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COMMENTARY

Evolution of Source Determination for Certain Emission Units in the Oil and Natural Gas Sector

On August 2, 2016, the Environmental Protection Agency's ("EPA") final rule regarding the aggregation of physically separate emitting surface sites into a single source for permit determinations in the oil and natural gas industry took effect.[1] This Source Determination for Certain Emission Units in the Oil and Natural Gas Sector rule came alongside updates to New Source Performance Standards ("NSPS").[2] These rules are part of President Obama's *Climate Action Plan: Strategy to Reduce Methane Emissions* and the Clean Air Act ("CAA"). Through this rulemaking, EPA has set out to clarify the term "adjacent" as applied to the determination of whether or not physically separate emitting sites in the onshore oil and gas sector should be aggregated into a single "stationary source" for the purposes of the Prevention of Significant Deterioration ("PSD") and Nonattainment New Source Review ("NNSR") programs and "major source" permitting under Title V of the CAA.[3]

Prior to this new rule, individual policy interpretations, the *Summit* litigation,[4] and resulting guidance have created uncertainty over the correct interpretation of "adjacent" as applied to determining whether individual sources should be aggregated as a single source for purposes of air permitting. The final EPA source determination rule states that EPA will consider pollutant-emitting activities adjacent when they are: (i) located on the same surface site or (ii) located within a quarter mile from each other (as measured from the center of the emitting equipment) *and* share equipment.[5] EPA asserts that this new definition of "adjacent" will allow permit applicants and permitting authorities in the oil and natural gas industry to make source determinations with greater ease and clarity.

Existing Legal Framework

Consistent with the term's use in § 111(a)(3) of the CAA, EPA defines a "stationary source" as "any building, structure, facility, or installation which emits or may emit a regulated NSR pollutant."[6] EPA promulgated an earlier stationary source determination regulation[7] that outlined three factors to aid permitting authorities in making these single source determinations:

- Same industrial grouping per Standard Industrial Classification ("SIC") codes,
- Location on contiguous or adjacent properties, and
- Common control of the same person or persons.

If these three factors are present, EPA aggregates the separate emitting activities into a single stationary source. Initially, permitting authorities made these determinations on a case-by-case basis without a clear indication of the meaning of "adjacent" or how each factor should be judged or weighed against one another.

When interpreting the meaning of "adjacent" within individual policy determinations, EPA focused generally on determining whether or not emitting activities met the "common sense notion of a plant"[8] until EPA Acting Assistant Administrator William Wehrum issued the Wehrum Memo in 2007.[9] The memorandum directed permitting authorities to focus on the location and proximity of each surface site, rather than the operational dependency of each site, to determine if two separate properties were adjacent. In 2009, the McCarthy Memo withdrew the Wehrum Memo.[10] The McCarthy Memo instructed permitting authorities to refocus on all three factors in the regulation, noting that permitting authorities must justify aggregation conclusions by reviewing all the factors, not just physical proximity.

The confusion continued following the Sixth Circuit's decision in the *Summit Petroleum* case.[11] In 2010, focusing on the interdependent nature of the operations, EPA aggregated Summit Petroleum's physically separate sweetening plant facilities into a single source for permitting purposes. In making this determination, EPA focused on the fact that all of Summit's wells were located within an eight-mile radius of its sweetening plant that processed all of the oil and gas from the connected wells. Upon review, the Sixth Circuit disagreed with the aggregation of these dispersed wells and plant, and it held that EPA's determination that these facilities were "adjacent" was unreasonable and contrary to the plain meaning of the unambiguous term.[12]

EPA responded to this decision by issuing the *Summit* Directive.[13] This directive instructed regional offices outside of the Sixth Circuit to disregard the *Summit* decision and to continue considering interrelatedness in the "adjacency" factor of the single source determination. The D.C. Circuit Court invalidated the *Summit* Directive because it violated EPA's "Regional Consistency" regulations and gave facilities located within the Sixth Circuit a competitive advantage.[14] The "Regional Consistency" regulations require EPA officials to "assure fair and uniform application by Regional offices of the criteria, procedures, and policies employed in implementing and enforcing the [Clean Air Act]."[15] The court saw the *Summit* Directive as placing companies and producers outside of the Sixth Circuit at a competitive disadvantage as they were more likely to have their operations aggregated into a single source for permitting purposes.[16] Following this decision, permitting authorities and applicants in the oil and gas industry were left without any definitive interpretation of the meaning of "adjacent" in source determinations.

New EPA Source Determination Rule

In an effort to resolve the ambiguity surrounding the meaning of "adjacent," EPA proposed the source determination rule for comment on September 18, 2015.[17] The proposed rule originally considered two options for the definition of "adjacent." The first of these options, which EPA preferred, centered around proximity and would have required permitting authorities to aggregate all onshore oil and natural gas activities located within a quarter-mile radius of each other.[18] The second option defined "adjacent" to include exclusively functionally interrelated equipment and would have aggregated all emitting equipment not only within the quarter-mile radius, but also beyond a quarter mile if the operations of each surface site were functionally dependent upon one another.[19] In both options, one would consider only the adjacency of equipment if that equipment is under common control. Rather than finalizing one of the originally proposed options, EPA selected a hybrid approach to the definition of "adjacent" as a reaction to comments by state permitting officials and applicants in the oil and gas industry.

The definition of "adjacent" in the final rule focuses on the proximity of the emitting activities under common control but also considers whether or not these emitting activities share common equipment. The final rule states that, "Pollutant emitting activities shall be considered adjacent if they are located on the same surface site; or if they are located on surface sites that are located within ¼ mile of one another (measured from the center of the equipment on the surface site) *and* they share equipment."[20] Under this new rule, EPA will consider such operations "adjacent" and will aggregate the emitting activities as a single source if the onshore activities are under SIC Major Group 13 and are under common control of

the same person. A "surface site" refers to any combination of one or more graded pad sites, gravel pad sites, foundations, platforms, or the immediate physical location upon which equipment is physically attached.[21] For aggregation of individual emitting locations under common control to meet the "common sense notion of a plant," it is necessary that the sites: (i) are located within a quarter mile of each other *and* (ii) share common equipment. If only one of these two conditions is met, EPA will not aggregate the sites into a single source.

Many commenters preferred option one over option two in the proposed rule because it offered a "bright-line" approach and was consistent with what they considered the plain meaning of "adjacent."[22] Multiple state and industry commenters, however, recommended a revision to this option. The commenters requested EPA to consider only emitting activities located within a quarter mile of one another as adjacent if they *also* satisfied the "common sense notion of a plant."[23] Additionally, two state commenters noted that while they use the quarter-mile boundary, they view it as an outer edge where all emitting activity beyond the edge is excluded, but all of the activity within it is not automatically aggregated.[24]

EPA selected the quarter-mile radius for the distance to measure "adjacency" after reviewing comments that proposed a broad range of distances. EPA retained the proposed quarter-mile distance to remain consistent with states that already use this measurement.[25] EPA rejected comments that recommended basing the distance on individual leases, finding that this would complicate the permitting process.[26] The quarter-mile distance is consistent with many existing state regulations and corresponds to a 40-acre lease. [27]

In the proposed rule, EPA requested comment on how to measure the quarter-mile radius. Commenters in the oil and gas industry preferred the measurement from the emitting equipment, while state commenters favored the property boundary line.[28] EPA ultimately agreed with the comments from the oil and gas industry, and thus, the new rule will establish the boundary from the center of the emitting equipment on the surface site of the new or modified source.[29] For an oil or gas well, this may be the wellhead, and for any type of surface site, the distance is measured from the center of the emitting activities. EPA determined this measurement would be easier to establish and enforce than the property boundary line.[30]

The final rule also offers some guidance on the meaning of "shared equipment," stating that shared equipment includes, but is not limited to, "produced fluid storage tanks, phase separators, natural gas dehydrators, or emissions control devices."[31] While that type of shared equipment would be considered a single source, EPA clarified that two individual well sites that feed into a common pipeline and do not share any of the same processing or storage equipment would not be considered a single source.[32] EPA indicated that the notion of shared equipment better satisfies the "common sense notion of a plant" in oil and gas operations than a focus on the "functional interrelatedness" of two sites.[33]

In its response to the comments on the proposed rule, EPA also addressed the problem of a "daisy chain" and rejected its application as stretching beyond the "common sense notion of a plant." [34] A "daisy chain" exists when each individual emitting unit under common control is located within a quarter mile of the next emitting unit, but the first and the last unit in the chain are separated by a much greater distance than one-fourth of a mile. Most of the commenters opposed "daisy chaining" and were concerned that it would extend the boundary for aggregation dozens of miles.[35] For example, under the new rule, if two sites of common ownership, A and B, were within one-fourth of a mile of one another, and B fed its produced water to the tank on site A, then A and B would be considered part of the same stationary source. If the same owner established a drilling well, C, within a quarter mile of site B, but more than one-fourth of a mile from A, and sites B and C did not share equipment, then under the new rule, C would be considered a single stationary source. If, however, the same owner constructed a well, D, within one-fourth of a mile from A, and it fed its produced water to site A, then D would be considered a modification to the source of A/B.[36] EPA expects the permitting authority to make these determinations on an individual case-by-case basis using this guidance. [37]

Similar to other EPA rules, the source determination rule applies prospectively and took effect on August 2, 2016.[38] EPA indicated that the rule does not apply retroactively, meaning that previous determinations will not be revisited unless the site undergoes modification.[39] Additionally, while EPA is adopting this definition of "adjacent" to apply to permits issued by EPA and by states to which EPA has delegated

federal authority, EPA is not requiring the revision of state and local EPA-approved permitting programs.[40]

Impact of the New Rule

It appears that the three factors EPA uses to define "adjacent" for sites under common control—(i) location on the same surface site, (ii) a quarter-mile distance (measured from the center of the equipment or emissions), and (iii) shared equipment—will bring long-awaited clarity to the definition of "adjacent" in onshore oil and gas source aggregation decisions. Nevertheless, there will continue to be to be inconsistent source determinations in the oil and gas sector as EPA makes new source determinations. For example, operators will likely struggle to fully understand what is meant by "shared equipment." In explaining its inclusion of produced fluids storage tanks, phase separators, natural gas dehydrators, or emissions control devices as shared equipment, EPA states that "the shared equipment is necessary for the operation of the new well site, and should be considered part of the same source because together all of the equipment operates as a 'plant.'"[41] Questions over what equipment is "necessary" and operates "together" as a plant will likely arise as operators struggle to determine when equipment utilized by multiple locations is more similar to a common pipeline, which EPA does not consider shared equipment, or a dehydration unit that is connected to multiple locations via pipe, which EPA considers to be shared equipment. Similarly, by not requiring states to adopt the definition for their permitting programs, operators are likely to see variation in oil and gas source aggregation decisions depending on jurisdiction.

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Endnotes

1 40 C.F.R. §§ 51, 52, 70, 71.

2 40 C.F.R.§ 60.

3 80 Fed. Reg. 56,579, 56,579 (Sept. 18, 2015).

4 *Summit Petroleum Corp. v. EPA*, 690 F.3d 733 (6th Circ. 2012), *reh'g en banc denied*, No. 09-4348/10-4572, 2012 U.S. App. LEXIS 23988 at *1 (6th Cir. Oct. 29, 2012). (Explaining that the term "adjacent" is unambiguous and implies physical proximity in geographic location rather than functional interrelatedness).

5 40 C.F.R. §§ 51.165(a)(i)(ii)(B), 51.166(b)(6)(ii), 52.21(b)(6)(ii), 70.2, 71.2.

6 40 C.F.R. §§ 52.21(b)(5), 51.165(a)(1)(i), 51.166(b)(5).

7 40 C.F.R. § 51.166(b)(6).

8 45 Fed. Reg. 52,676 (Aug. 7, 1980).

9 Memorandum from William L. Wehrum, Office of Air and Radiation, to EPA Regional Admin. I-X, Source Determinations for the Oil and Gas Industries (Jan. 12, 2007).

10 Memorandum from Gina McCarthy, Office of Air and Radiation, to EPA Regional Admin., Regions I-X. Withdrawal of Source Determinations for Oil and Gas Industries (Sept. 22, 2009).

11 *Summit Petroleum Corp.*, 690 F.3d at 751.

12 *Summit Petroleum Corp*, 690 F.3d at 741-44. ("The dictionary definition of 'adjacent' implies physical proximity … The EPA's interpretation of the term 'adjacent,' to which no deference is owed, runs contrary to its plain meaning.").

13 Memorandum from Stephen D. Page, Office of Air Quality Planning Standards, to Regional Air Division Directors I-X, Applicability of the Summit Decision to EPA Title V and NSR Determinations (Dec. 21, 2012).

14 *Nat'l Envtl. Dev. Ass'ns Clean Air Project v. EPA*, 752 F.3d 999, 1003 (D.C. Cir. 2014).

15 *Id.* at 1004 (citing 40 C.F.R. § 56.3(a)).

16 *Id.* at 1005.

17 45 Fed. Reg. at 56,579.

18 45 Fed. Reg. at 56,586.

19 45 Fed. Reg. at 56,587.

20 40 C.F.R. §§ 51.165(a)(i)(ii)(B), 51.166(b)(6)(ii), 52.21(b)(6)(ii), 70.2, 71.2.

21 40 C.F.R. § 63.762.

22 Source Determination for Certain Emission Units in the Oil and Natural Gas Sector, 81 Fed. Reg. 35,622, 35,626 (June 3, 2016).

23 *Id.*

24 *Id.* at 35,627.

25 *Id.* at 20.

26 *Id.* at 35,627.

27 *Id.*

28 *Id.* at 35,627-28.

29 *Id.* at 35,628.

30 *Id.*

31 40 C.F.R. §§ 51.165(a)(i)(ii)(B), 51.166(b)(6)(ii), 52.21(b)(6)(ii), 70.2, 71.2

32 *Id.*

33 81 Fed. Reg. 35,629.

34 *Id.* at 38,627.

35 *Id.*

36 *Id.*

37 *Id.*

38 *Id.* at 35,630.

39 *Id.*

40 *Id.*

41 81 Fed. Reg. at 35,624.