FULBRIGHT
& Jaworski L.L.P.
Attorneys at Law

98 San Jacinto Boulevard, Suite 1100 • Austin, Texas 78701
psarahan@fulbright.com • Direct: 512 536 2493 • Main: 512 474 5201 • Facsimile: 512 536 4598

October 30, 2012

Docket Clerk
Texas Commission on Environmental Quality
P. O. Box 13087
Austin, Texas 78711-3087

VIA HAND DELIVERY

Re: Use Determination Application No. 16413
TCEQ Docket No. 2012-1648-MIS-U
Brazos Electric Power-Cooperative, Inc.; Jack County Generation Facility

Dear Sir/Madam:

Enclosed please find the original and 8 copies of the Reply Brief of Appellant Brazos Electric Power-Cooperative, Inc. in connection with the above referenced matter. Please file the attached and return the endorsed copy to our courier.

We are providing copies of this reply brief to the individuals and entities identified on the Commission's mailing list from Docket No. 2012-1648-MIS-U.

Please contact our office should you have any questions. Thank you for your assistance.

Very truly yours,

Paul Sarahan

PCS/pd
Enclosures

TEXAS COMMISSION ON ENVIRONMENTAL QUALITY
2012 OCT 30 PM 12:39
CHIEF CLERKS OFFICE

cc:

Chief Appraiser Jack County Appraisal District P.O. Box 958 Jacksboro, Texas 76058 Telephone: 940/567-6301 Facsimile: 940/567-3640 E-mail: jcad@wf.net	Chance Goodin TCEQ Office of Air MC 206 P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-6335 Facsimile: 512/239-6188 E-mail: chance.goodin@tceq.texas.gov
Steve Hagle, Deputy Director TCEQ Office of Air MC 122 P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-2104 Facsimile: 512/239-3341	Robert Martinez TCEQ Environmental Law Division MC 173 P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-0600 Facsimile: 512/239-0606
Blas Coy TCEQ Office of Public Interest Counsel MC 103 P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-6363 Facsimile: 512/239-6377	Docket Clerk TCEQ Office of Chief Clerk MC 105 P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-3300 Facsimile: 512/239-3311
Kyle Lucas TCEQ Alternative Dispute Resolution Program MC P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-0687 Facsimile: 512/239-4015	C. Wayne Frazell, P.E., RPA Pritchard & Abbott, Inc. 4900 Overton Commons Court Ft. Worth, Texas 76132-3687 Telephone: 817/926-7861 Facsimile: 817/927-5314 E-mail: wfrazell@pandai.com

TCEQ DOCKET NO. 2012-1648-MIS-U

Appeal of Executive Director's Use Determination Issued to Brazos Electric Power Cooperative, Inc.; Jack County Generation Facility CN600128821 / RN100221985 Application No. UD 16413	§ § § § § §	**Before the Texas Commission on Environmental Quality**

CHIEF CLERK'S OFFICE
2012 OCT 30 PM 12:39
TEXAS COMMISSION ON ENVIRONMENTAL QUALITY

BRAZOS ELECTRIC POWER COOPERATIVE, INC.'S REPLY TO THE EXECUTIVE DIRECTOR'S RESPONSE TO THE APPEALS FILED ON THE NEGATIVE USE DETERMINATION FOR THE HEAT RECOVERY STEAM GENERATOR APPLICATIONS

TO THE HONORABLE COMMISSIONERS OF THE TCEQ:

COMES NOW, Brazos Electric Power Cooperative, Inc. ("BEPC") and files its Reply to the Executive Director's Response to the Appeals Filed on the Negative Use Determinations for the Heat Recovery Steam Generator Applications. BEPC has met the statutory and regulatory requirements to establish its eligibility for a positive use determination, as set forth in its application, its appeal, this Reply and the record before the Commission. The Executive Director's negative use determination is not supported by the facts or the law, is contrary to TEX. TAX CODE § 11.31(k), (m), and 30 TEX. ADMIN. CODE § 17.17(b), is contrary to the evidence presented by BEPC and others similarly situated,[1] and cannot stand. BEPC, therefore,

[1] The argument and evidence presented by those similarly situated is incorporated herein by reference as if fully set forth herein including, without limitation, the argument and evidence presented in relation to Application Nos. UD 07-11914 (Tenaska Gateway Partners, Ltd- Rusk County); UD 07-11966 (Freestone Power Generation, L.P. – Freestone County); UD 07-11971 (Borger Energy Associates, L.P.- Hutchinson County); UD 07-11969 (Brazos Valley Energy, L.P.- Fort Bend County); UD 07-11994 (Freeport Energy Center, L.P.- Brazoria County); UD 07-11926 (CER-Colorado Bend Energy LLC (f/k/a Navasota Wharton Energy Partners, L.P .) -Wharton County); UD 12696 (EN Service's LP- Harrison County); UD 16409 (Bosque Power Company, LLC- Bosque County); UD 12210 & 12211 (Topaz Power Group, LLC- Nueces County); UD 15506, 16410, 16411 & 16412 (Cottonwood Energy Company LP - Newton County); UD 12268 (WolfHollow I, LP- Hood County); UD 13534 (South Texas Electric Cooperative, Inc. –Victoria County); UD 13544 (Brazos Electric Cooperative, Inc.- Johnson County); UD 12004 (NRG Texas Power LLC- Limestone County); UD 07-12271 (Midlothian Energy Limited Partnership – Ellis County); UD 07-12202 (Wise County Power Company, LLC- Wise County); UD 07-12203 (Ennis Power Company, LLC- Ellis County); UD 15020 (Motiva Enterprises, LLC- Jefferson County); UD 07-12272 (Hay Energy Limited Partnership- Hays County); and UD 12826 (GIM Channelview Cogeneration LLC- Harris County).

respectfully requests that the Commission remand this matter to the Executive Director for a new determination consistent with the applicable statute and its rules.

I. Overview

A. Procedural Overview

BEPC filed Application No. 16413 for a Use Determination for Pollution Control Property on March 7, 2012, for a heat recovery steam generator at its Jack County Generation Facility (the "Plant'). A copy of this application is attached hereto as Attachment A. On April 19, 2012, the Executive Director issued to BEPC the results of TCEQ's administrative completeness review, a copy of which is attached hereto as Attachment B. TCEQ performed a review of the application for technical completeness, a copy of which was provided to BEPC for the first time as an attachment to the Executive Director's Response in this matter. A copy of this Application Review Summary is attached hereto as Attachment C.[2] On July 10, 2012, TCEQ issued a Notice of Negative Use Determination regarding Application No. 16413, a copy of which is attached hereto as Attachment D. The notice was addressed to BEPC's agent for the matter, Mr. Jim Harris of H&H Associates. Mr. Harris received the notice on July 12, 2012, as stated in Mr. Harris's affidavit, attached hereto as Attachment E. BEPC timely filed its appeal of the negative use determination on August 1, 2012. For evidentiary purposes, a certified copy of TCEQ's records related to Application No. 16413 is attached hereto as Attachment F.

B. Eligibility Requirements

1. Tax Code Requirements

Under TEX. TAX CODE § 11.31, a person is entitled to an exemption from taxation of all or part of real and personal property that the person owns and that is used wholly or partly as a

[2] A copy of the Executive Director's Technical Review Checklist, which was apparently created and used to support the Application Review Summary, is included within the TCEQ's records related to Application No. 16413, attached hereto as Attachment F.

facility, device, or method for the control of air, water, or land pollution. TEX. TAX CODE § 11.31(a). A "facility, device, or method for the control of air, water, or land pollution" means land that is acquired after January 1, 1994, or any structure, building, installation, excavation, machinery, equipment, or device, and any attachment or addition to or reconstruction, replacement, or improvement of that property, that is used, constructed, acquired, or installed wholly or partly to meet or exceed rules or regulations adopted by any environmental protection agency of the United States, this state, or a political subdivision of this state for the prevention, monitoring, control, or reduction of air, water, or land pollution. *Id.* at § 11.31(b).

In applying for an exemption under this section, a person seeking the exemption shall present in a permit application or permit exemption request to the executive director of the Texas Commission on Environmental Quality ("TCEQ" or the "Commission") information detailing:

(1) the anticipated environmental benefits from the installation of the facility, device, or method for the control of air, water, or land pollution;

(2) the estimated cost of the pollution control facility, device, or method; and

(3) the purpose of the installation of such facility, device, or method, and the proportion of the installation that is pollution control property.

Id. at § 11.31(c). If the installation includes property that is not used wholly for the control of air, water, or land pollution, the person seeking the exemption shall also present such financial or other data as the executive director requires by rule for the determination of the proportion of the installation that is pollution control property. *Id.*

The Texas Legislature required the TCEQ to adopt rules establishing a nonexclusive list of facilities, devices, or methods for the control of air, water, or land pollution, and required that the list include, among other things, heat recovery steam generators. *See id.* at § 11.31(k). TCEQ

may only remove an item from the list if TCEQ finds, through a rulemaking process, compelling evidence to support the conclusion that the item does not provide pollution control benefits. *Id.* at § 11.31(l). TCEQ has neither proposed nor adopted rulemaking to remove heat recovery steam generators from the list.

2. TCEQ's Regulatory Requirements

To obtain a positive use determination, the pollution control property must be used, constructed, acquired, or installed wholly or partly to meet or exceed laws, rules, or regulations adopted by any environmental protection agency of the United States, Texas, or a political subdivision of Texas, for the prevention, monitoring, control, or reduction of air, water, or land pollution. TEX. ADMIN. CODE § 17.4(a). In addition, pollution control property must meet the following conditions.

(1) Property must have been constructed, acquired, or installed after January 1, 1994;

(2) Land must include only the portion of the land acquired after January 1, 1994, that actually contains pollution control property;

(3) Equipment, structures, buildings, or devices must not have been taxable by any taxing unit in Texas on or before January 1, 1994, except that if construction of pollution control property was in progress on January 1, 1994, that portion of the property constructed, acquired, or installed after January 1, 1994, is eligible for a positive use determination; and

(4) Property purchased from another owner is eligible for a positive use determination if it is acquired, constructed, or installed by the new owner after January 1, 1994, will be used as pollution control property, and was not taxable by any taxing unit in which the property is located on or before that date.

Id.

The executive director shall determine the portion of the pollution control property eligible for a positive use determination. *Id.* at § 17.4(b). The executive director may not make a determination that property is pollution control property unless all requirements of § 17.4 and the applicable requirements of §§ 17.15 and 17.17 have been met. *Id.* at § 17.4(c). Property is not entitled to an exemption from taxation if the property is used, constructed, acquired or installed wholly to produce a good or provide a service; or if the property is not wholly or partly used, constructed, acquired or installed to meet or exceed law, rule, or regulation adopted by any environmental protection agency of the United States, Texas, or a political subdivision of Texas for the prevention, monitoring, control, or reduction of air, water, or land pollution. *Id.* at § 17.6(1)(C).

To be granted a use determination, a person shall submit to the executive director a completed and signed commission application form and one copy of the completed, signed form; and the appropriate fee. *Id.* at § 17.10(a). Along with the name of the appraisal district for the county in which the property is located, all use determination applications must contain at least the following:

(1) the anticipated environmental benefits from the installation of the pollution control property for the control of air, water, and/or land pollution;

(2) the estimated cost of the pollution control property;

(3) the purpose of the installation of such facility, device, or method, and the proportion of the installation that is for pollution control, such as, if deemed by the executive director to be relevant and essential to the use determination, a detailed description of the pollution source and a detailed and labeled process flow diagram that clearly depicts the pollution control property and the processes and equipment that generate the pollutant(s) being controlled;

(4) the specific sections of the law(s), rule(s), or regulation(s) being met or exceeded by the use, installation, construction, or acquisition of the pollution control property; and

(5) if the installation includes property that is not used wholly for the control of air, water, and/or land pollution and is not on the Tier I Table, a worksheet showing the calculation of the Cost Analysis Procedure, §17.17(c), and explaining each of the variables.

Id. at § 17.10(d).

TCEQ adopted an Expedited Review List as a nonexclusive list of facilities, devices, or methods for the control of air, water, and/or land pollution. *Id.* at § 17.17(b). This table consists of the list located in TEX. TAX CODE, §11.31(k), with a few minor variations, none of which is applicable to a review of Application No. 16413. *See id.* The table includes heat recovery steam generators ("HRSGs") among the "facilities, devices, or methods for the control of air, water, and/or land pollution." *See id.*

The following calculation, or cost analysis procedure ("CAP"), must be used to determine the creditable partial percentage for a property that is filed on a Tier III application:

[(Production Capacity Factor x Capital Cost New) – Capital Cost Old – NPVMP] / Capital Cost New x 100

Id. at § 17.17(c)(1).

C. Facts Set Forth in Application

BEPC Application No. 16413 met the requirements set forth in TEX. TAX CODE § 11.31 and TEX. ADMIN. CODE §§ 17.4, 17.10, 17.17. Through its application, BEPC identified the pollution control equipment as a "Heat Recovery Steam Generator (HRSG) and Dedicated Ancillary Systems;" acknowledged it was seeking a partial positive use determination; and asserted its qualification as pollution control equipment under TEX. TAX CODE § 11.31(k), and

No. B-8 on the Expedited Review List included in TEX. ADMIN. CODE § 17.17(b). A description of the property, a citation to the rule being met through the installation of the HRSG, and a description of the anticipated environmental benefit related to the installation of the HRSG were included as Attachment 1 of the application. See Attachment A. A process flow diagram and a plot plan were included as Attachments 2 and 3 of the application, respectively. Finally, a calculation, using TCEQ's CAP, was included as Attachment 4 of the application. Through its application, BEPC sought a partial positive use determination in the amount of 74.66%.

D. The Executive Director's Negative Use Determination

On July 10, 2012, the Executive Director issued a Negative Use Determination for Application No. 16413, and for every other application pending before the TCEQ that sought a use determination for a HRSG. In each of the negative use determinations, the Executive Director provided a single sentence in support of his decision, "Heat recovery steam generators and associated dedicated ancillary equipment are used solely for production; therefore, (sic) are not eligible for a positive use determination." As stated above, BEPC received notice of the negative use determination on July 12, 2012, and timely filed its appeal of the negative use determination on August 1, 2012.

II. Discussion

The Executive Director's negative use determination stands or falls on the validity of his assertion that a HRSG is used solely for production purposes and therefore is not eligible for a positive use determination. The Commission should remand this matter to the Executive Director because the determination is not supported by the law or the facts. As shown below, a HRSG is a device for the control of air pollution; the installation of a HRSG results in environmental benefits; BEPC acquired, installed and uses its HRSG, after January 1, 1994,

wholly or partly to meet or exceed EPA regulations; and BEPC utilized TCEQ's CAP, which is used to determine the creditable partial percentage for a property that is filed on a Tier III application, to support its claim for a positive use determination.

For purposes of clarity, this Section of the Reply is organized according to the elements established by the Legislature governing eligibility for a positive use determination. It concludes with an analysis of additional issues raised by the Executive Director, and an analysis of applicable standards for reviewing legislative and regulatory intent.

A. A HRSG is a Device for the Control of Air Pollution

A HRSG is a device for the control of air pollution, both from a legal and technical perspective. The Texas Legislature established a HRSG as a pollution control device in its enactment of HB 3732, which has been codified in TEX. TAX CODE § 11.31(k). TCEQ adopted rules confirming this status, and TCEQ has neither proposed nor adopted rules that would change this status. From a technical perspective, the use of a HRSG allows an entity to reduce air pollution, as described in further detail below.

1. The Texas Legislature Determined that a HRSG is a Pollution Control Device

In 2007, the Texas Legislature amended TEX. TAX CODE § 11.31 to require TCEQ to "adopt rules establishing a nonexclusive list of facilities, devices, or methods for the control of air, water, or land pollution." TEX. TAX CODE § 11.31(k). The Legislature went further though, by requiring that this list include, among other things, heat recovery steam generators. *Id.* By doing so, the Legislature mandated that TCEQ consider HRSGs to be pollution control devices. While the Legislature provided a mechanism for deleting a device from the list based on compelling evidence, through its enactment of TEX. TAX CODE § 11.31(l), TCEQ has not chosen to do so with respect to HRSGs or any other device or method specifically identified in TEX. TAX

CODE § 11.31(k). Absent such action, TCEQ is without power to revise the list and the Executive Director's attempt to do so on a wholesale basis with respect to HRSGs is improper and without any support. As a result, the matter must be remanded back to the Executive Director.

2. TCEQ Has Determined that a HRSG is a Pollution Control Device

TCEQ promulgated rules to implement the Legislature's directives with respect to pollution control equipment. In 2008, TCEQ adopted an Expedited Review List as a "nonexclusive list of facilities, devices, or methods for the control of air, water and/or land pollution." *See* 30 TEX. ADMIN. CODE § 17.17(b). Among the pollution control devices included on this list are Heat Recovery Steam Generators. *See id.* Through its adoption of this list, and its inclusion of HRSGs on the list, TCEQ has determined that HRSGs constitute pollution control equipment. Absent further rulemaking, the Executive Director and the Commission are without power to decide otherwise, particularly in the face of the Legislature's requirement that the removal of a device from the list requires "compelling evidence to support the conclusion that the item does not provide pollution control benefits." TEX. TAX CODE § 11.31(l).

Even if the deletion of HRSGs from the list could be accomplished via a negative use determination, the Executive Director's negative use determination was based solely on a conclusory statement that HRSGs are production equipment and are therefore ineligible for a positive use determination. In fact, the conclusory statement was not supported by any evidence, much less substantial evidence or, as required by TEX. TAX CODE § 11.31(l), compelling evidence.

An agency's conclusion of fact must be supported by such relevant evidence as a reasonable mind might accept as adequate. *See City of El Paso v. Public Util. Comm'n of Texas*,

344 S.W.3d 609, 618 (Tex. App. – Austin 2011). A reviewing court will also consider whether the agency decision violated a constitutional or statutory provision, whether the agency acted outside its authority in issuing the decision, and whether the agency violated procedural requirements in issuing the decision. TEX. GOV'T CODE § 2001.174. The Executive Director's evidence is insufficient to support an affirmance of the negative use determination.

The Executive Director's Response Brief does not include a technical analysis of the function and performance of a HRSG, and does not include any other competent evidence, much less compelling evidence, in support of additional conclusory statements that HRSGs are not pollution control devices. These statements do not meet the standard necessary to support a negative use determination in this matter.

Further, an agency's interpretation of its rules is not entitled to deference when the interpretation is plainly erroneous or inconsistent with the language of the statute, regulation, or rule. *See TGS-NOPEC Geophysical Co. v. Combs*, 340 S.W.3d 432, 438 (Tex. 2011); *Public Util. Comm'n of Texas v. Gulf States Utils. Co.*, 809 S.W.2d 201, 207 (Tex. 1991); *Stanford v. Butler*, 142 Tex. 692, 181 S.W.2d 269, 273 (1944). Courts defer only to the extent that the agency's interpretation is reasonable, and no deference is due where an agency's interpretation fails to follow the clear, unambiguous language of its own regulations. *TGS-NOPEC Geophysical Co.*, 340 S.W.3d at 438; *see also Public Util. Comm'n of Texas*, 809 S.W.2d at 207.

The Executive Director's decision in this matter is not supported by the evidence and cannot stand. The decision is also contrary to TEX. TAX CODE § 11.31(k), (m), and 30 TEX. ADMIN. CODE § 17.17(b). As a result, the matter must be remanded back to the Executive Director.

3. HRSGs Perform an Air Pollution Control Function

The Legislature defined a "facility, device, or method for the control of air … pollution" as "… any equipment, or device … that is used, constructed, acquired, or installed wholly or partly to meet or exceed rules or regulations of any environmental protection agency of the United States … for the prevention, monitoring, control, or reduction of air … pollution." Tex. Tax Code § 11.31(b). An "air pollution control device," therefore, can be one that prevents, monitors, controls, or reduces air pollution, in compliance with an EPA regulation, for example.

A HRSG prevents and reduces air pollution. As noted in BEPC's application and as verified by Clifton Karnei, BEPC's Executive Vice President and General Manager, BEPC's Plant consists of a combined-cycle gas turbine power plant with (1) gas combustion turbine ("CT") equipped with a HRSG and dedicated ancillary systems necessary to capture heat from the CTs exhaust and convert it into electrical power. Karnei Affidavit, attached hereto as Attachment G, para. 6. Gas turbines drive large electric generators. Their exhaust may contain substantial amounts of residual heat which used to be lost to the atmosphere. HRSGs are used to effectively extract every BTU of heat from this residual heat. *Id.*

The combined-cycle system combines two simple-cycle systems into one generation unit, and does so to maximize energy efficiency. *Id.* at para. 7. Energy is produced in the first cycle using a gas turbine. *Id.* The heat that remains is used to create steam, which is run through a steam turbine. *Id.* Thus, two single units – one gas unit and one steam unit, are combined to minimize lost potential energy, maximize energy efficiency, and reduce air pollution. *Id.*

The HRSG is a fabricated, metal piece of equipment that connects to the CT exhaust and directs the hot exhaust gas through a series of metal tubes to the exhaust stack. *Id.* at para. 8. The HRSG is installed at the exit of the CT to capture and utilize the waste heat of combustion

from the CTs exhaust gas and utilizes this waste heat to produce steam, which in turn powers a steam turbine-generator set to produce electrical power at the Plant in addition to the electrical power generated by the CT alone. *Id.* This process is depicted in a process flow diagram that was attached as Attachment 2 to BEPC's Application No. 16413. *See* Attachment A.

The Plant gains both production and pollution control benefits from the HRSG and its dedicated ancillary equipment (the "PC Property"). Karnei Affidavit, attached hereto as Attachment G, para. 9. First, the use of this waste heat of combustion by the HRSG creates a thermal efficiency benefit for the Plant. *Id.* Specifically, the use of waste heat from the CT exhaust gas results in the conversion of some of 50-55% of the chemical energy of the natural gas utilized at the Plant into electricity (HHV basis), a gain over the approximately 36% efficiency of the CTs alone use of the fuel in a simple cycle gas turbine (Brayton Cycle). *Id.* Second, due to this efficiency gain, the Plant is able to generate fewer emissions (particularly NOx emissions) than a traditional power generation facility utilizing a single thermodynamic cycle; thereby allowing the subject PC Property to appear on the Expedited Review List. *See id.*; *see also* TEX. TAX CODE § 11.31(k); 30 TEX. ADMIN. CODE 17.17(b). The HRSG allows the Plant to produce the necessary amount of electricity while using less energy and emitting less pollutants, principally NOx, than would be result from the use of a simple-cycle gas turbine power plant. Karnei Affidavit, Attachment G, para. 9.

Through the use of combined-cycle technology, emissions are prevented/reduced from those that would be generated from a simple-cycle gas turbine power plant, of equal power-generating capacity. *Id.* at para. 10. The HRSG is the device that allows BEPC's Plant to function as a combined-cycle gas turbine power plant, and to obtain the air pollution

prevention/reduction. *Id.* A HRSG, therefore, is an air pollution control device, as pre-approved in both the statute and in TCEQ's rules.

4. EPA Considers Combined-Cycle Technology to be BACT and Recognizes Environmental Benefits

The status of a HRSG as a pollution control device has also been confirmed by EPA, as recently as this past March and August. In a permitting matter with the Wisconsin Department of Natural Resources ("WDNR"), EPA questioned why WDNR's Best Available Control Technology ("BACT") analysis only considered simple cycle turbines and did not consider combined cycle turbines. EPA noted that increasing the efficiency of fuel burning equipment is a way to decrease emissions of regulated pollutants, in that case greenhouse gases ("GHGs"). EPA further noted that combined cycle turbines are generally more energy efficient than simple cycle turbines. *See* EPA Correspondence with Andrew Stewart, Chief, Permits and Stationary Source Modeling Section, Bureau of Air Management, WDNR, Mar. 15, 2012, attached hereto as Attachment H. *See also*, EPA Correspondence with Charles King, Air Compliance Manager, Virginia Department of Environmental Quality, Aug. 7, 2012 (BACT analysis should consider combined-cycle combustion turbines with higher thermal efficiency than the type of combined-cycle combustion turbines proposed by the applicant), attached hereto as Attachment I.

In Texas, EPA recently issued a Statement of Basis for the GHG Prevention of Significant Deterioration ("PSD") preconstruction permit for LCRA's Thomas C. Ferguson Plant, Permit No. PSD-TX-1244-GHG. *See* Attachment J. EPA noted that the existing steam electric generating unit was proposed to be replaced with a new combined-cycle power plant that "would be more efficient, more reliable and have improved environmental controls." *Id.*, at 4. EPA determined that the most efficient method to generate electricity from a natural gas fuel source is the use of a combined-cycle design, the major components of which are the combustion

turbine, a HRSG, and a steam turbine. *Id.*, at 7. EPA noted, "Specific energy efficiency processes, practices and designs are included in the permit application for each component of the combined cycle unit." *Id.*

EPA's recognition of the environmental benefits of combined-cycle units pre-dates its most recent consideration of the technology for purposes of reducing GHGs. In 2004, and again in 2006, EPA developed an economic impact analysis with respect to regulations it was developing under Section 111 of the Clean Air Act for new stationary combustion turbines. The proposed, and ultimately adopted, regulations were designed to reduce emissions of NOx and sulfur dioxide generated by the combustion of fossil fuels in new combustion turbines. *See* 40 C.F.R. Part 60, Subpart KKKK; 71 Fed. Reg. 38482 (Jul. 6, 2006).

In support of its rulemaking, EPA cited the environmental efficiency gains achieved from combined-cycle combustion turbines. According to EPA, the use of such a turbine system "decreases NOx emissions by 14 percent over simple-cycle combustion turbines and 89 percent over existing coal electricity generation plants. In addition, CO2 emissions will be 5 percent lower than emissions from SCCTs and 64 percent lower than existing coal plants." EPA, Economic Impact Analysis of the Stationary Combustion Turbines NSPS: Final Report, Feb. 2006, at 2-3, 2-4, a copy of which is attached as Exhibit 6 to the Karnei Affidavit, attached hereto as Attachment G. Applying EPA's data to BEPC's operation of the Plant in 2010, BEPC's use of the combined-cycle turbine system resulted in 34,153 lbs fewer NOx emissions than would have occurred utilizing a simple-cycle turbine system to generate the same amount of electricity. Karnei Affidavit, Attachment G, para. 11.

As noted above, the HRSG is the mechanism or device that allows BEPC's Plant to operate as a combine-cycle combustion turbine system. Without the HRSG, BEPC's Plant

would be a single-cycle combustion turbine system; more energy would be needed to produce the same amount of electricity; and, as EPA has noted, more emissions would result. The HRSG is, therefore, the device to which the air emission reductions are attributed.

5. Conclusion

The Legislature has designated a HRSG as a pollution control device through its inclusion of the HRSG on the mandated nonexclusive list of facilities, devices or methods for the control of pollution. Through its rulemaking, TCEQ has included the HRSG on its nonexclusive list of facilities, devices or methods for the control of air pollution adopted. The Legislature provided TCEQ with a mechanism by which TCEQ could remove a facility, device or method from the nonexclusive list, provided that TCEQ reaches this decision through a rulemaking process, and the decision is supported with compelling evidence. *See* TEX. TAX CODE § 11.31(l). TCEQ has neither proposed nor adopted rulemaking to remove the HRSG from the nonexclusive list of facilities, devices or methods for the control of air pollution. TCEQ is not empowered to make this change through a use determination. As such, the Executive Director's decision in this matter is not supported by the law or any evidence and cannot stand, and the matter must be remanded back to the Executive Director.

In further support of BEPC's position that the HRSG is both legally and technically, air pollution control equipment, as defined by TEX. TAX CODE § 11.31(b), BEPC has provided TCEQ with competent evidence related to the design and operation of its HRSG, as part of the combined-cycle combustion turbine system. EPA has confirmed combined-cycle combustion turbines as BACT, and has promulgated air pollution control requirements premised on the environmental benefits obtained from the use of this technology. As noted above, the HRSG is the mechanism or device that allows BEPC's Plant to operate as a combine-cycle combustion

turbine system. Without the HRSG, BEPC's Plant would be a single-cycle combustion turbine system; more energy would be needed to produce the same amount of electricity; and, more emissions would result. The HRSG is, therefore, the device to which the air emission reductions are attributed, and is, therefore, a device which is installed and used to prevent and reduce air pollution.

In conclusion, HRSGs are included in the statute's and the TCEQ's list of air pollution control equipment for which a positive use determination may be obtained. Given that: (1) the Executive Director's decision conflicts with the Legislature's designation of a HRSG as pollution control equipment; (2) TCEQ has designated a HRSG as air pollution control equipment; and (3) TCEQ has taken no steps to propose or adopt the rulemaking required by the Legislature to remove a HRSG from the pre-approved list of air control equipment, nor could it at this juncture, this matter should be remanded back to the Executive Director.

Further, the Executive Director's sole basis for the negative use determination was his contention that the HRSG was used solely for production and was not "pollution control equipment," and therefore was not eligible for a positive use determination. Because the Executive Director's justification for the negative use determination was limited to this single issue, the Commission should decline any issues raised by the Executive Director for the first time in his Response to BEPC's appeal. Without further consideration of these additional issues, the Commission should remand this matter to the Executive Director.

B. BEPC's HRSG was Reconstructed after January 1, 1994

The Legislature limited the tax exemption to land or other property acquired, constructed, reconstructed, replaced, improved or installed after January 1, 1994. TEX. TAX CODE § 11.31(a). BEPC constructed its HRSG as part of the total Plant construction from 2008 to 2011. Karnei

Affidavit, Attachment G, para. 3. The necessary equipment to perform the construction was purchased from 2008-2011. *Id.* The construction of the HRSG was completed on August 3, 2011. *Id.* The Executive Director declared BEPC's Application No. 16413 administratively complete on April 19, 2012. *See* Attachment B.

At no time during the processing of Application No. 16413 has the Executive Director raised an issue with respect to BEPC's compliance with this element of the use determination eligibility requirements. The Executive Director has not raised this issue in his Response. As a result, it is BEPC's understanding that the Executive Director has determined that BEPC has complied with this element of the use determination eligibility requirements and, with respect to this element, is eligible for a positive use determination.

C. BEPC's HRSG was Reconstructed and is Used To Meet or Exceed EPA Regulations

Before addressing this issue, it should be noted that the Executive Director did not include, as a basis of his negative use determination, any allegation that BEPC had failed to cite an applicable environmental regulation in Application No. 16413. BEPC objects to the inclusion of this issue in the Executive Director's Response, and requests that the Commission decline to consider this portion of the Executive Director's Response in this appeal. Subject to, and without waiving this objection, BEPC demonstrates herein that it complied with this element of the use determination eligibility requirements.

To be eligible for a positive use determination, the property for which an exemption is sought must have been "used, constructed, acquired, or installed wholly or partly to meet or exceed rules or regulations adopted by any environmental protection agency of the United States ...." BEPC's Application No. 16413 met this requirement. In its application, BEPC stated:

> The Pollution Control Property (PC) (i.e., the HRSG and the dedicated ancillary systems) was installed to meet the requirements of 40 CFR Part

> 60.44da(a) (sic) "Standards for nitrogen oxides (NOX) for Electric Utility Steam Generating Units for new source performance standards (NSPS).
>
> As well, the PC Property allows emissions to meet or exceed best available control technology (BACT) emission limitations established in federal operating permit # O-2169. Per 30 Texas Administration Code (TAC) §122.143(4), the permit holder must comply with all terms and conditions codified in the permit and any provisional terms and conditions required to be included with the permit.

EPA's regulations, set forth in 40 C.F.R. § 60.44Da(a), establish NOx emission limits and reduction requirements. BEPC meets these limits and reduction requirements through its use of a combined-cycle combustion turbine system. The HRSG is the mechanism or device that allows BEPC's Plant to operate as a combine-cycle combustion turbine system. Without the HRSG, BEPC's Plant would be a single-cycle combustion turbine system; more energy would be needed to produce the same amount of electricity; more emissions would result. Karnei Affidavit, Attachment G, para. 9-10. The HRSG, therefore, is a device used by BEPC to meet an EPA regulation, namely 40 C.F.R. § 60.44Da(a).

The Executive Director contends, for the first time, that for the cited regulation to meet the requirement of this element of eligibility for a positive use determination, there must be a "sufficient nexus" between the property and an environmental rule. The Executive Director stated, "A sufficient nexus must exist between the equipment and the environmental rule. Simply because an environmental rule applies to a piece of equipment, does not mean for the purposes of a use determination that this criteria is satisfied, nor does it mean the applicant qualifies for a property tax exemption." Response, at 11. The Executive Director continued, "No Applicant has cited to a rule that requires the installation of the HRSG. There is no rule that explicitly requires the installation of a HRSG nor is there a generally applicable efficiency standard that could only be met by installation of a HRSG." *Id.*

As noted above, the Legislature specified HRSGs as a type of equipment that could qualify for a positive use determination. The Executive Director's new interpretation of this element of eligibility for a positive use determination is inconsistent with the Legislature's action in this regard. Neither the statute nor TCEQ's rules reference a "nexus" requirement, or require the applicant to provide any information regarding the connection, link, tie, relationship, or interconnection between the property for which the positive use determination is sought, and the environmental rule that is met by its use, construction, acquisition, or installation. The Executive Director has not identified any source for this purported requirement nor has he defined or otherwise specified what relationship would meet his requirement for a "sufficient nexus."

The Executive Director's determination in this regard violates BEPC's due process rights. *See, e.g., Langford v. Employees Ret. Sys.*, 73 S.W.3d 560, 565-66 (Tex. App.-Austin 2002, pet. denied) (due process concerns arose when agency failed to give applicant grounds on which it would rely for its decision and when agency denied application without deliberation). BEPC was never given notice of this "nexus" requirement or the necessity of having to address it in its Application or otherwise. Karnei Affidavit, Attachment G, para. 13. Also, if the Executive Director determined that BEPC's Application was deficient in its failure to properly cite an applicable environmental regulation, BEPC was entitled to a Notice of Deficiency and an opportunity to cure its allegedly incomplete Application. *See* 30 TEX. ADMIN. CODE § 17.12(2)(A).

Second, the Executive Director's wholesale rejection of the regulations cited by BEPC and the other similarly situated applicants as "applicable environmental regulations" runs afoul of equal protection principles and the requirements of uniformity, equality and fairness in approach. *See* TEX. TAX CODE § 11.31(g)(2); TEX. CONST. art. VIII, § 1(a); *BMW of North*

America, LLC, v. Motor Vehicle Board, et al., 115 S.W.3d 722, 726 (Tex. App. – Austin 2003); *Reynolds v. Sims*, 377 U.S. 533, 565 (1964). The Executive Director has previously granted multiple positive use determinations based on regulations cited by BEPC and the other applicants subject to the Executive Director's recent negative use determinations. Imposition of any new "nexus" requirement against these applicants is intrinsically discriminatory.

The novelty of this interpretation is evident from the Executive Director's prior technical reviews conducted on applications for positive use determinations related to HRSGs. The Executive Director has uniformly approved HRSG applications citing 40 C.F.R. § 60.44Da(a) as the rule that is met or exceeded by the installation and use of the HRSG. *See e.g.*, Attachment K (copies of six use determinations approved based on a technical review determination that a HRSG was used to meet 40 C.F.R. § 60.44Da).

And rightfully so. This EPA rule establishes standards for NOx emissions and states:

> On and after the date on which the initial performance test is completed or required to be completed under §60.8, whichever date comes first, no owner or operator subject to the provisions of this subpart shall cause to be discharged into the atmosphere from any affected facility, except as provided under paragraphs (b), (d), (e), and (f) of this section, any gases that contain NOx (expressed as NO2) in excess of the following emission limits, based on a 30-day rolling average basis, except as provided under §60.48Da(j)(1):
>
> (1) NOX emission limits:
>
> Gaseous fuels:
> Coal-derived fuels ..... 210 ng/J, 0.50lb/MMBtu
> All other fuels ..... 86 ng/J, 0.20 lb/MMBtu
> ...
>
> (2) NOx reduction requirement (Percent reduction of potential combustion concentration):
>
> Gaseous fuels 25
> Liquid fuels 30

Solid fuels 65

40 C.F.R. § 60.44Da(a).

While HRSGs are not specifically mentioned in this section, HRSGs are subject to this regulation. EPA notes, within the applicability section of 40 C.F.R. Part 60, Subpart Da, that HRSGs are subject to this regulation:

> This subpart will continue to apply to all other electric utility combined cycle gas turbines that are capable of combusting more than 73 MW (250 MMBtu/hr) heat input of fossil fuel in the *heat recovery steam generator*. If the *heat recovery steam generator is subject to this subpart* and the stationary combustion turbine is subject to either subpart GG or KKKK of this part, only emissions resulting from combustion of fuels in the steam-generating unit are subject to this subpart. (The stationary combustion turbine emissions are subject to subpart GG or KKKK, as applicable, of this part).

40 C.F.R. § 60.40Da(a)(4) (emphases added).

The Executive Director correctly noted that other portions of EPA's regulations also subject HRSGs to particular requirements. *See* Executive Director's Response, note 42 (referring to the applicability of 40 C.F.R. Part 60, Subparts Da, Db and KKKK). As the Executive Director noted, these subparts are mutually exclusive, i.e., if a HRSG is subject to one of these subparts, it is not subject to the others. *See* 40 C.F.R. §§ 60.40b(i), 60.4305(b); *see also* 40 C.F.R. § 60.40c(e). Contrary to the Executive Director's assertion, a HRSG is subject to any one of four separate EPA regulations, including 40 C.F.R. § 60.44Da(a). BEPC's citation of 40 C.F.R. § 60.44Da(a) complies with the requirement to identify an applicable EPA regulation that is met or exceeded through the use and installation of the HRSG, even under the Executive Director's newly asserted "nexus" requirement.

The Executive Director asserted that 40 C.F.R. Part 60, Subpart Da regulates only a portion of the plant and that applicants contend HRSGs increase the efficiency of the whole

plant. Based on this assertion, the Executive Director concluded, "Because what is regulated by NSPS Da and Db is not the same as what Applicants state the control provided by HRSGs, there is not a sufficient nexus." Executive Director's Response, at 11. The "affected facility" to which 40 C.F.R. Part 60, Subpart Da is:

> ... each electric utility steam generating unit:
> (1) That is capable of combusting more than 73 megawatts (MW) (250 million British thermal units per hour (MMBtu/hr)) heat input of fossil fuel (either alone or in combination with any other fuel); and
> (2) For which construction, modification, or reconstruction is commenced after September 18, 1978.

40 C.F.R. § 60.40Da(a). "Electric utility steam generating unit" is defined as:

> ... any steam electric generating unit that is constructed for the purpose of supplying more than one-third of its potential electric output capacity and more than 25 MW net-electrical output to any utility power distribution system for sale.

40 C.F.R. § 60.41Da. Respectfully, the Executive Director's assertion is in error.

Subpart Da regulates each electric utility steam generating unit. *See* 40 C.F.R. § 60.40Da(a). An electric utility combined cycle gas turbine is part of such a unit. *See* 40 C.F.R. § 60.41Da. A HRSG is part of the combined cycle gas turbine system. *See* 40 C.F.R. § 60.40Da(a)(4). As noted above, the HRSG is the device that makes the turbine system a combined-cycle gas turbine system. Karnei Affidavit, Attachment G, at para. 10. Again, BEPC's citation of 40 C.F.R. § 60.44Da(a) complies with the requirement to identify an applicable EPA regulation that is met or exceeded through the use and installation of the HRSG.

The Executive Director's assertion that an applicant must refer to a rule that specifically requires the installation of a HRSG, or that includes a "generally applicable efficiency standard that could only be met by installation of a HRSG" is contrary to the statute and TCEQ's rule, and is inconsistent with the Executive Director's prior reviews of HRSG positive use determination

applications. Under the Executive Director's interpretation, it is unclear that any of the equipment identified by the Legislature as "pollution control equipment" would be eligible for a positive use determination. Neither the statute, nor TCEQ's rules, require that an applicant may only claim a positive use determination on equipment that constitutes the sole method of compliance with an environmental regulation.

The Executive Director's position is unsupported by the law and cannot stand. For this reason, this matter should be remanded back to the Executive Director.

D. BEPC's HRSG Produces Anticipated Environmental Benefits

As with the issue above, before addressing this issue, it should be noted that the Executive Director did not include, as a basis of his negative use determination, any allegation that BEPC did not identify the anticipated environmental benefits of its HRSG in Application No. 16413. BEPC objects to the inclusion of this issue in the Executive Director's Response, and requests that the Commission decline to consider this portion of the Executive Director's Response in this appeal. Subject to, and without waiving this objection, BEPC demonstrates herein that it complied with this element of the use determination eligibility requirements.

To be eligible for a positive use determination, the property for which an exemption is sought must present, in its application, "the anticipated environmental benefits from the installation of the facility, device, or method for the control of air, water, or land pollution." TEX. TAX. CODE § 11.31(c)(1); *see also* 30 TEX. ADMIN. CODE § 17.10(d)(1). As the Executive Director noted in his Response, "Generally, a piece of equipment provides an environmental benefit if it is used to prevent, monitor, control, or reduce air, water, or land pollution." Executive Director's Response, at 10, citing TEX. TAX CODE § 11.31(b).

In its application, BEPC stated:

> The PC Property reduces the formation of and/or controls the emission of NOx and other air emissions associated with the combustion of natural gas used in combined cycle power generation at the Facility. Since less fuel is required per kilowatt of power produced, less exhaust gas emissions (NOx, CO, CO2) are emitted. Therefore, the HRSG's primary purpose of capturing and converting waste heat from the combustion turbine results in meaningful environmental benefits.

See Attachment B, at Attachment 1, Section 9.13.

In his Application Review Summary, in reviewing the environmental benefit of BEPC's HRSG, the Executive Director noted, "Use of the HRSG will improve the thermal efficiency of the plant." Attachment C. The Executive Director, in this review, did not contest the environmental benefit of the HRSG. Nor did the Executive Director contest its environmental benefit in his negative use determination. *Id.* This element of the use determination eligibility requirements was not a basis upon which the Executive Director issued his negative use determination. As such, it cannot serve as a basis of a denial of BEPC's appeal and an affirmance of the Executive Director's use determination.

Further, the Executive Director's newly asserted position that HRSGs do not provide an environmental benefit is in error. As noted above, the Legislature, the TCEQ and EPA have confirmed the environmental benefits of HRSGs. The Legislature's recognition of this fact served as the basis for the inclusion of HRSGs on the mandated nonexclusive list of facilities, devices or methods for the control of pollution. TCEQ confirmed that recognition and has not taken action to reverse this recognition. Further, EPA has recognized the environmental benefits of HRSGs in recent BACT reviews as well as in its rulemaking addressing stationary combustion turbines. To avoid repetition, BEPC respectfully directs the Commission to Section II(A) of this Reply, which is incorporated herein for all purposes.

Based on the foregoing, a HRSG is both legally and technically, air pollution control equipment that prevents/reduces air pollution. Using EPA-cited data, BEPC's use of the combined-cycle turbine system resulted in 34,153 lbs fewer NOx emissions than would have occurred utilizing a simple-cycle turbine system to generate the same amount of electricity. Karnei Affidavit, Attachment G, at para. 11.

BEPC has, therefore, established that it has complied with this element of the use determination eligibility requirements. The Executive Director's position is unsupported by the law and the evidence and cannot stand. For this reason, this matter should be remanded back to the Executive Director.

E. BEPC Has Provided the Estimated Cost of the HRSG

The Legislature required that an applicant include, in its application for a use determination, the estimated cost of the pollution control facility, device or method. TEX. TAX CODE § 11.31(c)(2); *see also* 30 TEX. ADMIN. CODE § 17.10(d)(2). BEPC provided this cost estimate for the HRSG in Application No. 16413. *See* Attachment A, at Attachment 4. For purposes of this Response, BEPC has attached a list of its expenditures related to the HRSG. *See* Attachment G, Exhibit 2. The Executive Director has not contested this issue and has not raised this issue in his Response. As a result, it is BEPC's understanding that the Executive Director has determined that BEPC has complied with this element of the use determination eligibility requirements and, with respect to this element, is eligible for a positive use determination.

F. BEPC Provided the Proportion of the HRSG that is Pollution Control Property

As with the issues discussed above in Section II(C), and (D), before addressing this issue, it should be noted that the Executive Director did not include, as a basis of his negative use determination, any allegation that BEPC did not appropriately calculate the proportion of the cost

of the HRSG that is pollution control property in Application No. 16413. BEPC objects to the inclusion of this issue in the Executive Director's Response, and requests that the Commission decline to consider this portion of the Executive Director's Response in this appeal. Subject to, and without waiving this objection, BEPC will demonstrate that it complied with this element of the use determination eligibility requirements.

To be eligible for a positive use determination, if the installation includes property that is not used wholly for the control of air pollution, the person seeking the exemption shall present data, as required by TCEQ rules for the determination of the proportion of the installation that is pollution control property. TEX. TAX CODE § 11.31(c); *see also* 30 TEX. ADMIN. CODE § 17.10(d)(3). In its application, BEPC provided a calculation of the proportion of the cost of the HRSG that should be attributed to the pollution control aspect of the equipment. *See* Attachment A, Attachment 4. BEPC utilized the formula developed by the TCEQ, set forth in 30 TEX. ADMIN. CODE § 17.17(c)(1). Karnei Affidavit, Attachment G, at para. 14. The Karnei Affidavit includes a summary of the CAP calculations, with supporting documents and information, which is incorporated herein. *Id.*

The Executive Director did not contest BEPC's calculation in his Application Review Summary, and did not address BEPC's calculation in the negative use determination or in his Response. The Executive Director does contend that HRSGs are not eligible to receive a 100% positive use determination. BEPC does not seek to comment on this issue beyond noting that it is not seeking a 100% positive use determination in this matter. As noted above, through its application, BEPC sought a partial positive use determination in the amount of 74.66%. BEPC has complied with this element of the use determination eligibility requirements and, with respect to this element, is eligible for a positive use determination.

G. Additional Issues Raised by the Executive Director

In his Response, the Executive Director raised issues beyond those set forth in the negative use determination issued to BEPC with respect to Application No. 16413. To the extent that these issues are relevant to BEPC's application and have not been addressed above, they are addressed below.

1. Equipment Listed in § 11.31(k) is not Automatically Entitled to a Positive Use Determination

The Executive Director asserts that the presence of the HRSG on the list set forth in TEX. TAX CODE § 11.31(k) does not automatically entitle an applicant to a positive use determination. This assertion misses the intent of the Texas Legislature in inserting HRSGs in the list in TEX. TAX CODE § 11.31(k), which was to establish that the HRSG is pollution control equipment that is eligible for a positive use determination, provided that the other eligibility requirements are met. For example, the applicant must also submit a complete application demonstrating its eligibility for the positive use determination. As demonstrated above, such is the case with BEPC's application. BEPC's application addressed each of the elements necessary to establish its eligibility for a positive use determination.

The Executive Director also referred to TCEQ's preamble to the 2010 rule, which stated, "... inclusion of a piece of equipment on the Tier I Table or on the table in § 17.17(b) or the assertion that a piece of equipment falls under a category set forth on either list does not mean that the equipment would receive a positive use determination in all circumstances." Response, at 7, citing 35 Tex. Reg. 10964. The Executive Director stretches the import of this language too far. Simply because a HRSG might not receive a positive use determination in all circumstances, for example, where the applicant failed to submit a complete application, does not support the

Executive Director's determination, in this and the other pending HRSG matters, that a HRSG will never receive a positive use determination under any circumstances.

TCEQ's rules reflect the possibility that a Tier III applicant's calculation under TCEQ's cost analysis procedure, set forth in 30 TEX. ADMIN. CODE § 17.17(c)(1), could result in a negative number or a zero. TCEQ's rules note that, in such circumstances, the property would not be eligible for a positive use determination. *See* 30 TEX. ADMIN. CODE § 17.17(d). Such is not the case with BEPC's application. The CAP calculation demonstrated that BEPC was eligible for a 74.66% positive use determination. *See* Attachment A, Attachment 4.

The Executive Director, however, extrapolates from his "not always eligible" argument to support his "never eligible" determination. He states, "To obtain a positive use determination the equipment listed in § 11.31(k) must meet the same statutory and regulatory eligibility criteria as any other piece of equipment (i.e., provide an environmental benefit, meet or exceed an environmental rule, be partially or wholly used as pollution control property, etc.). Response, at 6 (emphasis added). He continues, "The Executive Director must determine the appropriate use determination percentage, which includes 0% if none of the equipment is used for pollution control." *Id.* (emphasis added).

It is through this analysis that it appears the Executive Director attempts to obtain authority to re-evaluate the status of a HRSG as "pollution control equipment," a status previously granted by the Legislature and by the TCEQ. This is contrary to the statute and the rules. The Legislature has determined that it is pollution control equipment. TCEQ's rules require that, with respect to equipment included on TCEQ's Expedited Review List, set forth in 30 TEX. ADMIN. CODE § 17.17(b), the CAP calculation be used to determine the creditable partial percentage for the equipment. *See* 30 TEX. ADMIN. CODE § 17.17(c). The Executive Director is

not authorized to determine that a HRSG is not pollution control equipment. His authority is limited to determining whether the HRSG is wholly or partially used as pollution control equipment, and for Tier III applicants, this determination is based on the CAP calculation.

The Executive Director failed to conduct this step of calculating the appropriate creditable partial percentage for BEPC's HRSG. The Executive Director's conclusion that HRSGs are not pollution control equipment is contrary to and unsupported by the law, TCEQ's rules, and the evidence presented in this matter. This matter must therefore be remanded back to the Executive Director so that he may conduct this required step and appropriately determine the creditable partial percentage for BEPC's HRSG.

The Executive Director also relies on the doctrine of legislative acceptance. *See* Response, at 7. This reliance is misplaced with respect to Application No. 16413, given that the Executive Director has never previously taken the position that under no circumstances will a HRSG be eligible for a positive use determination. In fact, every previous recommendation by the Executive Director has taken a contrary position and affirmed the conclusion that HRSGs are pollution control equipment and are eligible for a positive use determination. Most recently, in December 2008, the Executive Director recommended to the Commission that it adopt a positive use determination in the amount of 61% for all HRSGs. *See* Attachment L.[3] To the extent that the doctrine of legislative acceptance applies, it applies in favor of considering HRSGs air pollution control equipment that is eligible for a positive use determination.

[3] In relevant part, the Executive Director's recommendation to the Commission stated, "The thermal efficiency increase or production gain derived from the installation of a HRSG is approximately 39%. Since this percentage represents the additional amount of electrical energy produced for a given heat input, it therefore represents the production value of the equipment. Based on this production value, the pollution control percentage of a HRSG installed at a combined-cycle facility is 61%. Staff is therefore recommending the positive use determination of 61% for the installation of a HRSG in a combined-cycle facility." Attachment L at 11.

2. Rulemaking was Not Necessary for the Executive Director to Issue Negative Use Determinations

In his Response, the Executive Director asserts:

> The negative use determinations issued to each of the Applicants was the result of a case-by-case review of each application. The Executive Director followed his standard process for each application. A technical review was generated for each application. In deciding that HRSGs were production equipment, the Executive Director interpreted existing provisions and applied them on a case-by-case basis to the applications.
>
> This change is not a rule of general applicability. Rather if (sic) affects a limited number of Applicants for a use determination. Therefore, no rulemaking is necessary.

Response, at 17. To the extent that any case-by-case review was conducted by the Executive Director, it was limited to whether the applicant was seeking a use determination on a HRSG. If the property was a HRSG, a negative use determination was issued, in each and every case pending before the agency. The technical review, which was only provided to BEPC as an attachment to the Response, was cursory in nature, limited to a critique of the applicant's citation of environmental rules that were met or exceeded through the use of the HRSG, and a final determination that HRSGs are used solely for production and are therefore not eligible for a positive use determination. No CAP calculations were reviewed or conducted, at least as reflected in the Executive Director's Application Review Summary. *See* Attachment C. Nor does the Application Review Summary include any indication of, or background information supporting, the Executive Director's interpretation of existing provisions and his application of this interpretation, on a case-by-case basis, to the application. *Id.* The Technical Review Checklist, which is included with TCEQ's records related to Application No. 16413, is equally devoid of any analysis supporting the Executive Director's decision. *See* Attachment F. These facts reflect that the Executive Director determined that HRSGs would no longer receive a

positive use determination, no matter the particular circumstances of an individual applicant. This decision constitutes a rule of general applicability, which must proceed through formal rulemaking.

Under the Texas Administrative Procedures Act (the "Texas APA"), a "rule" is any "state agency statement of general applicability that ... implements, interprets, or prescribes law or policy," including "the amendment or repeal of a prior rule." TEX. GOV'T CODE § 2001.003(6). A state agency can only promulgate new rules through formal rulemaking procedures, including prior notice of a proposed new rule and an opportunity for public comment, legislative review, and a formal order adopting it. *Id.* at §§ 2001.23; 2001.029; 2001.032-.033. The Texas APA also requires the advance notice to contain enough information to allow interested persons to determine if they need to participate to protect their own rights. *Tex. Workers' Comp. Comm 'n v. Patient Advocates*, 136 S.W.3d 643, 650 (Tex. 2004).

Chapter 17 of the Texas Administrative Code was created to establish how any owner of pollution control property could get a use determination. 30 TEX. ADMIN. CODE § 17.1. Through rulemaking, TCEQ confirmed the legislatively-established status of a HRSG as pollution control equipment eligible for a positive use determination. *See* 30 TEX. ADMIN. CODE § 17.17(b); TEX. TAX CODE § 11.31(k).

The Executive Director has now chosen to apply a different uniform standard with respect to its consideration of use determinations related to HRSGs, i.e., "Heat recovery steam generators are used solely for production; therefore (sic) not eligible for positive use determination." The Executive Director's determination in this regard, applied as it is across the board to all pending HRSG-related use determination applications, reads HRSGs right out of TCEQ's rules and TEX. TAX CODE § 11.31(k) and (m). The Executive Director's determination,

therefore, impermissibly implements a new, universal rule applicable to all HRSGs, without the required rulemaking under the Texas APA. Because the Executive Director's effective removal of HRSGs from eligibility for positive use determinations was not undertaken in the form of a properly promulgated rule under the Texas APA, the Commission must remand this matter to the Executive Director.

This conclusion is further mandated by the fact that the Legislature established, through TEX. TAX CODE § 11.31(l), a specific process that it required TCEQ to follow, if it chose to remove one of the items included within TEX. TAX CODE § 11.31(k) items from the list of pollution control equipment. As stated therein, "An item may be removed from the list if the commission finds compelling evidence to support the conclusion that the item does not provide pollution control benefits." TEX. TAX CODE § 11.31(l). This provision also specifies that TCEQ's updates to the list shall be done by rule. *Id.* The Executive Director has not proposed such rulemaking. As others have noted, this process is not an academic exercise, but one that involves fundamental concepts of fairness, due process, and notice. Such concepts are not to be lightly trod upon, for they constitute the basic elements of our participatory democracy and are essential to the State's efforts to ensure an open and transparent government of, by, and for the people. *See, e.g.*, TEX. CONST. Art. I, §§ 2, 29; TEX. GOV'T CODE §§ 551.001 et seq., 552.001, et seq., 2001.001 et seq. Such a process ensures that the government's actions are reasoned, conducted in public, and subject to public notice and comment.

In short, the Legislature created a high hurdle for removing the "pollution control equipment" status that the Legislature had granted to certain pieces of equipment. TCEQ may take such action only based on compelling evidence, and may do so only by taking such action through a formal rulemaking process. The Executive Director has no authority to utilize the use

determination process to eliminate the HRSG from the Legislature's list of "pollution control equipment." Therefore, the Commission must remand this matter to the Executive Director because his negative use determination is contrary to, and unsupported by, the law, and the evidence in this matter.

The Executive Director's reliance on *Texas Mut. Ins. Co., v. Vista Community Medical Center, LLP.*, 275 S.W.3d 538, 555 (Tex. App.-- Austin 2008), in support of his position that rulemaking was not necessary, is misplaced. The Executive Director admits the Court distinguished that case from *El Paso Hosp. Dist. v. Texas Health and Human Serv. Comm'n*, 247 S.W.3d 709 (Tex. 2008), specifically on the basis that "the ...[Texas Mutual] report does not contradict Rule 134.401." *See Texas Mut. Ins. Co.*, 275 S.W.3d at 556. Here, the Executive Director's negative use determination directly conflicts with both a rule, 30 TEX. ADMIN. CODE § 17.17(b) (as well as the Figure accompanying that provision), and a statute, TEX. TAX CODE § 11.31(k), (m). To make such a material change in policy without formal rulemaking, constitutes an invalid rule under the Texas APA.

In *El Paso Hosp. Dist.*, the Court was asked to declare a rule invalid because the Texas Health and Human Services Commission ("THHSC") neglected to adopt it as the Texas APA requires. This case focused on THHSC's interpretation of what constitutes a "base year." THHSC's rules define the "base year" as "[a] 12-consecutive-month period of claims data selected by the [department] or its designee." 247 S.W.3d at 713, quoting 1 TEX. ADMIN. CODE § 355.8063(b)(5). THHSC's rules required that the "12-consecutive-month period" run concurrently with the State's fiscal year from September 1 to August 31. *Id.*, quoting 1 TEX. ADMIN. CODE § 355.8063(n). In administering its program, THHSC imposed a "cutoff date," selecting claims data only from base-year claims that are paid within the fiscal year plus a six-

month grace period. *Id.* In doing so, THHSC considered only the claims of Medicaid patients admitted during the base year that were actually paid within six months of the base-year's end. Claims for patients admitted during the base year, but not paid by February 28, were not included in determining the prospective reimbursement rates. *Id.*

The Hospitals alleged that THHSC does not use twelve consecutive months of claims data in computing rates as its rules require. *Id.* THHSC argued that it complied with the statutes, and that the February 28 cutoff was not a rule itself, but rather its interpretation of the base-year rule. *Id.* at 714. The Court agreed with the Hospitals, finding that THHSC's "cutoff date" constituted a statement of general applicability that implemented law or describes procedure and was not a statement regarding the agency's internal management or organization but rather affected the Hospitals' private rights. *Id.*, at 714-715.

The Court confirmed, "Under the APA, a rule: (1) is an agency statement of general applicability that either "implements, interprets, or prescribes law or policy" or describes [THHSC's] "procedure or practice requirements;" (2) "includes the amendment or repeal of a prior rule;" and (3) "does not include a statement regarding only the internal management or organization of a state agency and not affecting private rights or procedures." *Id.* at 714, quoting TEX.. GOV'T CODE § 2001.003(6)(A)-(C). As the Court noted, statements of general applicability are "statements that affect the interest of the public at large such that they cannot be given the effect of law without public input." *Id.*

As applied to the facts of this case, the Executive Director's determination abolishing a HRSG's status as pollution control equipment affects all entities seeking to obtain a positive use determination and the resulting tax exemption for having installed such equipment, as well as the respective appraisal districts with taxing authority over those entities. The Executive Director's

determination further implements policy and describes TCEQ's procedure for addressing use determinations for HRSGs. This conclusion is confirmed by the Executive Director's uniform application of this new policy to all of the HRSG use determinations pending before the agency. Finally, the Executive Director's determination is not simply a statement regarding only the internal management or organization of a state agency; it indeed affects the rights of private entities, including both those seeking use determinations and the appraisal districts affected by such determinations.

Consistent with the Court's decision in *El Paso Hosp. Dist.,* TCEQ is required to describe the process used to reach its use determinations through its formally promulgated rules. If the Executive Director proposes to change these procedures, he and the agency must do so through the required and proper rulemaking procedures. *See* TEX. GOV'T CODE § 2001.003(6)(C). Because the Executive Director has not done so, his determination regarding HRSGs is invalid, and this matter must be remanded to the Executive Director.

The Executive Director cites *Railroad Comm'n of Texas v. WBD Oil & Gas Co.*, 104 S.W.3d 69 (Tex. 2003), in support of his position that no rulemaking was required to effect the Executive Director's decision. This case is distinguishable from the use determination matters now before the Commission.

In *WBD Oil & Gas Co.*, the Court reviewed action taken by the Railroad Commission, beginning in January 1986, when the Commission initiated Docket No. 10-87,017. In this action, the Railroad Commission notified all operators in the Panhandle Fields, as well as all other interested persons and the public, that it would hold a hearing to consider consolidating the fields and changing the field rules. *Id.* at 71. The Commission's notice set out proposed changes in the rules but provided notice it would adopt "such rules, regulations, and orders as in its

order in the matter, and whether a declaratory judgment action may be brought under those rules. *See id.*, at 79.

In this matter, the Executive Director declined to provide any notice regarding his intent to change the use determination rules applicable to HRSGs. No opportunity for public comment was provided. No discovery was conducted. No matter was referred to the State Office of Administrative Hearings. No evidence was offered or considered. No trial-like, contested case hearing was conducted. No witnesses provided sworn testimony. No witnesses were cross-examined. No record was kept. None of the public participation mechanisms were utilized by the Executive Director, and the public, including affected regulated entities, was provided no opportunity to participate in the Executive Director's decision-making process. As a result, the Executive Director's reliance on *WBD Oil & Gas Co.* is not supportable.

The Executive Director's decision: (1) constitutes an agency statement of general applicability that either implements, interprets, or prescribes law or policy or describes procedure or practice requirements; (2) includes the amendment or repeal of a prior rule; and (3) does not include a statement regarding only the internal management or organization of a state agency and not affecting private rights or procedures. As such it is a rule under the Texas APA. Because the Executive Director failed to utilize formal rulemaking procedures required under the Texas APA, the Executive Director's decision constitutes an invalid rule. As a result, this matter must be remanded to the Executive Director.

H. The Executive Director's Action is Contrary to Statute and Rule and is Invalid

As noted above, the Executive Director's determination that HRSGs are not "pollution control equipment" is contrary to TEX. TAX CODE § 11.31(k), (m), and 30 TEX. ADMIN. CODE § 17.17(b). These provisions specify that a HRSG is "pollution control equipment" for purposes

of a use determination analysis, and further specify that any change in that status requires rulemaking.

In construing a statute, Texas courts place significant emphasis on the plain language of the statute. As the Texas Supreme Court has stated, "When construing a statute, we begin with its language. '[W]e consider it a fair assumption that the Legislature tries to say what it means, and therefore the words it chooses should be the surest guide to legislative intent.'" *In re Smith*, 333 S.W.3d 582, 586 (Tex. 2011) (quoting, *Leland v. Brandal*, 257 S.W.3d 204, 206 (Tex. 2008)). If a statute is not ambiguous, "a court must adopt the interpretation supported by the statute's plain language unless that interpretation would lead to absurd results." *Texas Prot. & Reg. Serv. v. Mega Child Care*, 145 S.W.3d 170, 177 (Tex. 2004); *TGS-NOPEC Geophysical Co.*, 340 S.W.3d at 439. When a statute's language is clear and unambiguous "'it is inappropriate to resort to the rules of construction or extrinsic aids to construe the language.'" *Texas Lottery Comm'n v. First State Bank of DeQueen*, 325 S.W.3d 628, 637 (Tex. 2010) (quoting *City of Rockwall*, 246 S.W.3d at 626); *Mega Child Care, Inc.*, 145 S.W.3d at 177 (Tex. 2004); *St Luke's Episcopal Hosp. v. Agbor*, 952 S.W.2d 503, 505 (Tex. 1997).

As noted above, no deference is due where an agency's interpretation fails to follow the clear, unambiguous language of its own regulations. *TGS-NOPEC Geophysical Co.*, 340 S.W.3d at 438; *see also Public Util. Comm'n of Texas*, 809 S.W.2d at 207. Under the plain language of TEX. TAX CODE § 11.31(k), (m), and 30 TEX. ADMIN. CODE § 17.17(b), a HRSG is "pollution control equipment." The Executive Director's attempt to determine otherwise is contrary to the law and TCEQ's regulations, and is due no deference.

The Executive Director asserts that the 2009 amendments to the Tax Code, in which the Legislature added TEX. TAX CODE § 11.31(g-1), broadened the Executive Director's authority for

reviewing use determination applications. It is presumed that an entire statute is intended to be effective and, in the event of a conflict between two provisions, the provisions shall be construed, if possible, so that effect is given to both. TEX. GOV'T CODE §§ 311.021(2), 311.026(a); *Acker v. Texas Water Comm'n*, 790 S.W.2d 299, 301 (Tex. 1990).

The two provisions at issue here, TEX. TAX CODE § 11.31(k) and (g-1), are not in conflict. The first provision identifies specific equipment that is designated to be "pollution control equipment" without further action by TCEQ. TEX. TAX CODE § 11.31(k). The second provision emphasizes that all property is required to meet the eligibility requirements for a use determination, including those listed in TEX. TAX CODE § 11.31(k). TEX. TAX CODE § 11.31(g-1). The effect is simply that the Legislature has already pre-determined, absent further rulemaking action by the TCEQ, that the items listed in TEX. TAX CODE § 11.31(k) have already met the "pollution control equipment" eligibility element.

To the extent that two statutory provisions address the same subject, the two should be harmonized if possible in such a manner as to give effect to both. *Acker*, 790 S.W.2d at 301. In this case, the two provisions can be harmonized, as set forth above. If the Commission is concerned that the two provisions cannot be harmonized, the special provision will prevail over the general provision unless the general provision is the later enactment and the manifest intent is that the general provision prevail. TEX. GOV'T CODE § 311.026(b); *Sultan v. Mathew*, 178 S.W.3d 747, 751 (Tex. 2005). The special provision in this case is that set forth in TEX. TAX CODE § 11.31(k).

In summary, the two provisions do not conflict. If the provisions conflicted, the Commission would need to harmonize the two to give effect to both. If the Commission could not harmonize the two provisions, the special provision, TEX. TAX CODE § 11.31(k), would

control. Under any of these scenarios, the Legislature's designation of a HRSG as "pollution control equipment" is confirmed, and the Executive Director's decision is unsupported. The matter instead must be remanded back to the Executive Director.

I. Affirmance of the Executive Director's Action Would be Arbitrary and Capricious

The Texas Supreme Court has held that, if an agency "does not follow the clear, unambiguous language of its own regulation, we reverse its action as arbitrary and capricious." *Rodriguez v. Serv. Lloyds Ins. Co.*, 997 S.W.2d 248, 255 (Tex. 1999). Because the statute and TCEQ's rules designate a HRSG as "pollution control equipment," the Executive Director's decision to the contrary cannot stand. Were the Commission to deny this appeal and affirm the Executive Director's decision, the Commission would not be following the unambiguous language of the statute and its own regulation, and its action would be subject to reversal. To prevent such an occurrence, the Commission should remand this matter for processing in a manner consistent with the statute and the agency's rules.

Further, although an agency is not bound to follow its decisions in prior cases in the same way that a court is, any alteration of an agency's prior interpretation must be accompanied by a timely and rational explanation. *Flores v. Employees Ret. Sys.*, 74 S.W.3d 532, 538-545 (Tex. App.-Austin 2002, pet. denied) (agency acted arbitrarily and capriciously by failing to give prehearing notice of intention not to follow previous decisions). Sudden and unexplained change is arbitrary, capricious and an abuse of discretion. *Smiley v. Citibank (S.D.), N.A.*, 517 U.S. 735, 742 (1996). Such is the case here, where there is no factual explanation for the Executive Director's action in treating similar properties in completely different ways, based on his new determination with respect to the "pollution control equipment" status of a HRSG. As a result,

this matter must be remanded back to the Executive Director for a new determination consistent with the statute and the agency's rules.

III. Conclusion

BEPC has met the statutory and regulatory requirements to establish its eligibility for a positive use determination, as set forth in this Reply and the record before the Commission. The Executive Director's negative use determination is not supported by the facts or the law, is contrary to TEX. TAX CODE § 11.31(k), (m), and 30 TEX. ADMIN. CODE § 17.17(b), and cannot stand. For this reason, this matter should be remanded back to the Executive Director. BEPC therefore respectfully requests that the Commission remand this matter to the Executive Director for a new determination consistent with the applicable statute and the agency's rules.

Prayer

WHEREFORE, PREMISES CONSIDERED, Brazos Electric Power Cooperative, Inc respectfully requests that the Commission remand this matter to the Executive Director for a new determination, consistent with the applicable statute and the agency's rules.

Respectfully submitted,

FULBRIGHT & JAWORSKI L.L.P.

PAUL C. SARAHAN
State Bar No.: 17648200
98 San Jacinto Blvd., Suite 1100
Austin, Texas 78701
Telephone: 512-536-2493
Facsimile: 512-536-4598

Attorneys for Respondent,

BRAZOS ELECTRIC POWER COOPERATIVE, INC.

CERTIFICATE OF SERVICE

I certify that on October 30, 2012, the original and 7 copies of Brazos Electric Power Cooperative, Inc.'s Reply to the Executive Director's Response to the Appeals Filed on the Negative Use Determinations for the Heat Recovery Steam Generator Applications was filed with the Office of the Chief Clerk, Texas Commission on Environmental Quality, and was served by first-class mail, agency mail, electronic mail, or facsimile to the following persons:

Chief Appraiser Jack County Appraisal District P.O. Box 958 Jacksboro, Texas 76058 Telephone: 940/567-6301 Facsimile: 940/567-3640 E-mail: jcad@wf.net	Chance Goodin TCEQ Office of Air MC 206 P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-6335 Facsimile: 512/239-6188 E-mail: chance.goodin@tceq.texas.gov
Steve Hagle, Deputy Director TCEQ Office of Air MC 122 P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-2104 Facsimile: 512/239-3341	Robert Martinez and Daniel Long TCEQ Environmental Law Division MC 173 P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-0600 Facsimile: 512/239-0606
Blas Coy TCEQ Office of Public Interest Counsel MC 103 P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-6363 Facsimile: 512/239-6377	Docket Clerk TCEQ Office of Chief Clerk MC 105 P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-3300 Facsimile: 512/239-3311
Kyle Lucas TCEQ Alternative Dispute Resolution Program MC P.O. Box 13087 Austin, Texas 78711-3087 Telephone: 512/239-0687 Facsimile: 512/239-4015	C. Wayne Frazell, P.E., RPA Pritchard & Abbott, Inc. 4900 Overton Commons Court Ft. Worth, Texas 76132-3687 Telephone: 817/926-7861 Facsimile: 817/927-5314 E-mail: wfrazell@pandai.com

PAUL C. SARAHAN