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Pennsylvania DEP Unveils Initial Draft of Carbon Dioxide Trading Rule to Air Quality Technical Advisory Committee

On February 13, 2020, the Pennsylvania Department of Environmental Protection presented its preliminary draft proposed rulemaking to establish a carbon dioxide budget trading program to the Air Quality Technical Advisory Committee (AQTAC). The proposed trading program would apply to fossil fuel-fired electricity generators of greater than 25 MW in Pennsylvania. The draft proposal reflects a first look at Pennsylvania DEP's vision for a cap-and-trade program as directed by Governor Tom Wolf's October 3, 2019 Executive Order 2019-07.

The draft proposed rule, although still in development, parallels the model rule prescribed by the Regional Greenhouse Gas Initiative (RGGI). RGGI is a coalition of 10 states in the Northeast and Mid-Atlantic that participate in a regional CO_2 cap-and-trade program for fossil fuel-fired electricity generating units that have a nameplate capacity of over 25 MWe. Under the program, each member state has a budget of CO_2 allowances, which it then allocates through set-aside programs, offsets, or periodic auctions. The number of allowances in each state's CO_2 budget that are allocated through auction varies widely among members. Each affected source ("CO_2 budget sources") is required to hold sufficient CO_2 allowances based on its CO_2 emissions as determined from continuous monitoring. Each allowance is equal to one ton of CO_2 emissions.

States' CO_2 budgets, and in turn, available allowances, periodically reduce over time. This requires each CO_2 budget source to either reduce CO_2 emissions as measured by continuous monitoring, or obtain extra CO_2 allowances to cover its emissions in excess of its allowance account. Under RGGI, auctions to obtain allowances generally occur quarterly, and may be open to qualified participants other than CO_2 budget sources. The draft proposed rule explicitly mentions financial institutions and environmental groups as potential auction participants. The proposal specifies an annual rather than quarterly auction process.

Unlike the majority of RGGI state members, Pennsylvania DEP has indicated that it does not intend to seek legislative authority to implement a CO_2 trading program, but rather, believes it has sufficient authority under the Pennsylvania Air Pollution Control Act. This position has been controversial, as some stakeholders contend that approval by the Pennsylvania General Assembly is necessary for such a trading program, including one that would involve other states. In November 2019, bills were introduced into the House (HB 2025) and Senate (SB 950) that would require General Assembly approval for any Pennsylvania carbon cap and trade program. This legal dispute is likely to give rise to significant ongoing challenges to the trading program rule.

FEBRUARY 18, 2020

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Pennsylvania DEP's draft proposed rule contains a number of differences from the RGGI model rule, most notably including:

- The proposed rule states that it is designed to reduce CO_2 emissions "in a manner that is protective of public health, welfare and the environment and is economically efficient," while the RGGI model rule only mentions economic efficiency in its statement of purpose. Numerous concerns were raised at the AQTAC meeting regarding the overall cost-effectiveness of the trading program, an analysis of which will be required under Pennsylvania's Regulatory Review Act, Commonwealth Attorneys Act, and the Climate Change Act. Pennsylvania DEP indicated that it is still assessing costs and benefits of the trading program. The overall economic impact of the regulation will be a critical issue to a variety of stakeholders as the rulemaking progresses.

- The draft proposed rule does not require the establishment of multi-state allowance auctions, as performed within RGGI. Rather, the draft proposal would give the Pennsylvania DEP discretion to hold auctions only within Pennsylvania if it determines, among other things, that its participation in a multi-state auction process would not provide more benefits than costs to Pennsylvania versus a statewide auction. There is no established timeframe in the draft proposed rule for Pennsylvania DEP to determine which approach it will take.

Pennsylvania DEP is operating on an accelerated timeframe to initiate and ultimately finalize the CO_2 budget trading program rulemaking. It intends to present a proposed version of the regulation to AQTAC in April 2020, at which point the Committee will vote on whether to advance the proposal to the Pennsylvania Environmental Quality Board. Pennsylvania DEP anticipates submitting the proposal to the EQB by July 2020 as required by Executive Order 2019-07. Assuming the EQB votes to adopt the regulation as a proposed rulemaking, public comments will be solicited in fall of 2020, and the final rulemaking could be promulgated by fall 2021. The Pennsylvania DEP expects the regulation to be effective in the first quarter of 2022.

Owners and operators of fossil fuel-fired electricity generating units greater than 25MW will be directly affected by the CO_2 budget trading program rulemaking if the rule is adopted in its currently-proposed form. In addition, the energy industry, manufacturers and consumers in general, are likely to be affected by the rulemaking based on the potentially far-reaching impacts to the nature of energy generation within Pennsylvania and regionally. Babst Calland's Climate Change attorneys are closely following this rulemaking. If you have questions about the proposed CO_2 budget trading program, please contact Kevin Garber, Jean Mosites, or Varun Shekhar.