Appendix A

Guidance Memorandum on Developing Fee Programs Required by Clean Air Act Section 185 for the 1-hour Ozone NAAQS

UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
RESEARCH TRIANGLE PARK, NC 27711

JAN 0 5 2010

OFFICE OF
AIR QUALITY PLANNING
AND STANDARDS

MEMORANDUM

SUBJECT: Guidance on Developing Fee Programs Required by Clean Air Act Section 185 for the 1-hour Ozone NAAQS

FROM: Stephen D. Page, Director
Office of Air Quality Planning and Standards

TO: Regional Air Division Directors, Regions I-X

Section 185 of the Clean Air Act (CAA) requires states with ozone nonattainment areas classified as Severe or Extreme to develop, as a revision to their state implementation plan (SIP), a fee collection rule to be implemented in the event that an area fails to attain the ozone standards by the required attainment date.[1] This memorandum provides additional guidance on fee collection programs for the 1-hour ozone National Ambient Air Quality Standard (NAAQS or standard), which are required as anti-backsliding measures during transition to the 1997 8-hour ozone standard.

Applicability of Section 185 to Ozone NAAQS Nonattainment Areas

The section 185 fee program requirement applies to any ozone nonattainment area that is classified as Severe or Extreme under the NAAQS, including any area that was classified Severe or Extreme under the 1-hour ozone NAAQS as of the effective date of the area's 8-hour designation.[2] The EPA had previously waived the section 185 fee program requirements applicable under the revoked 1-hour ozone NAAQS in rules issued to address the transition from the 1-hour standard to the 1997 8-hour standard.[3] However, on December 23, 2006, the United States Court of Appeals for the District of Columbia Circuit issued an opinion determining that EPA improperly waived the application of the section 185 fee provision for Severe and Extreme nonattainment areas that failed to attain the 1-hour ozone standard by their attainment date. South Coast Air Quality Management District v. EPA, 472 F.3d 882 (D.C. Cir. 2006).

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[1] See Attachment A for the text of CAA section 185. The CAA requires that fee program SIPs for nonattainment areas initially classified as Severe or Extreme for the 1-hour ozone standard be submitted to EPA by December 31, 2000 (see CAA section 182(d)(3)). Areas subsequently reclassified as Severe or Extreme have a SIP submission date as determined by EPA.

[2] The 1-hour ozone NAAQS were established in 1982 and revoked on June 15, 2004 for most areas. The 8-hour ozone NAAQS were first established in 1997. EPA is currently reconsidering the 8-hour ozone NAAQS that was last revised in 2008. EPA intends to complete the reconsideration by August 31, 2010.

[3] See 69 Fed Reg 23951 (April 30, 2004).

Summary of Section 185 Requirements

In the event that a nonattainment area classified as Severe or Extreme fails to attain the ozone standard by the required date, section 185 of the CAA requires each major stationary source of volatile organic compounds (VOC) and nitrogen oxides (NOx)[4] located in such area to pay a fee to the state for each calendar year following the attainment year for emissions above a "baseline amount." In 1990, the CAA set the fee as $5,000 per ton of VOC and NOx emitted by the source during the calendar year in excess of 80 percent of the "baseline amount." The fee must be adjusted for inflation based on the Consumer Price Index (CPI) on an annual basis. Attachment B sets forth the fees, as adjusted for inflation, for the years 1990-2009.

The CAA provides that the computation of a source's "baseline amount" must be the lower of the amount of actual or allowable emissions under the permit applicable to the source (or if no permit has been issued for the attainment year, the amount of VOC and NOx emissions allowed under the applicable implementation plan) during the attainment year. The CAA also provides that EPA may issue guidance on the calculation of the "baseline amount" as the lower of the average actual emissions or average allowable emissions over a period of more than one year in cases where a "source's emissions are irregular, cyclical or otherwise vary significantly from year to year." Accordingly, on March 21, 2008, EPA issued a memorandum entitled "Guidance on Establishing Emissions Baselines under Section 185 of the CAA for Severe and Extreme Ozone Nonattainment Areas that Fail to Attain the 1-hour Ozone NAAQS by their Attainment Date."

The CAA does not specify how states may spend or allocate the fees collected under a section 185 fee program. Therefore, states have discretion on how to use the fees. We believe that one beneficial approach would be to channel the fees into innovative programs to provide incentives for additional ozone precursor emissions reductions from stationary or mobile sources, or for other purposes aimed at reducing ambient ozone concentrations in the affected area.

If the state fails to adopt or implement a required fee program, EPA is required to collect the unpaid fees and may also collect interest on any unpaid fees. All revenue collected by EPA under authority of section 185 is required to be deposited in a special fund in the United States Treasury for licensing and other services and may be used to fund the Agency's activities for collecting such fees. See, CAA sections 185(d) and 502(b)(3)(C).

Alternatives to Section 185 Fee Programs

As a result of the 2006 court decision in South Coast, states with areas classified as Severe or Extreme nonattainment for the 1-hour ozone standard at the time of the initial nonattainment designation for the 8-hour standard are subject to the requirements of section 185. We believe states can meet this obligation through a SIP revision containing either the fee program prescribed in section 185, or an equivalent alternative program, as further explained

[4] While section 185 expressly mentions only VOC, section 182(f) extends the application of this provision to NOx, by providing that "plan provisions required under [subpart D] for major stationary sources of [VOC] shall also apply to major stationary sources...of [NOx]."

below. EPA believes that an alternative program may be acceptable if it is consistent with the principles of section 172(e) of the CAA, which allows EPA through rulemaking to accept alternative programs that are "not less stringent" where EPA has revised the NAAQS to make it less stringent. This discretion does not currently apply to a section 185 fee program obligation arising from failure to attain the 1997 8-hour ozone NAAQS by the attainment date associated with a Severe or Extreme classification for that NAAQS because that NAAQS has not been revoked.

Section 172(e) is an anti-backsliding provision of the CAA that requires EPA to develop regulations to ensure that controls are "not less stringent" than those that applied prior to relaxing a standard where EPA has revised a NAAQS to make it less stringent. In the implementation rule for the 1997 ozone NAAQS, EPA determined that although section 172(e) does not directly apply where EPA has strengthened the NAAQS, as it did in 1997, it was reasonable to apply the same principle for the transition from the 1-hour NAAQS to the 1997 8-hour NAAQS. As part of applying the principle in section 172(e) for purposes of the transition from the 1-hour standard to the 1997 8-hour standard, EPA can either require states to retain programs that applied for purposes of the 1-hour standard, or alternatively can allow states flexibility to adopt alternative programs, but only if such alternatives are "not less stringent" than the mandated program.

EPA is electing to consider alternative programs to satisfy the section 185 fee program SIP revision requirement. The remainder of this memorandum describes the circumstances under which we believe we can approve an alternative program that is "no less stringent." These interpretations will only be finalized through EPA actions taken under notice-and-comment rulemaking to address the fee program obligations associated with each applicable nonattainment area. If a state chooses to adopt an alternative program to the section 185 fee program, the state must demonstrate that the alternative program is no less stringent than the otherwise applicable section 185 fee program. If our preliminary assessment indicates that the alternative program is not less stringent, we would issue a notice in the Federal Register proposing to make such a determination at the same time we propose and take action on any accompanying SIP revision pursuant to section 110(k).

EPA believes that for an area that we determine is attaining either the 1-hour or 1997 8-hour ozone NAAQS, based on permanent and enforceable emissions reductions, the area would no longer be obligated to submit a fee program SIP revision to satisfy the anti-backsliding requirements associated with the transition from the 1-hour standard to the 1997 8-hour standard. In such cases an area's existing SIP should be considered an adequate alternative program. Our reasoning follows from the fact that an area's existing SIP measures, in conjunction with other enforceable federal measures, are adequate for the area to achieve attainment, which is the purpose of the section 185 program. The section 185 fee program is an element of an area's attainment demonstration, and its object is to bring about attainment after a failure of an area to attain by its attainment date. Thus, areas that have attained the 1-hour standard, the standard for which the fee program was originally required, as a result of permanent and enforceable emissions reductions, would have a SIP that is not less stringent than the SIP required under section 185. Also, once an area attains the 1997 8-hour ozone standard, which replaced the now revoked 1-hour standard, the purpose of retaining the section 185 fee program as an anti-backsliding measure would also be fulfilled as the area would have attained the 8-hour standard

for which the fee program was retained as a transition measure. We believe that it would unfairly penalize sources in these areas to require that fees be paid after an area has attained the 8-hour standard due to permanent and enforceable emission reductions because the fees were imposed due to a failure to meet the applicable attainment deadline for the 1-hour standard, not any failure to achieve the now applicable 8-hour standard by its attainment date. Similarly, for the reasons described above, areas that must still develop and submit a fee program may submit an alternative that provides that the fees end at the time that the area attains either the 1-hour or 1997 8-hour standard due to the existence of permanent and enforceable measures.

There is also an additional, independent basis for EPA's approach to determining that the anti-backsliding requirements associated with section 185 have been satisfied. Although section 185 provides that fees are to continue until the area is redesignated for ozone, EPA no longer promulgates redesignations for the 1-hour standard because that standard has been revoked. Therefore, relief from the1-hour fee program requirements under the terms of the statute is an impossibility, since the conditions the statute envisioned for relieving an area of its fee program obligation no longer can exist. There is, thus, a gap in the statute which must be filled by EPA. We believe that under these circumstances we must exercise our discretion under Chevron USA, Inc. v. Natural Resources Defense Council, 467 U.S. 837 (1984), to fill this gap, so as to carry out Congressional intent in the unique context of anti-backsliding requirements for a revoked standard. We believe that it is reasonable for the fee program obligation that applies for purposes of anti-backsliding to cease upon a determination, based on notice-and-comment rulemaking, that an area has attained the 1-hour or 8-hour standard due to permanent and enforceable measures. This determination centers on core criteria for redesignations under CAA section 107(d)(3). We believe these criteria provide reasonable assurance that the purpose of the 1-hour anti-backsliding fee program obligation has been fulfilled in the context of a regulatory regime where the area remains subject to other applicable 1-hour anti-backsliding and 8-hour measures. Under these circumstances, retention of the fee program under the anti-backsliding rule is no longer necessary for the purpose of achieving attainment of the 8-hour standard.

Additional Potential Equivalent Alternative Program Concepts

Following is a summary of concepts for additional alternative programs that a state might consider if all 1-hour nonattainment areas subject to the section 185 fee program anti-backsliding requirements within that state are not eligible for the EPA determination set forth in the section above, and/or if the state chooses to develop another alternative program that is no less stringent than a section 185 fee program. While section 185 focuses most directly on assessing emissions fees, we believe it is useful to interpret section 185 within the context of the CAA's ozone implementation provisions of subpart 2 (which includes section 185). The subpart 2 provisions are designed to provide an ever-growing incentive to reduce ozone-forming pollutant emissions to levels that achieve attainment of the ozone NAAQS. In this context, to satisfy the requirements of section 185 associated with the 1-hour NAAQS we believe it is appropriate for states to focus on fee assessments, achieving further emissions reductions, or some combination of both in developing an alternative program. For any alternative program adopted by a state, the state's demonstration that the program is no less stringent should consist of comparing expected fees and/or emissions reductions directly attributable to application of section 185 to the expected fees and/or emissions reductions from the proposed alternative program. For a valid

demonstration to ensure equivalency, the state's submission should not underestimate the expected fees and/or emissions reductions from the section 185 fee program, nor overestimate the expected fees and/or emissions reductions associated with the proposed alternative program.

Recently, a task force composed of members of the Clean Air Act Advisory Committee (CAAAC) was formed to discuss alternate ideas on complying with section 185.[5] The concepts described here were discussed by the task force, and the CAAAC forwarded a list of potential program features to EPA for review. EPA's assessment of whether and how certain program features identified by the CAAAC can be used in the context of satisfying the requirements of section 185 is included as Attachment C to this memorandum.

EPA cannot conclude at this time whether specific state-developed programs relying on these concepts or containing any of the features presented by the CAAAC would be approvable because such a determination would be based on the specific parameters of the program adopted. Further, any such determination would need to be made through notice-and-comment rulemaking. States may decide to develop unique alternative programs for each applicable nonattainment area, and we will independently evaluate the approvability of each alternative program. To assure a valid demonstration that an alternative is no less stringent, we recommend that states work with EPA on a case-by-case basis.

Additional Fee-Equivalent Alternative Programs

We anticipate (subject to notice-and-comment rulemaking as noted above) that we could approve a program that clearly raises at least as much revenue as the otherwise required section 185 fee program if the proceeds are spent to pay for emissions reductions of ozone-forming pollutants (NOx and/or VOC) in the same geographic area subject to the section 185 program. Under this approach, the state would estimate revenues that would result under the section 185 fee program if all section 185 sources paid fees for each applicable calendar year, develop an alternative program that would raise at least that much revenue, and establish a process where the revenues would be used to pay for emissions reductions that will further improve ozone air quality.

Under this concept, states could develop programs that shift the fee burden from the specific set of major stationary sources that are otherwise required to pay fees according to section 185, to other non-major sources of emissions, including owners/operators of mobile sources. This could allow states to recognize through reduced fees those major sources of emissions that have already installed the latest technology, and assess the remainder of the total required fees on other sources that are not already as well controlled. EPA recognizes that section 185 is not strategic in imposing emissions fees on all major stationary sources, including already well-controlled sources that have few, if any, options for avoiding fees by achieving additional reductions. States can be more strategic by crafting alternative programs that exempt or reduce the fee obligation on well-controlled sources, and assign the required fees to less well-controlled sources as an incentive for those sources to further reduce emissions of ozone-forming pollutants. The alternative program should not rely on emissions reductions already required by

[5] For more information on the CAAAC and the proceedings of the Task Force on section 185 fee programs, visit the following Web site: http://www.epa.gov/air/caaac/185.html

the applicable SIP, since the goal is to achieve further reductions to move the area expeditiously to attainment.

Additional Emissions-Equivalent Alternative Programs

EPA believes that as an alternative to the section 185 fee program a state could adopt a program that achieves at least as much additional emissions reductions as would be expected to result from the fee-minimization incentive of the section 185 fee program. EPA believes this would clearly be demonstrated if the alternative program achieves emissions reductions each year that are equal to or greater than the amount of emissions against which fees would be assessed each year under the section 185 fee program (i.e., actual emissions in excess of 80 percent of the baseline emissions).[6] For purposes of estimating the emissions reductions required in such a program, the state would assume that sources would reduce their emissions to the fee applicability threshold. This conservative approach would assure that emissions reductions from the alternative program are at least as great as reductions that might have occurred if the statutory fee program resulted in all major stationary sources reducing their emissions to no more than 80 percent of the baseline emissions. The emissions reductions in the alternative program could come from the same set of major sources subject to section 185, or from a different set of sources, in whole or in part, so long as all reductions come from within the nonattainment area and are equally beneficial in reducing ozone formation. The alternative program should not rely on emissions reductions already required by the applicable SIP, since the goal is to achieve further reductions to move the area expeditiously to attainment.

Under this approach, states would first calculate the emissions baseline for the major stationary sources of VOC and NOx in accordance with the methodology required under CAA section 185(b)(2) and as further described in the March 21, 2008 guidance memorandum. Once a state calculates the baseline amount of each pollutant for each source affected by section 185, the amount of emissions in excess of 80 percent of the baseline would be the amount of emissions of each pollutant that sources within the area would need to reduce on a calendar year basis in each year following the 1-hour ozone attainment year until such time as the fee program no longer applies.

Additional Alternative Programs Combining Emissions Reductions and Fees

A program that combines features of an emissions-equivalent program with a fee-equivalent program could also be adopted. For example, some portion of the emissions reductions necessary to demonstrate equivalence (as explained above) could be offset by fees collected on each ton of emissions that is offset. To illustrate, assume that 1000 tons of emissions reductions is needed to demonstrate equivalence. The state could instead adopt a program that obtains 600 tons of emissions reductions and collect fees totaling $2.0 million (calculated as the remaining 400 tons times $5,000 per ton).

[6] A program that achieves less than this amount of emissions reductions may also be approvable depending on the case-specific circumstances.

EPA Assistance

My office is available to provide any additional guidance and to consult with any state that wants to develop an alternative equivalent program to the section 185 fee program. For additional consultation you may contact Denise Gerth, 919-541-5550.

ATTACHMENT A
Text of CAA Section 185

SEC. 185. ENFORCEMENT FOR SEVERE AND EXTREME OZONE NONATTAINMENT AREAS FOR FAILURE TO ATTAIN.

(a) General Rule.- Each implementation plan revision required under section 182 (d) and (e) (relating to the attainment plan for Severe and Extreme ozone nonattainment areas) shall provide that, if the area to which such plan revision applies has failed to attain the national primary ambient air quality standard for ozone by the applicable attainment date, each major stationary source of VOCs located in the area shall, except as otherwise provided under subsection (c), pay a fee to the State as a penalty for such failure, computed in accordance with subsection (b), for each calendar year beginning after the attainment date, until the area is redesignated as an attainment area for ozone. Each such plan revision should include procedures for assessment and collection of such fees.

(b) Computation of Fee.-

(1) Fee amount.- The fee shall equal $5,000, adjusted in accordance with paragraph (3), per ton of VOC emitted by the source during the calendar year in excess of 80 percent of the baseline amount, computed under paragraph (2).

(2) Baseline amount.- For purposes of this section, the baseline amount shall be computed, in accordance with such guidance as the Administrator may provide, as the lower of the amount of actual VOC emissions ("actuals") or VOC emissions allowed under the permit applicable to the source (or, if no such permit has been issued for the attainment year, the amount of VOC emissions allowed under the applicable implementation plan "allowables")) during the attainment year. Notwithstanding the preceding sentence, the Administrator may issue guidance authorizing the baseline amount to be determined in accordance with the lower of average actuals or average allowables, determined over a period of more than one calendar year. Such guidance may provide that such average calculation for a specific source may be used if that source's emissions are irregular, cyclical, or otherwise vary significantly from year to year.

(3) Annual adjustment.- The fee amount under paragraph (1) shall be adjusted annually, beginning in the year beginning after the year of enactment, in accordance with section 502(b)(3)(B)(v) (relating to inflation adjustment).

(c) Exception.- Notwithstanding any provision of this section, no source shall be required to pay any fee under subsection (a) with respect to emissions during any year that is treated as an Extension Year under section 181(a)(5).

(d) Fee Collection by the Administrator.- If the Administrator has found that the fee provisions of the implementation plan do not meet the requirements of this section, or if the Administrator makes a finding that the State is not administering and enforcing the fee required under this section, the Administrator shall, in addition to any other action authorized under this title, collect, in accordance with procedures promulgated by the Administrator, the unpaid fees required under subsection (a). If the Administrator makes such a finding under section 179(a)(4), the Administrator may collect fees for periods before the determination, plus interest computed in accordance with section 6621(a)(2) of the Internal Revenue Code of 1986 (relating to computation of interest on underpayment of Federal taxes), to the extent the Administrator finds such fees have not been paid to the State. The provisions of clauses (ii) through (iii) of section 502(b)(3)(C) (relating to penalties and use of the funds, respectively) shall apply with respect to fees collected under this subsection.

(e) Exemptions for Certain Small Areas.- For areas with a total population under 200,000 which fail to attain the standard by the applicable attainment date, no sanction under this section or under any other provision of this Act shall apply if the area can demonstrate, consistent with guidance issued by the Administrator, that attainment in the area is prevented because of ozone or ozone precursors transported from other areas. The prohibition applies only in cases in which the area has met all requirements and implemented all measures applicable to the area under this Act.
[42 U.S.C. 7511d]

ATTACHMENT B
Inflation Adjustment for Section 185 Fees

Section 185 cross-references the methodology in section 502(b)(3)(B)(v) of the CAA. This method has been interpreted for use in determining permit fees in a 1992 EPA memorandum. (See, Memorandum of October 15, 1992, from Frank Bunyard, "Calculating Fees for Operating Permits.") EPA has used this method to calculate the Part 70 permit fee rate since 1990, and will continue to update the rate every year in September, when the August values are available. The adjusted section 185 fee, then, would be prorated to that adjusted permit fee, as shown in Table 1 below, by multiplying the Part 70 permit fee rate by 200 ($5000/$25). Since section 185 fees are assessed on a calendar year basis, and the inflation factor is applied in September, the calendar year fee is determined as a weighted average (8/12 of the fee associated with January to August, and 4/12 of the fee associated with September to December). The weighted fees appear in Table 2 below. These will be updated each year in the fall.

TABLE 1: SECTION 185 FEE RATE BASED ON PART 70 PERMIT FEE RATE

Effective Dates	Part 70 Permit Fee Rate*	Sect. 185 Fee Rate
Sept 1989–Aug 1990	$25.00	$5,000.00
Sept 1990–Aug 1991	$26.21	$5,242.00
Sept 1991–Aug 1992	$27.59	$5,518.00
Sept 1992–Aug 1993	$28.43	$5,686.00
Sept 1993–Aug 1994	$29.30	$5,860.00
Sept 1994–Aug 1995	$30.07	$6,014.00
Sept 1995–Aug 1996	$30.93	$6,186.00
Sept 1996–Aug 1997	$31.78	$6,356.00
Sept 1997–Aug 1998	$32.65	$6,530.00
Sept 1998–Aug 1999	$33.21	$6,642.00
Sept 1999–Aug 2000	$33.82	$6,764.00
Sept 2000–Aug 2001	$34.87	$6,974.00
Sept 2001–Aug 2002	$36.03	$7,206.00
Sept 2002–Aug 2003	$36.60	$7,320.00
Sept 2003–Aug 2004	$37.43	$7,486.00
Sept 2004–Aug 2005	$38.29	$7,658.00
Sept 2005–Aug 2006	$39.48	$7,896.00
Sept 2006–Aug 2007	$41.02	$8,204.00
Sept 2007–Aug 2008	$41.96	$8,392.00
Sept 2008–Aug 2009	$43.75	$8,750.00
Sept 2009–Aug 2010	$43.83	$8,766.00

* From www.epa.gov/oar/oaqps/permits/historicalrates.html

TABLE 2: ANNUALIZED SECTION 185 FEE RATE

Sect. 185 Year	Annualized Sect. 185 Fee Rate
1990	$5,080.67
1991	$5,334.00
1992	$5,574.00
1993	$5,744.00
1994	$5,911.33
1995	$6,071.33
1996	$6,242.67
1997	$6,414.00
1998	$6,567.33
1999	$6,682.67
2000	$6,834.00
2001	$7,051.33
2002	$7,244.00
2003	$7,375.33
2004	$7,543.33
2005	$7,737.33
2006	$7,998.67
2007	$8,266.67
2008	$8,511.33
2009	$8,755.33

ATTACHMENT C
Response to CAAAC Task Force Options

EPA's Clean Air Act Advisory Committee (CAAAC) submitted a letter to EPA dated May 15, 2009, asking whether "it is legally permissible under either section 185 or 172(e) for a state to exercise the discretion identified" in 10 bullet points listed in an attachment to the letter (see Attachment D). In general, we believe the language in section 185 is relatively clear regarding the provisions that must comprise an approvable program and, as indicated in the discussion below, we do not believe that many of the flexibilities raised by the CAAAC would be approvable provisions of a state-adopted section 185 fee program. However, EPA believes that an alternative program that contains some of these flexibilities may be acceptable if it is consistent with the principles of section 172(e) of the CAA, which allows EPA through rulemaking to accept alternative programs that are "not less stringent" where EPA has revised the NAAQS. Although the anti-backsliding provisions of section 172(e) facially apply only where EPA has revised the NAAQS to make it less stringent, in its implementation rule governing the transition from the 1-hour ozone standard to the more stringent 1997 8-hour standard, EPA concluded that it made sense to rely on the governing principles in section 172(e). Applying this principle for the transition from the 1-hour standard to the 1997 8-hour ozone standard, EPA can either require states to retain a specific program that applied for purposes of the 1-hour standard, or alternatively can allow states flexibility to adopt alternative programs, but only if such alternatives are "not less stringent" than the mandated program. EPA has not yet concluded whether to apply the principles of section 172(e) to any future transitions from the 1997 ozone NAAQS to any new or revised ozone NAAQS.

Consistent with the preceding distinction between a section 185 fee program and an alternative program that is "not less stringent," we address each of the 10 points separately below.

Point A asks whether a state may "authorize multi-facility operators to aggregate emissions from commonly-owned and -operated facilities within a single nonattainment area for the purpose of calculating the fee." We have defined "major stationary sources" in many contexts and have interpreted that definition in certain circumstances to allow for aggregation of sources. We anticipate that we would be able to approve a section 185 fee program SIP that relies on a definition of "major stationary source" that is consistent with the CAA as interpreted in our existing regulations and policies.

Point B asks whether a state "may permit major sources to aggregate their VOC and NOx emissions on a site-wide basis in calculating the fee" and includes a description of certain limitations that would be assumed for such aggregation. Provided that aggregation is not used to avoid a "major source" applicability finding, and aggregation is consistent with the attainment demonstration (e.g., if the area has received a NOx waiver under section 182(f), then NOx reductions cannot be substituted for VOC reductions), we believe states have discretion to allow a major source to aggregate VOC and NOx emissions.

Points C and D concern whether states may allow a discount for certain "pre-attainment year or attainment year" controls. We do not believe that section 185 allows for any such

consideration. The statutory language is clear that the baseline emissions are the lower of the actual emissions or emissions allowed under the applicable permit during the attainment year or allowed under the SIP during the attainment year where there is no such permit. The only exception to this calculation for baseline emissions is where a source's emission are "irregular, cyclical or otherwise vary significantly from year to year." EPA has previously issued guidance addressing this exception. Although consideration of these controls is not consistent with the express terms of section 185, states may be able to develop a "no less stringent" program consistent with the principles in section 172(e), taking into consideration such pre-attainment controls. See discussion of point I below.

Point E asks whether the purchase of emission reduction credits, or allowances, that are part of an area's attainment control measures "may reduce the amount of emissions upon which the fee is based or constitute an investment that should be credited against the fee." In the context of calculating both the attainment-year baseline emissions and the post-attainment year emissions, section 185 requires such emissions be the lower of actual or allowable emissions. We believe allowable emissions can include emission reduction credits or emissions allowances held by a source subject to fees. Whether holding the emissions allowances will affect a source's fee obligation depends on the amount that is determined to be the lower of actual or allowable emissions for that source. If states wish to provide some other form of credit for sources that purchase market-based control measures, they may be able to do so in the context of a program that is no less stringent than a section 185 program consistent with the principle in section 172(e). See discussion of point I below.

Point F asks whether sources may receive credit for post-attainment year emissions reductions or air quality investments. The Act is clear that post-attainment year emission reductions will be credited to the extent that they reduce emission levels from the baseline year. For example, if a source has 1000 tons of emissions in the attainment "baseline" year, the CAA requires that source to pay fees on any emissions in excess of 800 tons (80 percent of baseline) in each post-attainment year. If the source is able to reduce post-attainment year emissions from 1000 tons to 900 tons, then the source will pay fees on only 100 tons of emissions. With regard to crediting emission-reducing or air-quality investments, we note that section 185 does not specify how collected fees must be spent. In general, we believe that a state may choose to use collected fees to support air quality improvement projects at sources. However, we caution that any such provisions should not be developed in a way such that the provisions would appear to defeat the purpose of section 185, which is to encourage emission reductions that will bring the area into attainment with the ozone NAAQS in the near-term.

Point G asks whether post-attainment year new sources must be subject to the fees. We believe it is clear that the fee imposed is on major sources. Thus, to the extent a "new source" is considered a part of a major source that existed in the attainment year, the emissions from the new source must be considered as emissions from that major source. For new major sources that are not part of existing major sources, we believe section 185 does not provide a clear interpretation of the source's fee obligation. Therefore, we believe states have discretion in determining how fees apply to these sources. States should consider that section 185 requires "each major stationary source" to pay a fee; however, the baseline amount for sources that did not have a permit in the attainment year is calculated according to what the SIP "allowed" during

the attainment year. Therefore, states should examine how the applicable SIP addressed emissions from potential new major sources in the attainment year. For example, a state could determine that the SIP's new source review (NSR) requirements would provide that a new source employ emissions control that meets the requirements of "lowest achievable emissions rate" (LAER). Therefore, the attainment-year baseline for a new source is the level allowable after application of LAER. Alternatively, a state could determine the SIP's NSR requirements would provide that a new source's net emissions impact be no greater than zero (i.e., emissions levels after application of LAER must be offset at a ratio of at least 1 to 1). Therefore the attainment-year baseline for a new source is zero, subjecting the entire amount of a source's post-attainment year emissions to the per-ton emissions fee. Also, states may be able to develop "not less stringent" programs consistent with the principles in section 172(e), that exempt new major sources from fees, provided the alternative programs meet the 172(e) standard of equivalence. See discussion of point I below.

With regard to Point H, which references state discretion regarding the use of collected fees, we point to our response above for Point F.

Point I asks whether section 172(e) authorizes a state to develop an alternative program to that mandated under section 185. As an initial matter, we note that section 172(e) does not directly apply here, where we are transitioning from the 1-hour ozone standard to the more stringent 1997 8-hour standard. However, in developing our anti-backsliding rules in the Phase 1 Rule for Implementing the 8-hour Standard (69 FR 23951, April 30, 2004), we indicated that although section 172(e) did not directly apply, we were relying on the principles in section 172(e), as well as other indications of Congressional intent, in developing our anti-backsliding rules. In South Coast Air Quality Management District v. EPA, 472 F.3d 882 (D.C. Cir. 2006), the Court rejected our waiver of the section 185 fee program for the 1-hour standard, holding that such program was a "control applicable" to the area as that phrase is used in section 172(e) and thus must be retained under EPA's decision to apply section 172(e) to the transition from the 1-hour standard to the more stringent 8-hour standard. Not before the Court was the issue of the remaining language in section 172(e) that provides that EPA "shall promulgate requirements ... to provide for controls which are not less stringent than the controls applicable to areas designated nonattainment before such relaxation." EPA believes that this language clearly allows EPA by regulation to accept alternative control programs that "are not less stringent" than those that were mandated by the Act for the standard that has been replaced (i.e., the 1-hour standard).

Point J requests that EPA "clearly indicate the conditions under which the collection of fees may be terminated." Furthermore, it indicates that some members of the task force "would like the authority to terminate the section 185 fee program upon the first year in which an area achieves the relevant standard." EPA believes that for an area EPA determines through notice-and-comment rulemaking is attaining either the 1-hour or 1997 8-hour ozone NAAQS based on permanent and enforceable emissions reductions, the area would no longer be obligated to submit a fee program SIP revision, nor be obligated to continue implementing a section 185 fee program (or approved alternative equivalent program). The bases for EPA to make such a determination through notice-and-comment rulemaking are provided in the memorandum associated with this Attachment.

ATTACHMENT D
CAAAC Letter

United States Environmental Protection Agency
Clean Air Act Advisory Committee

May 15, 2009

The Honorable Elizabeth Craig
Acting Assistant Administrator
Office of Air and Radiation
U.S. EPA
Ariel Rios North
1200 Pennsylvania Avenue, N.W.
Mail Code 6101A
Washington, DC 20460

Re: Clean Air Act Sections 185 and 172(e)

Dear Assistant Administrator Craig:

At the May 14, 2009 meeting of the US EPA Clean Air Act Advisory Committee, on a unanimous vote, the Committee resolved to urge the Agency to provide prompt guidance to the States regarding the following question arising under the Clean Air Act:

> *Is it legally permissible under either section 185 or 172(e) for a State to exercise the discretion identified in Options A-J?*

The Clean Air Act Section 185 Task Force, a work group established under the Clean Air Act Advisory Committee, identified ten areas (A-J) of potential state discretion. These options are listed in the attachment to this letter. The Committee took no position on the reasonableness or legal permissibility of any option.

As several States are in the process of developing their section 185 nonattainment fee programs, time is of the essence in providing appropriate legal and policy guidance.

Thank you sincerely,

Co-Chairs of the Section 185 Task Force:

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A. Aggregation of Emissions Among Commonly-Owned Facilities

At its option, a State may authorize multi-facility operators to aggregate emissions from commonly-owned and –operated facilities within a single nonattainment area for the purpose of calculating the fee.

B. Aggregation of VOC and NOx Emissions

At its option, a State may permit major sources to aggregate their VOC and NOx emissions on a site-wide basis in calculating the fee to the extent such aggregation is consistent with attainment modeling previously submitted by the State for the applicable air quality control region. Such aggregation is not to be used for the purpose of avoiding a "major source" applicability finding (e.g., by spreading emissions over multiple sources so as to render the average facility emissions less than the major source threshold).

C. Consideration of Pre-Attainment Year or Attainment Year Installation of BACT or LAER

At its option, a State may consider to an appropriate extent pre-attainment or attainment year emission control investments by major sources. Without intending to define the precise boundaries of a State's discretion to recognize the degree of control already achieved by a source, the participants determined that sources that had recently (e.g., within five (5) years of the year for which the fee would be imposed) undergone new source review and, as a result, installed BACT or LAER, should not be required to include emissions from such equipment in calculating the fee.

D. Consideration of Pre-Attainment Year or Attainment Year Installation of Retrofit Controls.

In addition, at its option under appropriate circumstances, a State may designate emission performance standards that it has determined represent well-controlled (e.g., in the range of or superior to BACT or LAER) units for a given period of time and authorize a facility to demonstrate what portion of its emissions should be excluded from the fee calculation on that basis.

E. Consideration of Market-Based Programs

At its option under appropriate circumstances, a State may determine that purchases of emission reduction credits, or allowances, as part of a State's market-based attainment control measure may reduce the amount of emissions upon which the fee is based or constitute an investment that should be credited against the fee.

F. Credit Sources for Post-Attainment Year Emissions-Reducing or Air Quality Investments

At its option, a State should recognize and appropriately credit qualifying post-attainment year emissions-reducing or air quality-beneficial investments by major sources. These investments should be credited to such sources in a manner that reduces or eliminates fees that otherwise would be due under the program. States should identify the qualifications for such investments based on their unique attainment needs.

G. Post-Attainment Year New Sources

There was agreement that new sources constructed after the attainment year would not have a baseline; would already have installed BACT or LAER, would already have provided offsets, and therefore should not be subject to the fee for such equipment.

H. Use of Program Revenues

States retain full discretion regarding the use of collected revenues. Participants encouraged States to tailor strategies to their unique attainment challenges and to consider ways to address under-regulated sources (e.g., legacy vehicles and engines and certain area sources).

I. Equivalent Programs

Under section 172(e), a State should have the option of collecting equivalent or greater fees, or of requiring equivalent or greater emission reductions, by shifting the program target in part or in whole to under-regulated sources (e.g., legacy vehicles and engines, under-regulated area sources) or by applying the program in a manner that addresses other attainment gaps. Likewise, the task force envisioned that any recommended strategy not directly approvable under section 185 should be considered as an equivalent alternative program under 172(e). In such circumstances, the state may need to shift the fee burden among sources to demonstrate equivalency.

J. Program Sunset

EPA needs to clearly indicate the conditions under which the collection of fees may be terminated. Some members of the taskforce would like the authority to terminate the section 185 fee program upon the first year in which an area achieves the relevant standard.