatically spring back to life upon vacatur of CAIR. McLean Decl. ¶ 17. The Panel's further suggestion that section 126 may provide an interim remedy overlooks the fact that any such relief would occur years after the first CAIR compliance dates given the length of time required for States to prepare petitions and for EPA to address them, and the three-year compliance window for individual sources afforded by section 126(c), 42 U.S.C. § 7426(c).

Vacatur of CAIR will also have significant economic impacts, penalizing companies that acted early to reduce pollution. Billions of dollars were spent by utilities installing controls in anticipation of the effective date of CAIR. If CAIR is vacated, it is unclear if those controls will be operated and whether utilities will be authorized, or able, to recover the capital and operating costs of those controls. Vacatur will also destroy or reduce the value of the banked allowances that companies generated through early emission reductions. The price of Title IV SO_2 allowances declined from approximately $600 per ton before oral argument in this case, to $300

following the argument. It then plummeted to less than $100 after the decision, and has stabilized at approximately $150. This means that the 6.9 million tons of banked Title IV allowances have lost over three billion dollars in value. Such precipitous declines in allowance values will lead to companies slowing or stopping installation of controls, reducing or stopping operation of previously installed controls, and reducing use of other emission reduction strategies.

II. THE PANEL ERRED IN HOLDING THAT EPA LACKS AUTHORITY TO TERMINATE OR LIMIT TITLE IV ALLOWANCES IN IMPLEMENTING A PROGRAM PROMULGATED PURSUANT TO TITLE I

Rehearing or rehearing *en banc* is also warranted on the Panel's decision that EPA cannot terminate or limit Title IV SO_2 allowances to implement CAIR because the Panel's reading of the Clean Air Act is inconsistent with fundamental principles of statutory interpretation. The Panel's decision disregards the provisions in CAA section 403(f), 42 U.S.C. § 7651b(f), that SO_2 control requirements promulgated pursuant to CAA Title I can require sources to limit their SO_2 emissions below the levels permitted by the numbers of allowances they hold. As a result, the Panel's decision precludes EPA from reconciling the Act's mandates that the Agency both require sufficient reductions in SO_2 emissions under section 110 to meet the NAAQS and ensure a viable allowance program under Title IV, a reconciliation that Congress specifically provided for in section 403(f).

Title IV, which was added to the CAA by the 1990 Amendments to address the problem of acid rain, creates a cap-and-trade program for SO_2 emissions from EGUs with allowance allocations established by the statute. However, Congress recognized that more stringent regulation of SO_2 emissions might ultimately be required to respond to other public health or environmental risks and therefore included language to address it in section 403(f) of the Act.

Section 403(f) provides in relevant part:

> An allowance allocated under this subchapter is a limited authorization to emit sulfur dioxide in accordance with the provisions of this subchapter. Such allowance does not constitute a property right. Nothing in this subchapter or in any other provision of law shall be construed to limit the authority of the United

> States to terminate or limit such authorization. Nothing in this section relating to allowances shall be construed as affecting the application of, or compliance with, any other provision of this chapter to an affected unit or source, including the provisions related to applicable [NAAQS] and State implementation plans . . . .

42 U.S.C. § 7651b(f). The first three sentences of this section demonstrate that Congress meant to be very clear that Title IV allowances are not a property right or any other sort of irrevocable grant, but rather are a "limited authorization" to emit SO_2 that the United States may limit or terminate. Because EPA is an agency of the United States,[3/] EPA may limit or terminate Title IV allowances in appropriate circumstances. Furthermore, the legislative history suggests that one of the purposes of section 403(f) was to provide that EPA could limit or eliminate Title IV allowances if appropriate in implementing its broad authorities under the Act. Language in an earlier House Bill providing that allowances could be terminated or limited "by Act of Congress" and "may not be extinguished by the Administrator" was deleted from the final legislation. See H. Rep. 101-490, pt.1, at102 (1990) (proposed section 503(f)), reprinted in 2 A Legislative History of the Clean Air Act Amendments of 1990, at 3126 (Comm. Print 1993) ("Legislative History"). As explained in a floor statement by a Senate conference manager explaining the final legislation, allowances can be terminated or limited by Congress or the Administrator and "are but the means of implementing an emissions limitation program, which can be altered in response to changes in the environment or for other sound reasons of public policy. S. Debate, Conf. Rep., Oct. 27, 1990, 1 Legislative History at 1034. But see 136 Cong. Rec. E 3672 (daily ed. Nov. 2, 1990) (extension of remarks of Rep. Michael Oxley expressing contrary view). EPA's interpretation of this ambiguous statutory language and legislative history is reasonable, see 70 Fed. Reg. at 25291, n.137. The Panel's decision is inconsistent with EPA's reasonable reading of the statute.

[3/]The term "United States" is a broad term that is never used to mean only Congress in the CAA. Compare 42 U.S.C. §§ 7402(c) and 7589(e)(3) (referencing "Congress") with 42 U.S.C. §§ 7411(b)(4), 7413(a)(3), (b)(2), (c)(1), (c)(3), (d)(1)(B), 7417(b), 7418(a), 7602(e), 7604(a)(1), (e) (referencing "United States" in contexts where it logically cannot mean only Congress).

The Panel's holding is also inconsistent with the final quoted sentence, which it did not address. That sentence states that, in exercising its authority concerning the NAAQS and SIPs, EPA is not limited by the Title IV allowance authorization provisions. This provision applies squarely to CAIR where EPA determined that additional controls on SO_2 emissions are necessary to eliminate the significant contributions of upwind States to nonattainment in other States, and relied on its broad authority under CAA sections 110 and 301 to provide criteria for the review of SIPs to help ensure they meet CAA requirements, including the requirements of section 110(a)(2)(D). See 42 U.S.C. §§ 7410(k)(5), 7601.

In doing so EPA was also cognizant of the congressional directive to promote "orderly and competitive functioning of the [Title IV] allowance system," 42 U.S.C. § 7651b(d)(1), and Congress' recognition that the allowances were "intended to function like a currency that is sufficiently valuable to stimulate . . . [emission control] efforts." See S. Rep. No.101-228 (1990), 5 Legislative History at 8664. In order to reconcile its competing statutory obligations, i.e., to require more stringent regulation of SO_2 under section 110(a)(2)(D) while ensuring a viable allowance trading system under Title IV, EPA required that Title IV allowances be used and terminated to satisfy the requirements of CAIR.

The Panel recognized that "it may be reasonable for EPA, in structuring" the optional trading program "to consider the impact on the Title IV [allowance] market," Op. at 44. However, the Panel made it impossible for EPA to do that by holding that EPA had no legal authority under section 110(a)(2)(D) to require the termination of Title IV allowances to eliminate interstate contribution to nonattainment. The Panel failed to recognize that Congress, in the fourth sentence of section 403(f), had given primacy to EPA's responsibility to require SIPs to achieve the emission reductions necessary to attain the NAAQS. Furthermore, this fourth sentence must be read in conjunction with the rest of section 403(f), which specifically states that the United States may limit or eliminate Title IV allowances.

The Panel's decision is inconsistent with basic principles of statutory interpretation. The Court owes deference to EPA's interpretation of an ambiguous statute. Chevron U.S.A., Inc. v. NRDC, 467 U.S. 837, 842-43 (1984). It is unreasonable to hold that Congress would have recognized EPA's authority to limit a facility's ability to emit SO_2 below the level of allowances held by the facility, while at the same time depriving EPA of the ability to use that authority in a way that ensures that the congressionally-mandated Title IV program is not eviscerated. It is reasonable to read the Act, as EPA has, to give EPA the authority to modify Title IV allowances in the course of implementing its Title I authority if necessary to reconcile the goals of the two provisions. As this Court has previously recognized agencies have inherent authority to reconcile contradictory statutory requirements. See Atwell v. Merit Sys. Prot. Bd., 670 F.2d 272, 286 (D.C. Cir. 1981); Citizens to Save Spenser County v. EPA, 600 F.2d 844, 870-71 (D.C. Cir. 1979). In this case, that authority was specifically confirmed by Congress by including section 403(f) in the statute. Because the Panel failed to properly defer to EPA's reasonable interpretation of the Clean Air Act, rehearing or rehearing *en banc* is appropriate.

CONCLUSION

Because the Panel in deciding to vacate CAIR did not consider the full record before EPA resulting in its opinion being inconsistent with this Court's decision in Michigan, and did not consider the substantial public health, environmental, and economic harms resulting from vacatur, Panel rehearing or rehearing *en banc* on the question of vacatur should be granted to allow EPA to properly address those issues, either through further briefing and argument, or on remand without vacatur. The Panel's decision that EPA lacks authority to terminate or limit Title IV allowances in implementing CAIR is inconsistent with basic principles of statutory interpretation and should be reheard or reheard *en banc*.

Respectfully submitted,

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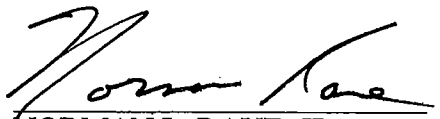

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September 24, 2008

CERTIFICATE OF SERVICE

I hereby certify that on this 24th day of September, 2008, I caused a true and correct copy of the foregoing Respondent EPA's Petition for Rehearing or Rehearing En Banc to be served by first class mail, postage-prepaid, on the following:

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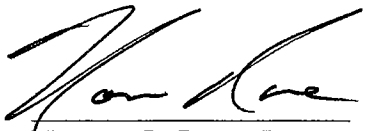

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