

The Texas Natural Resource Conservation Commission (commission) proposes new §101.380, Definitions; §101.382, Applicability; §101.383, General Provisions; and §101.385, Recordkeeping and Reporting. The proposed new sections are to be grouped into Subchapter H, Emissions Banking and Trading; new Division 5, System Cap Trading. The sections will also be submitted to the United States Environmental Protection Agency (EPA) as revisions to the state implementation plan (SIP).

BACKGROUND AND SUMMARY OF THE FACTUAL BASIS FOR THE PROPOSED RULES

The proposed rules would simplify emission trading for electric generating facilities (EGFs) operating under a system emission cap in the Dallas/Fort Worth (DFW) ozone nonattainment area and in the attainment counties of east and central Texas. The rules represent a continuing commitment by the commission to incorporate maximum flexibility for the electric industry in achieving the nitrogen oxides (NO_x) emissions reductions necessary to achieve the goal of ozone attainment in the DFW area while maintaining reliability of service. The proposed procedure may be applied to other facilities subject to a system cap under Chapter 117 in subsequent rulemaking.

Emission reduction credit (ERC) trading among companies is allowed under the April 19, 2000 adoption of the DFW ozone attainment demonstration rules for EGFs, which were published in the May 5, 2000 issue of the *Texas Register* (25 TexReg 4140). In order to complete a trade under these existing rules, one source owner must bank an emission credit with the commission and another source owner must receive the executive director's approval to use the credit. This procedure works well for trades which are made relatively infrequently, such as tend to occur when emissions are limited annually. In contrast, the ozone attainment demonstration rules for EGFs in DFW establish daily NO_x

limits because the EGFs in DFW mostly operate on days conducive to exceedences of the ozone standard. This proposed rulemaking would add a trading alternative which would facilitate daily emission trading by reducing the steps necessary to trade allowable emissions among different owners. Under this rule proposal, the source owners would be simply required to report trades and the commission would have the opportunity to review, on a quarterly basis, the daily emissions, 30-day rolling average emissions, and any emission trades which occurred during the preceding calendar quarter.

Currently, individual sources under common ownership or control may be voluntarily grouped together in a system with a system cap on total emissions from the sources in the system. Emission allowables may be transferred from source to source within the system, provided the cap is not exceeded. This proposal would allow the increase of system caps, provided that surplus emission allowables are obtained from another source owner participating in a system cap. The system cap may be increased daily using a daily surplus or on a 30-day rolling average using 30-day rolling average surpluses for the same period.

The rules adopted on April 19, 2000 also established an annual system cap for EGFs in the attainment counties of east and central Texas (25 TexReg 4101). This proposal would allow the exceedence of that system cap provided surplus emission allowable is obtained from another EGFs participating in the system cap. The EGFs affected by Chapter 117 are in the following counties: Atascosa, Bastrop, Bexar, Brazos, Calhoun, Cherokee, Fannin, Fayette, Freestone, Goliad, Gregg, Grimes, Harrison,

Henderson, Hood, Hunt, Lamar, Limestone, Marion, McLennan, Milam, Morris, Nueces, Parker, Red River, Robertson, Rusk, Titus, Travis, Victoria, and Wharton.

The transfer of emission allowable remains restricted to the area, nonattainment or attainment, in which it originates.

SECTION BY SECTION DISCUSSION

The proposed new §101.380 contains definitions for use in this division. Surplus emission allowable is defined as an amount, greater than zero, by which a source's allowable source cap emissions exceed actual emissions for a single day or a 30-day average or tons per year for a calendar year for a source subject to Chapter 117, Subchapter B, Division 2, Utility Electric Generation in East and Central Texas.

The proposed new §101.382 would apply the trading provisions of this division to sources located within a single nonattainment area or other area with unique emission limits as defined in Chapter 117.

The proposed new §101.383 would allow the increase of system cap limits provided surplus allowances are obtained from another owner or operator participating in the system cap. Emissions caps may be increased daily or on a 30-day rolling average, provided allowances are obtained that match the period when the increase occurs. System cap limits for EGFs as regulated under Chapter 117, Subchapter B, Division 2, may be exceeded with surplus emission allowable obtained for that calendar year from another source owner or operator participating in the system cap.

The proposed new §101.385 would require owners or operators of sources in an ozone nonattainment area participating in this trading program to submit quarterly reports based on a calendar year within 30 days of the end of the reporting period. The reports would contain daily NO_x emissions from each source and supporting calculations, rolling 30-day average for each source with supporting calculations, and all emission trades during the reporting period including trade date or period, quantity traded, and trading participants. Similarly, EGFs complying with Chapter 117, Subchapter B, Division 2, would submit reports dated on annual period beginning January 1 of each year and submitted within 30 days following the end of the annual period. The report would detail annual emissions with supporting calculations and all emission trades during the report period including trade date, quantity traded, and trade participants. This section would also require owners or operators to report to the commission, within 48 hours, any exceedences of a system cap when there were not allowances available to compensate for that exceedence.

FISCAL NOTE: COSTS TO STATE AND LOCAL GOVERNMENT

John Davis, Technical Specialist with Strategic Planning and Appropriations, determined for each year of the first five-year period the proposed rules are in effect, there may be positive fiscal implications, which are not anticipated to be significant, for owners of boilers and turbines in the four-county DFW nonattainment area and the 95-county central and east Texas attainment area as a result of administration or enforcement of the proposed rules. There are 23 investor-owned boilers and 13 boilers owned by municipalities in the DFW area that could be affected by the proposed rules. In addition, there are approximately 65 investor-owned boilers and turbines and 36 boilers and turbines owned by municipalities, cooperatives, or river authorities in the east and central Texas attainment

areas that could be affected by the proposed rules. There will be no fiscal implications for units of state and local government that do not own or operate boilers or turbines at EGFs in the affected areas. The proposed rules are intended to simplify and expand the trading of emissions for regulated NO_x sources in the affected areas.

This proposal is intended to provide increased flexibility for regulated NO_x sources by adding another emission trading alternative to meet required emission levels. Regulated NO_x sources in the affected areas that are operating under a system cap are eligible to participate in the system cap trading program. This proposal would allow the trading of emissions between different entities as long as participating sources are operating under a system cap. A NO_x source would only be allowed to exceed the system cap by obtaining surplus emissions from other sources.

The system cap trading program differs from the emission credit banking and trading program, because there is no banking of emissions with the agency. All trading is done between entities with overall trading reports and emission levels provided to the commission on a quarterly or annual basis. The proposed system cap trading program is intended to enhance daily trading of emissions by allowing direct trades between entities without prior agency approval and to implement annual trading in the east and central Texas attainment area. The commission does not anticipate significant fiscal impacts to units of state and local government due to the quarterly reporting requirement.

Examples of NO_x sources at facilities that could be affected by the proposed rules include electric utility boilers and stationary gas turbines. Currently, only EGFs are eligible under Chapter 117 rules to participate in the system cap trading program.

There are approximately 23 investor-owned boilers and 13 boilers owned by municipalities in the DFW area that could be affected by the proposed rules if the owners of these boilers decide to participate in the system cap trading program. In addition, there are approximately 65 investor-owned boiler and turbine EGFs and 36 boiler and turbine EGFs owned by river authorities, cooperatives, or municipalities in the east and central Texas attainment area which could be affected by the proposed rules if the owners of these boilers and turbines decide to participate in the system cap trading program.

The counties in the affected attainment areas are: Atascosa, Bastrop, Bexar, Brazos, Calhoun, Cherokee, Fannin, Fayette, Freestone, Goliad, Gregg, Grimes, Harrison, Henderson, Hood, Hunt, Lamar, Limestone, Marion, McLennan, Milam, Morris, Nueces, Parker, Red River, Robertson, Rusk, Titus, Travis, Victoria, and Wharton. The transfer of emission allowable remains restricted to the area, nonattainment or attainment, in which it originates. Although the exact cost per ton for an emission credit traded in the system cap trading program is unknown, the commission estimates that the cost will be similar to ERCs currently traded in the DFW and Houston/Galveston (HGA) areas. The current cost for ERCs in HGA is approximately \$3,600 per ton per year. Actual costs will be dependent on availability and demand. Total costs to state and local government sites that elect to participate in the system cap trading program will depend on the amount of emissions purchased. Emission trading under this program is intended to provide flexibility for regulated NO_x sources and potential cost savings in planning and determining the most economical mix of the application of

emission control technology with the purchase of surplus emissions from other NO_x sources to meet emission reduction requirements. Additionally, facilities that remain within their emission caps may receive additional revenue from selling surplus emissions to other emission sources.

PUBLIC BENEFIT AND COSTS

Mr. Davis also determined for each of the first five years the proposed rules are in effect, the public benefit anticipated as a result on implementing the rules will be the reduction of emissions of NO_x in the DFW and east and central Texas areas and increased flexibility for regulated facilities to meet emission reduction requirements.

This proposal is intended to provide increased flexibility for regulated NO_x sources by adding another emission trading alternative to meet required emission levels. Regulated NO_x sources in the affected areas that are operating under a system cap are eligible to participate in the system cap trading program, which allows the trading of emissions between different entities as long as participating sources are operating under a system cap. A NO_x source would only be allowed to exceed the system cap by obtaining surplus emissions from other sources.

It is anticipated that the majority of owners and operators of the approximately 23 investor-owned and operated boilers located at EGFs in the DFW area would be affected by the proposed rulemaking by electing to participate in the system cap trading program. Although the exact cost per ton for an emission credit traded in the system cap trading program is unknown, the commission estimates the cost will be similar to ERCs currently traded in the DFW and HGA areas. The current cost for ERCs in

HGA is approximately \$3,600 per ton per year. Actual costs will be dependent on availability and demand. Total costs to individuals and businesses that elect to participate in the system cap trading program will depend on the amount of emissions purchased. Emission trading under this program is intended to provide flexibility for regulated NO_x sources and potential cost savings in planning and determining the most economical mix of the application of emission control technology with the purchase of other NO_x source's surplus emissions to meet emission reduction requirements. Additionally, facilities that remain within their emission caps may receive additional revenue from selling surplus emissions to other emission sources.

SMALL BUSINESS AND MICRO-BUSINESS ASSESSMENT

No adverse fiscal implications are anticipated for small or micro-businesses as a result of administration or enforcement of the proposed rules. The proposed rules would allow EGFs in the DFW and east and central Texas areas to participate in the system cap trading program. There are no known small or micro-businesses that own or operate affected EGFs in the affected areas; therefore, the commission anticipates there will be no fiscal impact for small or micro-businesses as a result of the proposed rules.

DRAFT REGULATORY IMPACT ANALYSIS DETERMINATION

The commission reviewed the proposed rulemaking in light of the regulatory analysis requirements of Texas Government Code, §2001.0225. The commission determined that these proposed new sections do not meet the definition of a "major environmental rule" as defined in Texas Government Code, §2001.0225. "Major environmental rule" means a rule, the specific intent of which, is to protect the environment or reduce risks to human health from environmental exposure, and that may adversely

affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, or the public health and safety of the state or a sector of the state. The commission is proposing these new sections to allow greater flexibility for sources in the affected areas to meet NO_x emission limitations and for NO_x emissions trading. The proposed new sections do not adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, or the public health and safety of the state or a sector of the state; therefore, this proposal does not constitute a major environmental rule. In addition, Texas Government Code, §2001.0225, only applies to a major environmental rule, the result of which is to: 1.) exceed a standard set by federal law, unless the rule is specifically required by state law; 2.) exceed an express requirement of state law, unless the rule is specifically required by federal law; 3.) exceed a requirement of a delegation agreement or contract between the state and an agency or representative of the federal government to implement a state and federal program; or 4.) adopt a rule solely under the general powers of the agency instead of under a specific state law. This rulemaking is not subject to the regulatory analysis provisions of §2001.0225(b), because the proposed rules do not meet any of the four applicability requirements. Specifically, the emission banking and trading requirements were developed in order to meet the ozone national ambient air quality standard (NAAQS) set by the EPA under the Federal Clean Air Act (FCAA), §109 (42 United States Code (USC), §7409), and therefore meet a federal requirement. Provisions of 42 USC, §7410, require states to adopt a SIP which provides for “implementation, maintenance, and enforcement” of the primary NAAQS in each air quality control region of the state. While §7410 does not require specific programs, methods, or reductions in order to meet the standard, state SIPs must include “enforceable emission limitations and other control measures, means or techniques (including economic incentives such as fees, marketable permits, and

auctions of emissions rights), as well as schedules and timetables for compliance as may be necessary or appropriate to meet the applicable requirements of this chapter,” (meaning Chapter 85, Air Pollution Prevention and Control). It is true that 42 USC does require some specific measures for SIP purposes, like the inspection and maintenance program, but those programs are the exception, not the rule, in the SIP structure of 42 USC. The provisions of 42 USC recognize that states are in the best position to determine what programs and controls are necessary or appropriate in order to meet the NAAQS. This flexibility allows states, affected industry, and the public, to collaborate on the best methods for attaining the NAAQS for the specific regions in the state. Even though 42 USC allows states to develop their own programs, this flexibility does not relieve a state from developing a program that meets the requirements of §7410. Thus, while specific measures are not generally required, the emission reductions are required. States are not free to ignore the requirements of §7410 and must develop programs to assure that the nonattainment areas of the state will be brought into attainment on schedule.

The requirement to provide a fiscal analysis of proposed regulations in the Texas Government Code was amended by Senate Bill (SB) 633 during the 75th Legislative Session, 1999. The intent of SB 633 was to require agencies to conduct a regulatory impact analysis (RIA) of extraordinary rules. These are identified in the statutory language as major environmental rules that will have a material adverse impact and will exceed a requirement of state law, federal law, or a delegated federal program, or are adopted solely under the general powers of the agency. With the understanding that this requirement would seldom apply, the commission provided a cost estimate for SB 633 that concluded “based on an assessment of rules adopted by the agency in the past, it is not anticipated that the bill will have

significant fiscal implications for the agency due to its limited application.” The commission also noted that the number of rules that would require assessment under the provisions of the bill was not large. This conclusion was based, in part, on the criteria set forth in the bill that exempted proposed rules from the full analysis unless the rule was a major environmental rule that exceeds a federal law. As previously discussed, 42 USC does not require specific programs, methods, or reductions in order to meet the NAAQS; thus, states must develop programs for each nonattainment area to ensure that area will meet the attainment deadlines. Because of the ongoing need to address nonattainment issues, the commission routinely proposes and adopts SIP rules. The commission bases these actions on the presumption that the legislature understands this federal scheme. If each rule proposed for inclusion in the SIP was considered to be a major environmental rule that exceeds federal law, then every SIP rule would require the full RIA contemplated by SB 633. This conclusion is inconsistent with the conclusions reached by the commission in its cost estimate and by the Legislative Budget Board (LBB) in its fiscal notes. Because it is a rule of statutory interpretation that the legislature is presumed to understand the fiscal impacts of the bills it passes, and that presumption is based on information provided by state agencies and the LBB, the commission believes that the intent of SB 633 was only to require the full RIA for rules that are extraordinary in nature. While the SIP rules will have a broad impact, that impact is no greater than is necessary or appropriate to meet the requirements of the FCAA. For these reasons, rules proposed for inclusion in the SIP fall under the exception in Texas Government Code, §2001.0225(a), because they are required by federal law. The rulemaking does not exceed a standard set by federal law, exceed an express requirement of state law (unless specifically required by federal law), or exceed a requirement of a delegation agreement. The rulemaking was not developed solely under the general powers of the agency, but was specifically developed to meet the

NAAQS established under federal law and authorized under Texas Clean Air Act (TCAA), §§382.011, 382.012, and 382.017 as well as under 42 USC, §7410(a)(2)(A).

The commission invites public comment on the draft RIA.

TAKINGS IMPACT ASSESSMENT

The commission completed a takings impact assessment for the proposed rules. The following is a summary of that assessment. The sections are proposed as part of a strategy to reduce and permanently cap emissions of NO_x to a level which would allow the DFW nonattainment area to attain the NAAQS for ozone and to maintain air quality in the east and central Texas area. Promulgation and enforcement of the rules will not burden private real property. The proposed new sections do not affect private property in a manner which restricts or limits an owner's right to the property that would otherwise exist in the absence of a governmental action. Additionally, the NO_x emissions under the system cap that are the subject of these rules are not property rights. Consequently, the proposed sections do not meet the definition of a takings under Texas Government Code, §2007.002(5). Although the proposed sections do not directly prevent a nuisance or prevent an immediate threat to life or property, they do prevent a real and substantial threat to public health and safety, and partially fulfill a federal mandate under the USC, §7410. Specifically, the emission limitations and control requirements that are the subject of this proposal were developed in order to meet the ozone NAAQS set by the EPA under the USC, §7409. States are primarily responsible for ensuring attainment and maintenance of the NAAQS once the EPA has established them. Under the USC, §7410 and related provisions, states must submit, for approval by the EPA, SIPs that provide for the attainment and maintenance of NAAQS through

control programs directed to sources of the pollutants involved. Therefore, the purpose of the rule proposal is to implement a NO_x strategy which is necessary for the DFW area to meet the air quality standards established under federal law and to maintain air quality in east and central Texas.

Consequently, the exemption which applies to these proposed rules is that of an action reasonably taken to fulfill an obligation mandated by federal law. Therefore, these proposed revisions will not constitute a takings under Texas Government Code, Chapter 2007.

CONSISTENCY WITH THE COASTAL MANAGEMENT PROGRAM

The commission determined the proposed rulemaking relates to an action or actions subject to the Texas Coastal Management Plan (CMP) in accordance with the Coastal Coordination Act of 1991, as amended (Texas Natural Resource Code, §§33.201 et seq.), and the commission's rules in 30 TAC Chapter 281, Subchapter B, concerning Consistency with the Texas Coastal Management Program. As required by 30 TAC §505.11(b)(2) and 30 TAC §281.45(a)(3), relating to actions and rules subject to the CMP, commission rules governing air pollutant emissions must be consistent with the applicable goals and policies of the CMP. The commission reviewed this action for consistency with the CMP goals and policies in accordance with the regulations of the Coastal Coordination Council and determined the proposed rules are consistent with the applicable CMP goal expressed in 31 TAC §501.12(1) of protecting and preserving the quality and values of coastal natural resource areas, and the policy in 31 TAC §501.14(q), which requires the commission protect air quality in coastal areas. The proposed new sections would allow greater flexibility in meeting system cap requirements by trading NO_x emissions between sources in the DFW and east and central Texas areas. These proposed rules do not authorize

any new NO_x air emissions. Interested persons may submit comments on the consistency of the proposed rules with the CMP during the public comment period.

EFFECT ON SITES SUBJECT TO THE FEDERAL OPERATING PERMITS PROGRAM

The proposed new sections, if adopted, would become part of the state's ozone attainment strategy; therefore, these revisions would be submitted as part of the SIP. As a result, the proposed sections would become applicable requirements under the federal operating permit program and sources would be required to amend their permits.

ANNOUNCEMENT OF HEARING

The commission will hold public hearings on this proposal in Irving on January 3, 2001 at 6:00 p.m. at the City of Irving Public Library Auditorium, located at 801 West Irving Boulevard and in Austin on January 4, 2001, at 2:00 p.m., at the Texas Natural Resource Conservation Commission, Building B, Room 201A, located at 12100 Park 35 Circle. The hearings will be structured for the receipt of oral or written comments by interested persons. Individuals may present oral statements when called upon in order of registration. There will be no open discussion during the hearings; however, an agency staff member will be available to discuss the proposal 30 minutes prior to the hearings and will answer questions before and after the hearings.

Persons with disabilities who have special communication or other accommodation needs, who are planning to attend the hearings, should contact the Office of Environmental Policy, Analysis, and Assessment at (512) 239-4900. Requests should be made as far in advance as possible.

SUBMITTAL OF COMMENTS

Comments may be submitted to Lola Brown, Office of Environmental Policy, Analysis, and Assessment, MC 206, P.O. Box 13087, Austin, Texas 78711-3087 or faxed to (512) 239-4808. All comments should reference Rule Log Number 2000-046-101-AI. Comments must be received by 5:00 p.m., January 5, 2001. For further information, please contact Matthew R. Baker at (512) 239-1091 or Beecher Cameron at (512) 239-1495.

STATUTORY AUTHORITY

The new sections are proposed under the Texas Health and Safety Code, TCAA, §382.011, which authorizes the commission to control the quality of the state's air; §382.012, which authorizes the commission to develop a plan for control of the state's air; §382.017, which provides the commission the authority to adopt rules consistent with the policy and purposes of the TCAA; and 42 USC, §7410(a)(2)(A), which requires SIPs to include enforceable emission limitations and other control measures or techniques, including economic incentives such as fees, marketable permits, and auction of emission rights.

The proposed new sections implement TCAA, §382.011, General Powers and Duties; §382.012, State Air Control Plan; and §382.017, Rules.

SUBCHAPTER H: EMISSIONS BANKING AND TRADING

DIVISION 5: SYSTEM CAP TRADING

§§101.380, 101.382, 101.383, 101.385

§101.380. Definitions.

The following words and terms, when used in this division, shall have the following meanings, unless the context clearly indicates otherwise: **Surplus emission allowable** - The amount, greater than zero, that a source owner or operator's allowable emissions in a system cap emission limit specified in Chapter 117 of this title (relating to Control of Air Pollution from Nitrogen Compounds) is greater than the actual emissions in that system, in:

(1) pounds per day for a:

(A) single day; or

(B) rolling 30-day average period; or

(2) tons per year for a calendar year period for a source subject to Chapter 117, Subchapter B, Division 2 of this title (relating to Utility Electric Generation in East and Central Texas).

§101.382. Applicability.

Trades of emission allowables are limited to sources located within a single nonattainment area or within another single area with unique emission limits identified in Chapter 117 of this title (relating to Control of Air Pollution from Nitrogen Compounds).

§101.383. General Provisions.

(a) System cap limits may be exceeded with surplus emission allowable obtained for that day from another source owner or operator participating in a system cap. The owner or operator may exceed the:

(1) maximum daily cap with a one-day surplus emission allowable generated on the same day; and

(2) rolling 30-day average daily system cap emission limitation with a surplus emission allowable generated over the same period.

(b) System cap limits for utility electric generating units as regulated under Chapter 117, Subchapter B, Division 2 of this title (relating to Utility Electric Generation in East and Central Texas) may be exceeded with surplus emission allowable obtained for that calendar year from another source owner or operator participating in a system cap.

(c) The cap requirements of Chapter 117 of this title (relating to Control of Air Pollution from Nitrogen Compounds) continue to apply, except as modified in subsection (a) of this section.

§101.385. Recordkeeping and Reporting.

(a) The owner or operator of a source in an ozone nonattainment area participating with this division shall submit to the executive director a quarterly report.

(1) Each quarterly report will be based on a three-calendar month period beginning on January 1 of each year.

(2) The report shall be submitted within 30 days following the end of the quarterly period.

(3) The report shall detail the following:

(A) the daily nitrogen oxides (NO_x) emissions from each source along with supporting calculations for the maximum daily cap and the rolling 30-day average system cap emission limitation;

(B) all emission trades during the reported time period including the trade date or period, quantity traded, and trading participants.

(b) The owner or operator of a source participating in a system cap limit for sources subject to Chapter 117, Subchapter B, Division 2 of this title (relating to Utility Electric Generation in East and Central Texas) shall submit to the executive director an annual report.

(1) Each annual report will be based on a 12-month calendar period beginning on January 1 of each year.

(2) The report shall be submitted within 30 days following the end of the annual period.

(3) The report shall detail the following:

(A) the annual NO_x emissions from each source along with supporting calculations; and

(B) all emissions trades during the reported time period including trade date, quantity traded, and trade participants.

(c) The owner or operator of any system participating in this division shall report within 48 hours to the executive director any time that the system exceeded its daily or rolling 30-day average system cap emission limitation, or within 30 days any time that the system exceeded its annual system cap, and did not obtain surplus emission allowable for that time period. This report shall include:

(1) cause of the exceedence with data to demonstrate the amount of emissions in excess of the applicable limit;

(2) date or period of exceedence;

(3) amount of exceedence; and

(4) number of surplus emissions allowables traded on the date of or during the period of the exceedence.