Environment Land Use
& Natural Resources

May 16, 2016

EPA Charts Middle Path for Making "Stationary Source" and "Major Source" Determinations

In Clarifying Meaning of Term "Adjacent," EPA Rejects Industry's Most and Least Preferred Options

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A quarter mile is a common distance used for horse racing, drag racing, and track and field sprints. It is now also the farthest distance at which U.S. Environmental Protection Agency (EPA) will consider two emission sources to be "adjacent" for purposes of major source air permitting. Under a new EPA final rule applicable to upstream and midstream emission sources in the oil and gas sector, new or modified equipment or activities are "adjacent" if they are on the same surface site[1] or on sites that share equipment and are within one quarter mile of each other.

This definition of "adjacent" is critical because the adjacency of oil and gas equipment and activities is a key factor in determining whether they must be deemed a single "stationary source"[2] for purposes of the Prevention of Significant Deterioration (PSD) and Nonattainment New Source Review (NNSR) programs or a "major source"[3] for purposes of the Clean Air Act Title V operating permit program. Oil and natural gas production fields often cover large areas, and unlike many other industries, the expanse of land on which these commonly controlled operations are situated frequently is not owned or controlled by the

[1] 40 CFR §63.761 defines surface sites as "any combination of one or more graded pad sites, gravel pad sites, foundations, platforms, or the immediate physical location upon which equipment is physically affixed."

[2] The term "stationary source" is defined to mean ''any building, structure, facility, or installation which emits or may emit a regulated NSR pollutant.'' 40 CFR §§52.21(b)(5), 51.165(a)(1)(i), 51.166(b)(5). A "building, structure, facility, or installation" is defined as "all of the pollutant-emitting activities" that satisfy the following three elements: they "belong to the same industrial grouping"; "are located on one or more contiguous or adjacent properties"; and "are under the control of the same person (or persons under common control)." 40 CFR §§51.165(a)(1)(ii); 51.166(b)(6).

[3] 40 CFR §§70.2 and 71.2 define "major source" as ''any stationary source (or group of stationary sources that are located on one or more contiguous or adjacent properties, and are under common control of the same person (or persons under common control)) belonging to a single major industrial grouping….''

owner/operator of the production activity. The aggregated emissions of these single or major sources can result in greater regulatory obligations. Under this final "Source Determination Rule" adopted on May 12, 2016, onshore oil and gas equipment and activities must be treated as a single source if they share the same industry grouping, are under common control, and are located on the same site or on sites that share equipment and are within a one quarter mile of each other. The one quarter-mile boundary is measured from the center of the equipment at the new or modified source for construction permits.

EPA's proposed source determination rule in September 2015 put forward two options for defining "adjacent"; the second option threatened to implement a case-by-case evaluation of the functional interrelatedness between emitting equipment that was on separate, nearby sites. *See* Source Determination for Certain Emission Units in the Oil and Natural Gas Sector, 80 Fed. Reg. 56579 (Sept. 18, 2015). Industry opposed this option as without statutory support, inconsistent with the plain meaning of the term "adjacent," and overly subjective. EPA ultimately determined in this final rule that one quarter mile was a reasonable bright-line distance within which sources in oil and natural gas operations are likely to be interconnected. Thus, EPA will not consider any source more than one quarter mile distant from another "adjacent" for purposes of determining the source.

However, not all emitting equipment located on separate surface sites within one quarter mile of each other will be considered "adjacent" automatically. Instead, there must also be shared equipment necessary to process or store oil or natural gas in order for the separate surface sites within one quarter mile of each other to be aggregated as a single stationary source. Fortunately for industry, in adopting the "shared equipment" test, EPA rejected as overly vague its previously proposed generalized notion of "functional interrelatedness." According to EPA, examples of shared equipment include produced fluids storage tanks, phase separators, natural gas dehydrators, or emissions control devices. In addition, two well sites that feed to a common pipeline are not part of the same stationary source if there is no commonly shared processing or storage equipment between them. Separate surface sites within one quarter mile of each other that do not include shared emitting equipment will not be aggregated.

By replacing its previous policy interpretation and guidance with a somewhat more bright line rule, EPA hopes the clarity of the term "adjacent" for permitting authorities and industry will result in more consistent determinations of the scope of a source.

The final rule, which only applies prospectively, will become effective 60 days after its publication in the Federal Register. It is applicable to industry groups with the following industrial codes:

Industry Groups Affected	NAICS Code
Oil and Gas Extraction	21111
Crude Petroleum and Natural Gas Extraction	211111
Natural Gas Liquid Extraction	211112
Drilling Oil and Gas Wells	213111
Support Activities for Oil and Gas	213112

EPA is not requiring states with EPA-approved permitting programs to apply the new meaning of the term "adjacent." State and local regulatory authorities with EPA-approved programs continue to have discretion to make source determinations for the oil and gas sources. However, states that administer permitting programs under a delegation of federal authority must follow EPA's final rule. At the same time, states with local air quality concerns may adopt more stringent requirements.

Determining the adjacency of sources and the scope of a single source or major source has been a confusing and subjective process for regulated industry. Many in industry argued that "adjacent" is an unambiguous term that should be defined by the dictionary, in which case "adjacent" would mean contiguous, abutting or touching. The definition of "adjacent" had not been clarified previously in a formal rulemaking, only informal agency guidance. EPA advanced an interpretation that the "functional interdependence" or "functional interrelatedness" of sources should be considered in determining whether they are located on "adjacent" properties. Determinations based on the functional interrelatedness of nearby—but not adjoining—operations were appealed. In *Summit Petroleum Corp. v. EPA*, 690 F.3d 733, 742 (6th Cir. 2012), EPA had looked at the interrelatedness of a natural gas sweetening plant and multiple sour gas production wells within an eight-mile radius to determine that all the sources were major sources. EPA had concluded that Summit's facilities satisfied the regulatory requirement of being "located on ... adjacent properties" because, although physically independent, they were truly interrelated. *Id.* at 735. On appeal, the Sixth Circuit held the term "adjacent" to be unambiguous, looked to the dictionary, and rejected EPA's more expansive interpretation. The Sixth Circuit held that EPA's use of interrelatedness in determining whether sources were "adjacent" was unreasonable and contrary to the plain meaning of the term.

EPA attempted to limit the effect of the *Summit Petroleum* decision by issuing a memorandum (*Summit* Directive), which stated EPA would follow the Sixth Circuit's decision only in the four states within that court's jurisdiction (Michigan, Ohio, Kentucky and Tennessee), and that it would continue to apply its preferred approach to source aggregation in other circuits. The D.C. Circuit invalidated the *Summit* Directive soon after. *Nat'l Envtl. Dev. Ass'n's Clean Air Project v. EPA*, 752 F.3d 999 (D.C. Cir. 2014) (*NEDACAP*). The D.C. Circuit in NEDACAP held that the *Summit* Directive was "plainly contrary to the agency's own 'Regional Consistency' rules" (40 C.F.R. Part 56), which express a "firm commitment to national uniformity in the applications of its permitting rules," and do not provide an exemption for judicial decisions that the agency finds disfavorable. *Id.* at 1009-10. The court offered EPA three alternatives: (1) revise regulations for aggregating emissions from multiple facilities so that functionally interrelated rather than adjacent facilities are aggregated, (2) appeal to the Supreme Court (which EPA did not do), or (3) revise the regional consistency regulations to allow for regional variances created by judicial decisions or circuit splits. *See id.* at 1010.

Prompted by the *Summit Petroleum* and *NEDACAP* decisions, EPA has attempted to follow the *NEDACAP* court's first and third alternatives and revise both its source aggregation regulations and its regional consistency regulations. Under EPA's proposal to amend its regional consistency regulations—which is not yet finalized—only decisions of the U.S. Supreme Court or the D.C. Circuit that arise from challenges to nationally applicable regulations or EPA actions will apply uniformly across all states. *See* "Amendments to Regional Consistency Regulations," 80 Fed. Reg. 50250 (Aug. 19. 2015). EPA Headquarters' employees would not need to revise existing regulations or policies to address decisions arising from challenges to locally or regionally applicable actions. In addition, EPA regional employees would not need to seek concurrence from Headquarters to act inconsistently with national policy if inconsistent action is required to comply with a federal court decision.

In the source determination rule, EPA rejects the premise that the Sixth Circuit's reference to the dictionary definition of "adjacent" in *Summit Petroleum* precludes EPA from ignoring the dictionary and promulgating a more expansive definition in this rulemaking. EPA argues that the Sixth Circuit was interpreting a term not defined by a rule, and EPA now should be accorded deference because it is defining a term in a formal rulemaking procedure.

Nevertheless, the legal status of the new source determination rule is questionable, particularly in the Sixth Circuit, because EPA redefines rather than removes the adjacency element and has not yet finalized its regional consistency policy. With the current regional consistency policy still in effect, and the Sixth Circuit's holding that "adjacent" was unambiguous, the final source determination rule takes us back to *Summit Petroleum*. Moreover, the proposed amendments to the regional consistency policy, even if finalized, are questionable by themselves, given that the proposed changes would allow regional differences that may conflict with Clean Air Act section 301(a)(2)'s call for national uniformity. The Sixth Circuit in *NEDACAP* did not decide "whether the CAA allows EPA to adopt different standards in different circuits," so that question remains open. *See NEDACAP*, 752 F.3d at 1011.

While most industry likely would have preferred for EPA to endorse the literal dictionary definition of "adjacent" as the Sixth Circuit did in *Summit Petroleum*, the quarter-mile proximity radius and consideration of "shared equipment" rather than "interrelatedness" provides relatively more certainty. Therefore, although EPA did not endorse its preference, industry can breathe a sigh of relief that EPA did not adopt a more subjective standard unbounded by a specific geographic boundary and requiring a case-by-case evaluation of functional interrelatedness.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors below.

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