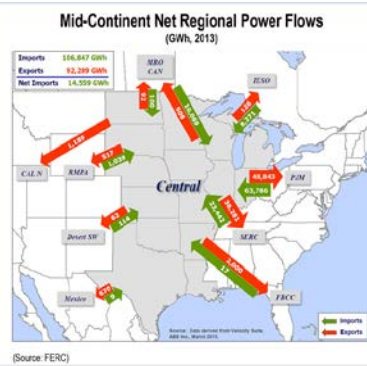


# EPA's CO<sub>2</sub> Rules and the Common Elements Approach

*Legal and Practical Issues with the Compliance Avenue*



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## **Executive Summary**

***The Common Elements Approach leaves many significant questions remaining to be addressed.*** Until these issues are resolved, states cannot consider the approach or variations on this approach as a viable compliance option.

***The Common Elements Approach requires state implementing legislation.*** The brief describing the approach compares the single state trading regimes to REC trading markets, which generally required state implementing legislation to create common currencies and other trading architecture. RGGI also required state legislation. States moving forward without legislation face significant legal risk.

***The authors fail to designate a basic level of “common elements” needed to implement the approach.*** The brief explaining the Common Elements Approach does not set forth the proposed components of the “common platform” with any significant level of detail. It notes that “[i]ndividual state definitions of compliance instruments will determine which states interact under the common elements approach.” RGGI illustrates that the “common platform” that is necessary would require more than just a common currency. The RGGI Model Rule encompasses a detailed allowance system that features a trading market, measurement and verification processes, compliance reporting, compliance evaluation and public reporting. These are real, non-trivial administrative oversight processes that would need to be institutionalized.

***The Common Elements Approach does not appear to comply with the proposed Clean Power Plan.*** No discussion in the proposed rule contemplates the single state plan approach as set forth in the Common Elements Approach. The Clean Power Plan discusses multi-state plans in the context of predetermined states working together and not on a “TBD” basis. Moreover, a state plan premised on the Common Elements Approach and without implementing legislation would fail to satisfy EPA’s stated approval criteria, specifically the requirement that state plans be enforceable. State institutional issues also remain as a compliance hurdle.

***The timing issues remain difficult if not insurmountable.*** A state submitting a single state plan will have two years, at most, to submit its plan. RGGI took five years to design and implement, and the cap-and-trade component of Assembly Bill 32 in California took nearly seven years to come to fruition. This is no fault of the architects of the Common Elements Approach, but states pursuing it would have to develop and implement the approach on an extraordinarily tight timeline. Despite the purported ease of implementation given the use of individual state plans, the timing challenges stem from the need to develop common CO<sub>2</sub> trading architecture. This is a significant political, regulatory and administrative undertaking that would have to be completed within just a fraction of the time that other market designs have required in RGGI states and California.

## I. Introduction

Last month the Nicholas Institute for Environmental Policy Solutions at Duke University issued a policy brief entitled *Enhancing Compliance Flexibility under the Clean Power Plan: A Common Elements Approach to Capturing Low-Cost Emissions Reductions*.<sup>1</sup> This brief<sup>2</sup> urges states to build on the “established track record of market-based compliance strategies” under the Clean Air Act and adopt the so-called “common elements approach.” (Common Elements Approach) The authors summarize this approach as follows: “[A] state could develop an individual-state plan to meet its own emissions target (rather than a multistate plan to meet a joint target) and allow EGU [electric generating unit] operators to transfer compliance credits among units within a state and among states that share common elements in their compliance plans.”<sup>3</sup> To be sure, market-based compliance mechanisms have been employed under the Clean Air Act; however, the Common Elements Approach raises several questions within the Clean Power Plan (CPP) construct that are not addressed in the Nicholas brief. This White Paper<sup>4</sup> endeavors to offer a constructive critique of the Common Elements Approach. These questions and open issues include:

(1) the need for state implementing legislation;

(2) the basic level of “common elements” needed between states to allow for, *inter alia*, interstate trading and approval of the single state plan by the Environmental Protection Agency (EPA);

(3) whether the Common Elements Approach complies with the proposed CPP;

(4) whether timing issues render the Common Elements Approach proposal impractical or even moot, as opposed to creating a viable compliance pathway; and,

(5) other public policy considerations related to carbon dioxide (CO<sub>2</sub>) budget trading in different parts of the country.

## II. Overview of the Common Elements Approach

The Common Elements Approach attempts to find a way around “barriers” to “interstate market programs,” specifically the need to commandeer resources to evaluate and design a multi-state compliance plan.<sup>5</sup> These barriers also include significant constitutional issues, as multi-state plans creating interstate market programs will require an interstate enforcement mechanism. This creates a need for an interstate compact under the Compact Clause that may well require congressional approval -- an issue explored at some length in our earlier CPP analyses.<sup>6</sup> In addition, and perhaps most significantly, “political opposition to cap-and-trade programs may constrain officials in some states from considering market-based compliance mechanisms even if the data suggest that such mechanisms would be more cost-effective for citizens.”<sup>7</sup>

The Common Elements Approach is presented as a “middle ground” where “[s]tates would develop individual-state plans (not multistate plans) to achieve individual-state targets, defining EGU operators’ obligations and the suite of strategies the operators may

<sup>1</sup> Jonas Monast, Tom Profeta, Jeremy Tarr, & Brian Murray, *Enhancing Compliance Flexibility under the Clean Power Plan: A Common Elements Approach to Capturing Low-Cost Emissions Reductions* (Mar. 2015), available at [http://nicholasinstitute.duke.edu/sites/default/files/publications/ni\\_pb\\_15-01.pdf](http://nicholasinstitute.duke.edu/sites/default/files/publications/ni_pb_15-01.pdf) (hereinafter “Common Elements Approach”).

<sup>2</sup> All references to the “Nicholas brief” in this White Paper refer to the paper referenced in the previous footnote and proposing the Common Elements Approach.

<sup>3</sup> *Common Elements Approach*, at 2.

<sup>4</sup> Trading regimes facilitated through multi-state plans with a single, aggregated CO<sub>2</sub> performance goal amongst the participating states are outside the scope of this White Paper. These approaches have been addressed in our previous White Papers addressing the CPP.

<sup>5</sup> *Common Elements Approach*, at 3.

<sup>6</sup> Raymond L. Gifford, Gregory E. Sopkin, and Matthew S. Larson, *State Implementation of CO<sub>2</sub> Rules: Institutional and Practical Issues with State and Multi-State Implementation and Enforcement*, at 14-17 (July 2014), available at <http://www.wbklaw.com/uploads/file/Articles-%20News/White%20Paper%20-%20State%20Implementation%20of%20CO2%20Rules.pdf>.

<sup>7</sup> *Id.*

implement to meet their respective emissions limits. The state plan would allow the operator to determine whether to use tradable compliance instruments (*i.e.*, credits) or other means to meet its compliance obligation.”<sup>8</sup> Market-based options would need to include a “process for creating and tracking compliance instruments.” The state adopting this approach with select common elements in its state plan could, after approval by EPA of the individual state plan, partner with states with similar state plans and effectively back in to multi-state CO<sub>2</sub> trading markets. These markets would not necessarily share common regions or electrical interconnections, but would share “common elements.”

The Nicholas brief claims several benefits to the Common Elements Approach, specifically that it: (1) allows for ease of adoption and administration,<sup>9</sup> (2) preserves state autonomy,<sup>10</sup> and (3) obviates state institutional issues and authority gaps.<sup>11</sup> These claimed benefits raise several questions as discussed below.

### III. Need for State Legislation

The Nicholas brief is silent on the need for state legislation, but the Common Elements Approach would

<sup>8</sup> *Id.*

<sup>9</sup> *Id.* at 4 (“Because individual-state plans are the backbone of the common elements approach, regional planning in the form of negotiations, model rule writing, multistate plan development and submittal, or a memorandum of understanding between states is unnecessary.”)

<sup>10</sup> *Id.* (“States could decide individually the degree to which they wish to coordinate with one another on these issues, thereby ensuring state plan alignment and opportunities to transfer credits between states. Similarly, states may decide to align other plan components, such as protocols for crediting energy efficiency and renewable energy in a rate-based compliance system. Overall, states would remain free to make their own decisions about the nature of compliance credits (e.g., mass based or rate based), how to distribute the compliance obligation among EGUs/companies, how to resolve stakeholder concerns, and other issues.”)

<sup>11</sup> *Id.* at 5. (“A strategy that identifies targets for covered units and that identifies a suite of compliance strategies from which EGU operators may choose would maintain state-level agencies’ traditional roles. The state environmental agency would develop the state compliance plan, including obligations for covered entities and parameters of compliance options from which operators may choose, such as a carbon market. Unit operators and utility regulators would continue to make energy decisions and address reliability considerations. State energy offices would continue to pursue their mandates.”)

need state legislation to be lawfully implemented. The analogies in the Nicholas brief to existing energy and environment trading markets illustrate this point.

The Common Elements Approach is described as follows:

A common elements approach operates much like existing renewable energy credit (REC) markets. Twenty-nine states have renewable portfolio standards (RPSs), which require a portion of electricity generation or sales to come from renewable sources .... State laws implementing RPSs define what constitutes a renewable source (*e.g.*, solar, wind, biomass, or swine waste) and prescribe how RECs are created. These jurisdictions often allow covered entities to utilize credits that originate either inside or outside the state, so long as they meet criteria specified by the state of compliance. In addition to defining the RECs and what constitutes a renewable energy facility, state RPSs designate approved tracking systems to protect against double counting.<sup>12</sup>

State RPSs and REC markets are created by state statute. These state laws are necessary to create the trading architecture, including the trading currency (typically RECs or a similarly structured currency with a different moniker). For example, in prominent REC markets such as California,<sup>13</sup> Colorado<sup>14</sup> and Texas,<sup>15</sup>

<sup>12</sup> *Id.*

<sup>13</sup> Cal. Pub. Util. Code § 399.12(f) (defining REC as “a certificate of proof, issued through the accounting system established by the Energy Commission... that one unit of electricity was generated and delivered by an eligible renewable energy resource. .... ‘Renewable energy credit’ includes all renewable and environmental attributes associated with the production of electricity from the eligible renewable energy resource, except for an emissions reduction credit issued pursuant to Section 40709 of the Health and Safety Code and any credits or payments associated with the reduction of solid waste and treatment benefits created by the utilization of biomass or biogas fuels.”)

<sup>14</sup> Colo. Rev. Stat. § 40-2-124(1)(d) (“In accordance with article 4 of title 24, C.R.S., the commission shall revise or clarify existing rules to establish the following: ... (d) A system of tradable renewable energy credits that may be used by a qualifying retail utility to comply with this standard. The commission shall also analyze the effectiveness of utilizing any regional system of renewable energy credits in existence at the time of its rule-making process and



state legislation created the markets, either with specificity or by providing authority to a state agency to do so. The state legislation established the market parameters and delegated the requisite authority for development and establishment of the REC markets to an appropriate agency. To be clear, the Common Elements Approach does *not* state that legislation is unnecessary, but it also does not address the issue. However, in the explanation of how state REC markets are similar to the scheme contemplated by the Common Elements Approach, the Nicholas brief notes that the referenced REC trading markets (North Carolina, Missouri and Kansas) were created by statute:

These three states -- North Carolina, Missouri, and Kansas -- neither formally coordinated the provisions of their RPS programs *nor named each other in their state statutes*. Nevertheless, RECs that originate in each state can be used toward compliance in the other states because the three states' programs allow for out-of-state RECs and designate common or electronically linked tracking platforms .... Similarly, EGUs in states with common elements (i.e., common credit definitions and a mutual (or linked) platform) could transfer CPP credits across state lines for compliance without a formal multistate agreement.<sup>16</sup>

The comparison between the Common Elements Approach and REC markets is appropriate, and the latter statement regarding interstate CPP trading may in fact be true assuming some of the other hurdles in this White Paper are addressed and overcome by the implementing state. For this to be possible, however, a state needs to pass legislation just as states did to authorize and implement REC trading markets.<sup>17</sup> This

determine whether the system is governed by rules that are consistent with the rules established for this article.”)

<sup>15</sup> Texas Util. Code Ann. 39.904(b) (“The commission shall establish a renewable energy credits trading program. Any retail electric provider, municipally owned utility, or electric cooperative that does not satisfy the requirements of Subsection (a) by directly owning or purchasing capacity using renewable energy technologies shall purchase sufficient renewable energy credits to satisfy the requirements by holding renewable energy credits in lieu of capacity from renewable energy technologies.”)

<sup>16</sup> *Common Elements Approach*, at 5 (emphasis added).

<sup>17</sup> Arizona is an outlier with regard to the adoption of its RPS (entitled a Renewable Energy Standard and Tariff (REST) in

legislation would likely engender the same “political opposition” cited in the Nicholas brief<sup>18</sup> given that the underlying purpose of any such bill would be to facilitate intra- and interstate CO<sub>2</sub> budget trading.

The Regional Greenhouse Gas Initiative (RGGI) provides another relevant example and is favorably cited in the Common Elements Approach.<sup>19</sup> RGGI is based upon single state implementation, but it also required new legislation<sup>20</sup> to implement the detailed and extensive Model Rule.<sup>21</sup> The Model Rule contains general provisions and establishes authorized account representatives, permit requirements, CO<sub>2</sub> allowance allocations, a CO<sub>2</sub> allowance tracking system and monitoring and reporting requirements, among other

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Arizona), which was implemented by the Arizona Corporation Commission (ACC) without state legislation. Arizona Corporation Commission Decision No. 69127, Docket No. RE-00000C-05-0030 (Nov. 14, 2006), available at <http://www.azcc.gov/divisions/utilities/electric/res.pdf?d=12>. The ACC was sued by several ratepayers for exceeding its authority in promulgating the REST. The Court of Appeals of Arizona upheld the REST as “within [the ACC’s] plenary power over ratemaking” under the Arizona Constitution. *Miller v. Ariz. Corp. Comm’n*, 251 P.3d 400, 406 (Ariz. Ct. App. 2011). However, the ACC has consistently enjoyed considerable latitude and powers far beyond the purview of most, if not all, state public utilities commissions. For that reason, adoption of Arizona’s administrative approach carries significant litigation risk. The Arizona Court of Appeals decision in *Miller* is therefore of limited import in the context of the Common Elements Approach.

<sup>18</sup> *Common Elements Approach*, at 3.

<sup>19</sup> *Id.*

<sup>20</sup> See Connecticut (R.C.S.A 22a-174-31; Conn. Gen. Stat. Section 22a-200c); Delaware (7 DE Admin Code 1147; Title 7 Chapter 60 of the Delaware Code, Subchapter IIA, §6043); Maine (DEP Chapter 156-158; Maine Rev. Stat., Title 38, Chapter 3-B); Maryland (Department of Environment, Title 26, Subtitle 9; Environment Article, §§1-101, 1-404, 2-103, and 2-1002(g), Annotated Code of Maryland); Massachusetts (DEP Regulations 310 CMR 7.70; 225 CMR 13.00; M.G.L. c. 21A, §22); New Hampshire (NH Code of Admin. Rules, Chapter Env-A 4600; Chapter Env-A 4700; Chapter Env-A 4800; RSA 125-O:19-28p; RSA 125-O:8, I(c)-(g)); Rhode Island (Dept. of Environmental Management Office of Air Resources, Air Pollution Control Regulation No. 46 and 47; R.I. Gen. Laws §42-17.1-2(19), §23-23 and §23-82); Vermont (30 V.S.A. § 255; 30 V.S.A. § 209(d)(3); Agency of Natural Resources, Vermont CO<sub>2</sub> Budget Trading Program 23-101 – 23-1007).

<sup>21</sup> Regional Greenhouse Gas Initiative Model Rule, available at

<https://www.rggi.org/docs/Model%20Rule%20Revised%2012.31.08.pdf> (providing 135 pages of model language).

structures and processes. The same would be needed for the Common Elements Approach and, as with nearly all RGGI states save one, would require state implementing legislation.

Common Elements Approach proponents will point to New York as an example of a state implementing RGGI without legislation. New York promulgated its RGGI rule through an administrative agency without state legislation. However, the state was also embroiled in multi-year litigation by virtue of this course of action.<sup>22</sup> Because the claims were ultimately time-barred, the court did not address the merits of the challenge to New York's approach. This case is instructive to states from a practical standpoint, however, because moving forward with implementation of a CO<sub>2</sub> budget trading apparatus without state legislation carries litigation risk.

The Nicholas brief also makes passing reference to other EPA trading programs and implies that the existence of these programs -- implemented without state legislation -- supports the proposition that the Common Elements Approach does not require enabling authority in state statute. On the other hand, a summary of these programs within the proposed CPP shows distinguishing characteristics for each program:

Specifically in the area of pollution control, state governments and the federal government have repeatedly taken advantage of the integrated nature of the electricity system when designing programs to allow the industry to meet the pollution control objectives in a least-cost manner. Examples include several cap-and-trade programs to reduce national or regional emissions of SO<sub>2</sub> and NO<sub>x</sub>: The SO<sub>2</sub>-related portion of the CAA Title IV Acid Rain Program, the Ozone Transport Commission (OTC) NO<sub>x</sub> Budget Program, the NO<sub>x</sub> SIP Call NO<sub>x</sub> Budget Trading Program, and the Clean Air Interstate Rule (CAIR) annual SO<sub>2</sub>, annual NO<sub>x</sub>, and ozone-season NO<sub>x</sub> trading programs. While the Acid Rain Program was created by federal legislation, the OTC NO<sub>x</sub> Budget Program was developed primarily through the joint efforts of a group of northeastern states. In the NO<sub>x</sub> SIP Call and CAIR programs, the federal

government set emission budgets and developed trading programs that states could use as a compliance option. Each of these programs was designed to take advantage of the fact that in an integrated electricity system, some EGUs can reduce emissions at lower costs than others, and that by allowing the industry to determine through market mechanisms which EGUs to control and which to leave uncontrolled, and which EGUs to potentially operate more and which to potentially operate less, overall compliance costs can be reduced.<sup>23</sup>

Federal legislation created the Acid Rain Program. The OTC NO<sub>x</sub> Budget Program involved a multi-state effort, while the Common Elements Approach is premised on single state plans with "no predetermined group of states working together ..." <sup>24</sup> and therefore is distinguishable. Finally, the NO<sub>x</sub> SIP Call and CAIR programs involved federal emission budgets established by EPA, which is the case with the CPP, but also featured trading programs *developed by EPA* as a compliance option. Trading is a compliance option under the proposed CPP, but there is no program set up by EPA. Indeed, despite requests from stakeholders that EPA develop a model rule on interstate emissions trading in the CPP, <sup>25</sup> EPA declined to do so and instead merely invited public comment on the idea. Without the EPA-driven trading architecture as with the NO<sub>x</sub> SIP Call and CAIR programs, the Common Elements Approach is more akin to RGGI and REC markets -- both of which required state implementing legislation.

Finally, the conclusion that state legislation is needed to implement the Common Elements Approach is consistent with EPA analyses supporting the proposed rule. Indeed, in its Technical Support Document entitled "State Plan Considerations," EPA states:

*State and regional GHG emission budget trading programs are authorized through individual state legislation and implemented through state regulations.* For example, California implemented its emission budget

<sup>22</sup> *Thrun v. Cuomo*, 112 A.D.3d 1038 (N.Y. App. Div. Dec. 5, 2013).

<sup>23</sup> 79 Fed. Reg. 34,880 (June 18, 2014).

<sup>24</sup> *Common Elements Approach*, at 5.

<sup>25</sup> 79 Fed. Reg. 34,847 ("Some groups thought that the EPA should put forward a model rule for an interstate emissions credit trading program that could be easily adopted by states who wanted to use such a program for its plan.")

trading program under the authority of its 2006 Global Warming Solutions Act, which requires the state to reduce its 2020 GHG emissions to 1990 levels. Each RGGI state has separate authorizing legislation, and in some cases their legislation specifically directs the use of auction proceeds. For example, Maine authorized its participation in RGGI through Statute 580-A, Title 38 Chapter 3B: Regional Greenhouse Gas Initiative. This statute also requires that 100 percent of auction proceeds go towards carbon reduction and energy conservation efforts. RGGI is implemented through individual state CO<sub>2</sub> budget trading program regulations.<sup>26</sup>

EPA's categorical position on the need for state legislation to create and authorize CO<sub>2</sub> budget trading programs does not appear to provide any exception for the Common Elements Approach. Therefore, EPA's own discussion on this issue suggests that state legislation would be required for implementation of the Common Elements Approach.

#### IV. Incongruent State Regimes

The Nicholas brief touts the Common Elements Approach as having a "lower administrative burden" because it obviates the need for formal regional planning and negotiations.<sup>27</sup> It further states:

A state could develop a compliance plan without engaging in formal interstate negotiations and still benefit from low-cost mitigation opportunities in another state if the two states choose the same credit definition and tracking platform. Informal conversations among states could allow them to strategically choose a common platform and credit definition and thereby

permit their EGUs to access a larger pool of credits.<sup>28</sup>

This White Paper does not dispute the ease of adoption that would flow from removing the regional overlay to CPP compliance planning. However, the Nicholas brief does not explain the proposed components of the "common platform" with any significant level of detail. It notes that "[i]ndividual state definitions of compliance instruments will determine which states interact under the common elements approach."<sup>29</sup> Turning again to RGGI for guidance, the need for congruency of the "common platform" requires more than just a common currency.

The RGGI Model Rule encompasses a detailed allowance system that features a trading market, measurement and verification processes, compliance reporting, compliance evaluation and public reporting. It also puts in place the RGGI CO<sub>2</sub> Allowance Tracking System (RGGI COATS), which allows for uniform system of compliance evaluation across the participating states. Each and every component of the comprehensive RGGI platform, including its compliance and verification functions, may not need to be adopted for states to have "common elements." However, the Nicholas brief does not define some minimum floor or basic level of overlapping elements necessary to facilitate the Common Elements Approach.

The Nicholas brief acknowledges that "[w]hen it comes to designating a tracking system for CPP purposes, states have a range of choices."<sup>30</sup> States may avail themselves of this "range of choices," which may result in incompatible, or at a minimum incongruent, trading currencies, platforms and verification processes. While "[s]tates could decide individually the degree to which they wish to coordinate with one another on these issues, thereby ensuring state plan alignment and opportunities to transfer credits between states," surely there is some basic level of commonality or congruity needed and that is undefined and unaddressed in the Common Elements Approach brief.

This omission may be easy to ignore or overlook now as states rush to meet an unprecedented compliance deadline of June 30, 2016. However, the haste may ultimately cause latent compliance problems

<sup>26</sup> EPA Office of Air and Radiation, *State Plan Considerations – Technical Support Document for Carbon Pollution Emission Guidelines for Existing Stationary Sources: Electric Utility Generating Units*, at 103, Docket ID No. EPA-HQ-OAR-2013-0602 (June 2014) (emphasis added), available at <http://www2.epa.gov/sites/production/files/2014-06/documents/20140602tsd-state-plan-considerations.pdf> (hereinafter "State Plan Considerations TSD").

<sup>27</sup> *Common Elements Approach*, at 4.

<sup>28</sup> *Id.* at 4-5.

<sup>29</sup> *Id.* at n. 11.

<sup>30</sup> *Id.* at 6.

for states, and proponents of the Common Elements Approach need to explain the “elements” that would need to be “common” to allow for a “plug and play” scenario without predetermined and coordinated state participation.

## V. Compliance with the CPP

Compliance, and by extension enforcement, is the definitive inquiry and usually takes its rightful place at the front of any regulatory analysis. But given the significant open questions in the Common Elements Approach, *i.e.*, the need for state legislation and the minimum level of interlocking components between states, the issue of whether the Common Elements Approach complies with the CPP carries substantial uncertainty. With that caveat, the proposed rule does not appear to allow for approval of a state plan premised on the Common Elements Approach.

The Nicholas brief holds the Common Elements Approach out as the quintessential deployment of state flexibility, but offers little detail on how the rule allows for this approach. Rather, “[a]lthough the common elements approach described in this policy brief is not expressly discussed in the proposal, it is consistent with the state plan requirements outlined in the proposal.”<sup>31</sup> This amorphous “consistency” argument belies two fundamental flaws. First, the CPP does not contemplate this type of submittal by a state. Second, the Common Elements Approach does not meet EPA’s approval criteria set forth in the proposed rule.

A footnote in the Nicholas brief cites a discussion in the proposed rule that purports to allow for a Common Elements Approach-driven state plan:

The proposal discusses a version of a multistate plan in which ‘*all states participating in a multi-state plan* separately make individual submittals that address all elements *of the multi-state plan,*’ as opposed to one joint plan submittal. Proposed Clean Power Plan, at 34,911. Unlike the multistate option identified in the proposed CPP, the common elements approach would not require states to negotiate with one another to develop a multistate plan. Rather, the individual-state plans would describe the nature of compliance credits, designate a

tracking platform, and allow for interstate transfers of credits among states with plans that share these essential common elements.<sup>32</sup>

The Common Elements Approach facially fails to satisfy EPA’s vision in this portion of the proposed rule: there is no multi-state plan under the Common Elements Approach because these are “no predetermined group of states working together ...”<sup>33</sup> Accordingly, the scenario referenced in the rule is distinguishable as it contemplates a predetermined group of states actively working together and developing individual state plans *to effectuate and implement the agreed upon multi-state compliance approach*. In addition, the proposed CPP is replete with references to the expectation that multi-state plans be submitted in a single plan or as a state-specific plan with *known state partners*.<sup>34</sup> In sum, the referenced language does not support the proposition that the Common Elements Approach fits within the proposed rule such that the proposed form of submittal is permitted.

In addition to the form of submission issue, the Common Elements Approach does not seem to meet EPA’s approval criteria. The proposed rule provides as follows:

<sup>32</sup> *Id.* at n. 10 (emphasis added).

<sup>33</sup> *Id.* at 5.

<sup>34</sup> *See, e.g.*, 79 Fed. Reg. 34,911 (“*For states wishing to participate in a multi-state plan, the EPA is proposing that only one multi-state plan would be submitted on behalf of all participating states.* The joint submittal would be signed by authorized officials for each of the states participating in the multi-state plan and would have the same legal effect as an individual submittal for each participating state. The joint submittal would adequately address plan components that apply jointly for all participating states and for each individual state in the multi-state plan, including necessary state legal authority to implement the plan, such as state regulations and statutes.”) (emphasis added); 79 Fed. Reg. 34,915 (“*[F]or states wishing to participate in a multi-state plan, the EPA is proposing that only one multi-state plan would be submitted on behalf of all participating states, provided it is signed by authorized officials for each of the states participating in the multi-state plan and contains the necessary regulations, laws, etc. for each state in the multi-state plan. In this instance, the joint submittal would have the same legal effect as an individual submittal for each participating state.*”) (emphasis added).

<sup>31</sup> *Id.* at 3.



The EPA is proposing to evaluate and approve state plans based on four general criteria: 1) enforceable measures that reduce EGU CO<sub>2</sub> emissions; 2) projected achievement of emission performance equivalent to the goals established by the EPA, on a timeline equivalent to that in the emission guidelines; 3) quantifiable and verifiable emission reductions; and 4) a process for biennial reporting on plan implementation, progress toward achieving CO<sub>2</sub> goals, and implementation of corrective actions, if necessary.<sup>35</sup>

The criteria apply universally to single and multi-state plans submitted pursuant to the CPP. A state submitting a plan relying on the Common Elements Approach, specifically the trading component of it, without state authorizing legislation is at risk of failing to submit an enforceable state plan. The State Plan TSD makes clear that “[s]tate and regional GHG emission budget trading programs are authorized through individual state legislation and implemented through state regulations.”<sup>36</sup> Therefore, when the agency is confronted with a state plan permitting intrastate trading (at a minimum), with the potential for interstate trading if and when Common Elements Approach partners emerge, the agency will look for authorizing legislation and implementing regulations creating the architecture of the trading regime. Absent a statute, it is likely the measures in the state plan are not enforceable, which puts the state at risk of disapproval and imposition of a federal plan. In addition, even if EPA is willing to approve the state plan without legislation (and the agency might give the thinly veiled desire for intra- and interstate trading in the proposed rule), EPA would subject itself to litigation for approving a state plan that did not satisfy the approval criteria in the rule. This outcome, by extension, puts the state plan at risk and injects uncertainty into state compliance efforts.

A further consideration related to the enforcement criterion stems from the Nicholas brief’s assertion that the Common Elements Approach allows states to “maintain traditional state agency roles.”<sup>37</sup> However, some state organ must oversee and administer a trading program as part of any Common Elements Approach. This function, *i.e.*, conducting a CO<sub>2</sub> budget trading

program, does not fall within any “traditional” agency role and again comes back to the need for state legislation. Some state agency or office needs to assume a position similar to RGGI, Inc.,<sup>38</sup> the non-profit corporation established to develop and administer RGGI, and conduct these activities on an intrastate basis. Accordingly, the notion that this approach obviates the state legal authority issues is undeveloped and unfounded.

To be sure, in its ardor to facilitate intra- and interstate CO<sub>2</sub> budget trading, EPA could attempt to enable a Common Elements Approach-type trading system in the final rule. Such turnabouts are not unknown in the annals of rulemaking. However, this would require EPA to significantly revise the proposed rule and include a model rule in the final CPP, which it declined to do in the proposed rule.<sup>39</sup> Moreover, even if EPA enables a Common Elements Approach or some derivation in the final rule, the legislative and administrative apparatuses to ensure the allocations are fungible, verifiable and effective at triggering switching from more to less carbon-intensive generation will take time and require significant effort to develop.

## VI. Timing Issues

A final issue is timing, which is no fault of the Common Elements Approach. Because a single state plan is involved, the submission deadline is June 30, 2016 with the possibility of a one-year extension to June 30, 2017.<sup>40</sup> The required state legislation and subsequent rulemakings to create the architecture for a CO<sub>2</sub> budget trading platform will take time. Consider that discussions around RGGI began in late 2003, with the first allowance auction in 2008 and first compliance period beginning January 1, 2009.<sup>41</sup> In other words, it took over five years for the trading platform to be designed and implemented. Similarly, Assembly Bill 32, the California Global Warming Solutions Act of 2006, passed in 2006 but the cap-and-trade program

<sup>38</sup> RGGI, Inc. Home Page, *available at*

<http://www.rggi.org/rggi>.

<sup>39</sup> 79 Fed. Reg. 34,847.

<sup>40</sup> 79 Fed. Reg. 34,952 (proposed 40 C.F.R. § 60.5755(a)-(b)).

<sup>41</sup> Environmental Defense Fund & International Emissions Trading Association, *The World’s Carbon Markets: A Case Study Guide to Emissions Trading*, at 1 (May 2013), *available at*

[http://www.ieta.org/assets/Reports/EmissionsTradingAroundTheWorld/edf\\_ieta\\_rggi\\_case\\_study\\_may\\_2013.pdf](http://www.ieta.org/assets/Reports/EmissionsTradingAroundTheWorld/edf_ieta_rggi_case_study_may_2013.pdf).

<sup>35</sup> 79 Fed. Reg. 34,838.

<sup>36</sup> *State Plan Considerations TSD*, at 103.

<sup>37</sup> *Common Elements Approach*, at 5.

commenced on January 1, 2013.<sup>42</sup> States pursuing the Common Elements Approach would have to develop and implement it on an extraordinarily short timeline.

Notably, an EPA official discussed a questionable compliance approach at the Western Regional Technical Conference on EPA's Clean Power Plan held by the Federal Energy Regulatory Commission (FERC) in Denver on February 25, 2015. Under questioning from FERC Commissioner Tony Clark, EPA Associate Administrator for Climate and Senior Counsel Joseph Goffman discussed an idea where states "could get an approvable plan in place, move forward and then over [time] in a more gradual fashion make any legal changes that would be required."<sup>43</sup> Goffman appeared to offer up, without explicit endorsement, the notion that state plans contingent on future legislation could be approved so long as a state committed to putting in place the necessary state laws in the future.

This raises significant legal issues, not the least of which is how a state air regulator and EPA can bind future state legislatures to specific legislation.<sup>44</sup> Any such action fundamentally conflicts with notions of democratic governance and legislative prerogatives. Accordingly, a state submitting a state plan premised on the Common Elements Approach with a soft commitment to pass the necessary authorizing

<sup>42</sup> California Air Resources Board, *Assembly Bill 32 Overview*, available at <http://www.arb.ca.gov/cc/ab32/ab32.htm>.

<sup>43</sup> Federal Energy Regulatory Commission Technical Conference on Environmental Regulations and Electric Reliability, Wholesale Electricity Markets, and Energy Infrastructure, Docket No. AD15-4-000, Transcript at 41:21-23 (Feb. 25, 2015), available at <http://www.ferc.gov/CalendarFiles/20150318075034-AD15-4-02-25-15.pdf>.

<sup>44</sup> See, e.g., Public Utilities Commission of Texas, Texas Railroad Commission, and Texas Council on Environmental Quality, Comments on Proposed Carbon Pollution Emission Guidelines for Existing Electric Generating Units, at 86, Docket ID No. EPA-HQ-OAR-2013-0602 (Dec. 1, 2014) (stating in part that "a state agency (presumably TCEQ and possibly PUCT) could not agree (as part of the [state plan] extension process) to bind a future Texas Legislature to pass the laws necessary for Texas to implement Rule 111(d)."), available at <http://www.regulations.gov/#!documentDetail;D=EPA-HQ-OAR-2013-0602-23305>. While the Texas state agencies raised this concept in the context of the proposed state plan extension criteria, the concept is equally applicable with regard to the compliance approach discussed by Mr. Goffman.

legislation at a later date would need to be prepared for near certain litigation and the compliance uncertainty the litigation would bring to the state, its EGU owners and operators, and its energy future.

## VII. Public Policy Considerations

The discussion of CO<sub>2</sub> budget trading regimes is particularly relevant as a matter of public policy in light of Washington Governor Jay Inslee's Carbon Accountability Act of 2015<sup>45</sup> and its proposal to direct the projected \$1 billion in annual revenues from the trading program towards transportation, education and disadvantaged communities. In addition, the state of New York has and is diverting RGGI revenues to the general fund.<sup>46</sup> The use of CO<sub>2</sub> trading to subsidize other state government activities may tempt states to follow approaches like the Common Elements Approach, without addressing the threshold issues discussed in this White Paper that could thwart CPP compliance efforts.

The notion of creating an intra-governmental cross-subsidy, however, faces ideological political opposition in some, and likely many, states. Moreover, it raises legal and practical questions, including whether this trading structure and revenue distribution results in a new tax subject to constraints imposed by state law, including specific legislative or even voter approval.<sup>47</sup>

<sup>45</sup> Washington Senate Bill 5283, available at <http://app.leg.wa.gov/billinfo/summary.aspx?bill=5283&year=2015>; Washington House Bill 1314, available at <http://app.leg.wa.gov/billinfo/summary.aspx?bill=1314&year=2015> (companion bills).

<sup>46</sup> Scott Waldman, *Sources: Lawmakers agree to sweep clean energy funds*, Capital New York (Mar. 26, 2015) ("State lawmakers have reached a tentative deal to move \$41 million from a clean energy fund and put it in the state's general fund. Under a deal reached Wednesday, lawmakers will put \$18 million of the revenue earned by the Regional Greenhouse Gas Initiative in to the Environmental Protection Fund, according to sources close to the talks. An additional \$23 million will go toward other programs, sources said .... RGGI has raised \$760 million since it started in 2008. Counting the additional amount this year, about \$130 million has been diverted from the fund since then.")

<sup>47</sup> The Colorado Constitution, for example, requires a vote of the people before the State or any local government may create new debt, levy new taxes, increase tax rates or institute tax policy changes directly causing a net tax revenue gain. Colo. Const. Art. X, § 20. According to a 2010 National Conference of State Legislatures study, 30 states have some kind of tax or expenditure limitation. Bert Waisanen, *State Tax and Expenditure Limits – 2010* (2010), available at

A critical issue is who owns the CO<sub>2</sub> currency, *e.g.*, utilities and their customers or state government, and where revenues flow based on this ownership. While RGGI revenues do and Carbon Accountability Act revenues would go into state coffers, many utilities trading excess RECs receive the revenues from these excess RECs and in some instances share them with customers. These are just a sample of the public policy and legal issues inherent in the CO<sub>2</sub> trading and cross-subsidization model proposed in Washington and implemented, *de facto*, in New York.

## VIII. Conclusion

The Nicholas brief and its authors have offered innovative solutions to some of the problems with the CPP, an environmental rule that controls state energy policy as opposed to a typical pollution control program. However, there are open issues and threshold questions that need to be addressed with regard to the Common Elements Approach proposal, specifically: (1) the need for state legislation; (2) further identification of minimum state components necessary to establish interstate congruency; (3) further inquiry and analysis of how this approach, both in form in substance, is consistent with the proposed and final CPP; (4) more discussion of the timing issues, although we do not fault the Common Elements Approach for being unable to solve that conundrum; and (5) consideration of peripheral public policy issues. The Common Elements Approach, though well-intentioned, has significant questions that need to be addressed before states can seriously consider it as a viable compliance option.

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<http://www.ncsl.org/research/fiscal-policy/state-tax-and-expenditure-limits-2010.aspx>. This white paper does not opine on whether the Common Elements Approach implicates these limits, as each is unique, but it remains a worthwhile consideration for states and policymakers evaluating this compliance strategy.

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