The Texas Natural Resource Conservation Commission (TNRCC or commission) adopts new §101.330, Definitions; §101.331, Applicability; §101.332, General Provisions; §101.333, Allocation of Allowances; §101.334, Allowance Deductions; §101.335, Allowance Banking and Trading; §101.336, Emission Monitoring, Compliance Demonstration, and Reporting; and §101.337, El Paso Region. The sections are adopted with changes to the proposed text as published in the September 10, 1999 issue of the *Texas Register* (24 TexReg 7137). The adopted rules will also be submitted as a proposed revision to the state implementation plan (SIP).

BACKGROUND AND SUMMARY OF THE FACTUAL BASIS FOR THE ADOPTED RULES

Senate Bill 7 (SB 7), 76th Legislature, 1999, amended the Texas Utilities Code (TUC), Title 2, Public Utility Regulatory Act, Subtitle B, Electric Utilities, and created a new Chapter 39, Restructuring of Electric Utility Industry. SB 7 requires the commission to implement the permitting and allowance requirements of new TUC, §39.264, concerning Emissions Reductions of "Grandfathered Facilities." TUC, §39.264 requires the commission to develop a mass cap and trade system to distribute emission allowances for use by grandfathered and electing electric generating facilities (EGF). Under TUC, §39.264, two categories of EGFs are eligible to use the adopted trading system. The first category consists of EGFs in existence on January 1, 1999, which were not subject to the requirement to obtain a permit under Texas Clean Air Act (TCAA), §382.0518(g). These facilities are referred to as "grandfathered" facilities. The second category of EGFs consists of permitted EGFs that are not subject to the permitting requirements of TUC, §39.264, yet elect to participate in the allowance trading system. These facilities are referred to as "electing" EGFs. TUC, §39.264 also requires that

grandfathered EGFs apply for a permit on or before September 1, 2000, and obtain a permit by or cease operation after May 1, 2003.

These new sections are adopted concurrently with new sections in 30 TAC Chapter 116, concerning Control of Air Pollution by Permits for New Construction or Modification. The new Chapter 116, Subchapter I, concerning Electric Generating Facility Permits, contains the requirements for permitting of grandfathered and electing EGFs. The adopted amendments to Chapter 116 are published in this issue of the *Texas Register*.

TUC, §39.264(g) and (h) requires the commission to allocate emission allowances to grandfathered EGFs in defined regions of the state. As stated in TUC, §39.264(c), the Legislature intended that total annual emissions of nitrogen oxides (NO_x) from grandfathered EGFs would not exceed 50% of the emissions during 1997 as reported to the commission, and additionally for coal-fired grandfathered EGFs, total annual emissions of sulfur dioxide (SO_2) would not exceed 75% of the emissions during 1997 as reported to the commission. To further this goal, TUC, §39.264(h) provided emission rates to calculate specific allowances.

TUC, §39.264(c) allows emission limitations to be met through an emissions allocation and allowance transfer system. An allowance trading program is a regulatory program which caps emissions over a designated region to a level consistent with regulatory goals. Each grandfathered and electing EGF must hold allowances equal to or greater than its emissions to be in compliance with the program. For example, if a grandfathered EGF's emissions are 100 tons over the control period, the compliance

account for this grandfathered EGF should reflect a balance equal to or greater than 100 tons of allowances. The program encourages EGFs to determine the methods of control which will allow the EGF to meet its allowances. Further, the program allows for trading of allowances between grandfathered and electing EGFs in the same region, thereby creating alternatives for control. For example, if a grandfathered EGF emitted 100 tons over the control period and has a balance of 150 allowances in its compliance account, the grandfathered EGF may sell the unused portion--50 tons of allowances--to another grandfathered or electing EGF. This trading provision allows companies to determine the most economical method of meeting the regulation, either by purchasing surplus allowances created by another grandfathered or electing EGF's reductions, or by making their own reductions.

Consistent with TUC, §39.264(i), EGFs currently permitted under 30 TAC Chapter 116, Subchapter B, concerning New Source Review Permits, may elect to participate in the permitting program adopted concurrently in Chapter 116, Subchapter I. These permitted facilities electing to participate in the permitting program under Chapter 116, Subchapter I are called “electing” EGFs. In the concurrently adopted amendments to Chapter 116, the existing New Source Review (NSR) permit will be altered to include a reference to a permit issued under Chapter 116, Subchapter I. Participation in the permitting program will allow electing EGFs to obtain allowances under the emissions banking and trading of allowances (EBTA) program. It may be advantageous for a company to include all EGFs, regardless of permitting status, in the permitting program to allow maximum flexibility in control strategies. Under TUC, §39.264(i)(2) and (4), electing EGFs are given allowances equal to their actual emissions

reported in the 1997 Emissions Scorecard from EPA's Acid Rain Program unless a federal or state standard otherwise limits the emission rate.

SECTION BY SECTION DESCRIPTION

The new §101.330 contains the definitions to be used in the EBTA. "Allowance" means the authorization to emit one ton of NO_x or SO_2 during the specified control period or any specified control period thereafter. "Authorized account representative" is the responsible person who is authorized, in writing, to transfer and otherwise manage allowances. "Banked allowance" is an allowance which is not used to reconcile emissions in the designated year of allocation, but which is carried forward into next year and noted in the compliance or broker account as "banked." In response to public comment, a new definition of "Broker" was added to §101.330(4). "Broker" means a person who opens an account and participates in the EBTA for the purposes of banking and trading emissions allowances and not to satisfy emission requirements of an EGF. "Broker account" means the account where allowances held by a broker are recorded. Allowances held in a broker account may not be used to satisfy compliance requirements for these rules. Grandfathered and electing EGFs can purchase allowances from brokers; however, the allowances are not eligible to meet reduction requirements until the ownership of the allowances has been transferred and the allowances reside in the purchaser's compliance account. The definition of "Coal" was added to §101.330(6) to clarify any references to coal-fired EGFs. "Coal" means all solid fuels classified as anthracite, bituminous, subbituminous, or lignite by the American Society for Testing and Materials Designation ASTM D388–92 ''Standard Classification of Coals by Rank'' (as incorporated by reference in Title 40 Code of Federal Regulations (CFR), §72.13 (effective June 25, 1999)). The definition of "Coal-fired" was added to §101.330(7) to

clarify any references to coal-fired EGFs. "Coal-fired" means the combustion of fuel consisting of coal or any coal-derived fuel (except coal-derived gaseous fuels with a sulfur content no greater than natural gas), alone or in combination with any other fuel. The definition is independent of the percentage of coal or coal-derived fuel consumed during any control period. "Compliance account" means the account for a grandfathered or electing EGF or for multiple grandfathered or electing EGFs in which allowances are held. An EGF not under common control or ownership may have separate compliance accounts for the purpose of meeting the requirements of the EBTA and Chapter 116, Subchapter I. "Control period" means the 12-month period beginning May 1 of each year and ending April 30 of the following year, which is consistent with TUC, §39.264(c). Control periods will begin May 1, 2003. "East Texas Region" means all counties traversed by or east of Interstate Highway 35 (IH-35) north of San Antonio, or traversed by or east of Interstate Highway 37 (IH-37) south of San Antonio, and also including Bexar, Bosque, Coryell, Hood, Parker, Somerville, and Wise Counties. The commission has modified the definition of "East Texas Region" from TUC, §39.264(g) to clarify that counties east of IH-35 and west of IH-37 are not included in this region. The commission believes that had the Legislature intended for the definition to include these counties, the definition would have simply referenced IH-35 and not IH-37 also. Additionally, these counties (between IH-35 and IH-37) have been excluded from commission plans involving statewide air control strategies, and the commission believes that the Legislature was attempting to be consistent with current commission planning structures. "Electric generating facility" means a facility that generates electric energy for compensation and is owned or operated by a person in this state, including a municipal corporation, electric cooperative, or river authority. "Electing electric generating facility" is an EGF that is not subject to the requirements of TUC, §39.264, that elects to comply with Chapter 116, Subchapter I.

The definition of "El Paso Region" was revised in response to comments, and the basis for this revision is discussed in the ANALYSIS OF TESTIMONY portion of this preamble. The "El Paso Region" is now defined to include all of El Paso County, Ciudad Juarez, Mexico, and Sunland Park, New Mexico. The definition for "Grandfathered electric generating facility" was added to §101.330(14) to clarify any references to "grandfathered" EGFs. "Grandfathered electric generating facility" means a facility that is not subject to the requirements to obtain a permit under TCAA, §382.0518(g) and that generates electric energy for compensation and is owned or operated by a person in this state, including a municipal corporation, electric cooperative, or river authority. The commission originally modified this definition to exclude a facility that generates electric energy primarily for internal use, but during 1997 sold to a utility power distribution system less than one-third of its potential electrical output capacity. This exclusion eliminates cogeneration facilities that were not intended to be included in this program. This portion of the definition regarding cogeneration facilities was removed and placed under §101.331(b), regarding Applicability. The exemption was modified to also exclude EGFs that sold less than 219,000 megawatt hours to a utility power distribution system. This reference was added to exempt small cogenerators who may exceed the one-third limitation. This is more consistent with the Acid Rain Program exemption for affected units. "Heat input" is the heat derived from the combustion of any fuel at an EGF. Heat input does not include the heat derived from reheated combustion air, recirculated flue gas, or exhaust from other sources. The definition of "NO_x" was revised in response to comments. "NO_x allowance" is an authorization to emit NO_x, valid only for the purposes for meeting the requirements of this division and Chapter 116, Subchapter I. The definition of "Permitted electric generating facility" was removed from §101.330. The term "permitted" was unclear as used in the proposed rule as to whether "permitting" was referencing a permit under Chapter 116, Subchapter

B, Subchapter H, or Subchapter I. The rules were changed to specifically identify the type of permit being referenced. The definition of "Person" was added to §101.330(17) in response to comments. "Person" for the purpose of initial issuance of permits under Chapter 116, Subchapter I, and for the issuance of allowances under these rules, includes an individual, a partnership of two or more persons having a joint or common interest, a mutual or cooperative association, and a corporation, but does not include an electric cooperative. "SO_2 allowance" is an authorization to emit SO_2, valid only for the purposes for meeting the requirements of these rules and Chapter 116, Subchapter I. "West Texas Region" means all counties not contained in the East Texas or El Paso Regions.

The new §101.331 establishes the applicability of banking and trading allowances. EGFs subject to the concurrently adopted Chapter 116, Subchapter I or electing EGFs would be required to comply with EBTA. The section also allows the opening of broker accounts for those not required to participate in the EBTA. Since §101.330(4) now includes the definition of "Broker," this section was revised to refer to "brokers."

The new §101.332 contains the general provisions for the EBTA. Compliance with the allowance system would begin with the control period beginning May 1, 2003. Allowances would only be valid for meeting the purposes of the EBTA, and cannot be used to meet or exceed the limitations of any permit or applicable law, generate emission reduction credits, or satisfy emission offset requirements under federal NSR. Because allowances do not by themselves meet federal criteria as creditable emission reductions, they may not be used to satisfy other requirements of the Federal Clean Air Act (FCAA), such as netting for Prevention of Significant Deterioration (PSD), NSR, or offsets under a

nonattainment NSR permit. Neither a NO_x allowance nor an SO_2 allowance constitutes a security or property right. To meet the requirements of TUC, §39.264(e), this section requires that on June 1 of each year, beginning in 2004, an EGF shall hold in its compliance account a quantity of allowances that is equal to or greater than the total emissions of that air contaminant emitted during the prior control period. The original proposal required that the quantity of allowances should be in place by May 1; however, this was in response to comments to allow a 30-day reconciliation period. The commission requires that allowances be allocated, transferred, or used as whole allowances. For simplicity, the number of allowances will be rounded down for decimals less than 0.50 and rounded up for decimals of 0.50 or greater. This section also allows only one compliance account for use by multiple permitted EGFs located at the same property and under common ownership or control. These limitations on the number of compliance accounts will assist the commission in the allocation of allowances and tracking of allowance transfers. Section 101.332(i), which incorporated TUC, §39.264(n), concerning the deduction of allowances from compliance accounts where the EGF exceeded its allowances, was moved to §101.333(4) for organizational clarity.

The new §101.333(1) and (2) contains the methods by which allowances for grandfathered and electing EGFs are calculated. As specified in TUC, §39.264(h), the allowances will be calculated by multiplying total heat input measured in millions of British thermal units (MMBtu) during 1997 by an emission rate expressed in pounds/MMBtu divided by 2,000. To determine allowances, the commission will use information obtained from the United States Environmental Protection Agency's (EPA) 1997 Acid Rain Program's Emissions Scorecard. This scorecard is the only readily-available, consistently-reported, and comprehensive source of 1997 heat input data for EGFs. This was the basis

for determining the emission rates necessary to achieve the program's goals of a 50% reduction in NO_x emissions, and for coal-fired EGFs, 25% reduction in SO_2 emissions from 1997 levels. If information for an EGF concerning heat input is not reported to the acid rain scorecard, the executive director may approve a method for calculating heat input for that EGF as long the method is consistent with the requirements of the acid rain scorecard. Paragraphs (1) and (2) also specify the emission rates for the El Paso, East Texas, and West Texas Regions. In the East Texas Region, the emission rate is 0.14 pounds of NO_x per MMBtu and 1.38 pounds of SO_2 per MMBtu. The emission rate in the West Texas and El Paso Regions is 0.195 pounds of NO_x per MMBtu. Consistent with TUC, §39.264(i)(2), the allowances for electing EGFs are equal to the EGF's emission in tons in 1997. Should a coal-fired EGF permitted under Chapter 116, Subchapter B, elect to participate in the permitting program under Chapter 116, Subchapter I, the annual emissions of SO_2 from 1997 would be used to establish its allowances.

In addition to the 50% reduction expected from grandfathered EGFs under TUC, §39.264, the commission anticipates adopting additional requirements for EGFs in nonattainment areas to meet the ozone National Ambient Air Quality Standard (NAAQS). For each nonattainment area, the amount of reductions for the SIP will be consistent with the SIP modeling efforts for that area. At this time, the point source reductions expected in the Dallas/Fort Worth (DFW) area are 88%. Reductions in the Beaumont/Port Arthur (BPA) area are expected to be 40-50%, and reductions in the Houston/Galveston (HGA) area are expected to be 90%. The commission expects to propose the reductions for BPA and DFW areas in December of 1999. For the HGA area, proposal is expected in May of 2000. The commission expects to propose reductions in attainment counties of east and central Texas not later than

December of 1999. Future rulemaking addressing these reductions may affect the EBTA and the allocation of future allowances. TUC, §39.264(s) recognizes the current authority of the commission to require additional reductions of NO_x or SO_2, and as future SIP rules are developed allowances may be reduced accordingly. The new §101.333(3) incorporates this authority. The new §101.333(4), concerning the deduction of allowances from compliance accounts where the EGF exceeded its allowances, was added to incorporate the requirements of TUC, §39.264(n). Paragraph (4) was moved from §101.332(i) for organizational clarity.

The commission must allocate allowances for grandfathered EGFs by January 1, 2000, as required by TUC, §39.264(h). In order to meet this deadline, the commission will issue an order prior to January 1, 2000 to allocate these allowances. The list entitled "Nitrogen Oxide and Sulfur Dioxide Allowances for Grandfathered Electric Generating Facilities" is available from the commission on request and is available on the commission's Web Site. To meet the statutory deadline to issue allowances by January 1, 2000, the new §101.333(5) provides that a commission order will be issued by that date with the allowances for grandfathered EGFs. The allowances allocated for subsequent years will reflect the same values issued in the initial allocation.

Initial allowances for electing EGFs for the control period beginning May 1, 2003 will be allocated by January 1, 2001. Since the commission will not know which EGFs are electing to participate in the permitting program until September 1, 2000, it would be impossible to allocate allowances for electing EGFs on the same schedule as the grandfathered allocations. This later allocation schedule will allow companies to determine whether to participate in the programs and which programs best suit their

individual business needs. The new §101.333(5)(A)(ii), formerly §101.333(4)(A)(ii), requires allocation of allowances for electing EGFs by January 1, 2001. This section was revised to include municipal corporations, electric cooperatives, and river authorities that choose to obtain a permit under Chapter 116, Subchapter I for EGFs that were previously exempted under 30 TAC §116.910(d) from the permitting program. These EGFs will also be allocated allowances by January 1, 2001.

To allow EGFs to identify potential sellers of allowances, the commission shall maintain a publicly available registry of the allowances in each compliance account as provided in the new §101.333(7). For each transfer, the registry shall include the price paid per allowance. The registry shall not contain proprietary information. The commission believes that public access to information regarding the price and transfer of allowances will promote an open trading system.

In response to comments, the new §101.334 was renamed "Allowance Deductions" and modified extensively from the proposal. The section now addresses only the deduction of allowances from compliance accounts. The section specifies the method or equations that will be used to determine the amount of allowances to be deducted at the end of each control period from compliance accounts in three circumstances: (1) for electing EGFs whose heat input for the control period is equal to or greater than its heat input for 1997, for all grandfathered EGFs, and electing EGFs whose heat input for the control period is less than its heat input for 1997 where the reduced utilization or shutdown has been replaced by another EGF permitted under Chapter 116, Subchapter I. This formula allows any surplus allowances not used by grandfathered EGFs and any surplus allowances not created by reduced utilization or shutdowns from electing EGFs to be banked or traded; (2) for electing EGFs if the heat

input for the control period was less than the heat input for 1997 and whose reduced utilization or shutdown has not been replaced by another EGF. The formula ensures that surplus allowances resulting from reduced utilization or shutdowns from these electing EGFs cannot be banked or transferred, as provided in TUC, §39.264(i)(3); and (3) for electing EGFs whose heat input for the control period was less than the heat input for 1997, whose reduced utilization or shutdown has been replaced by another EGF, and for EGFs not permitted under Chapter 116, Subchapter I. This formula allows surplus allowances to be banked or traded if they were generated from reduced utilization or shutdown and the EGF can document that the reduced utilization or shutdown has been replaced by another EGF. The requirements concerning the trading of allowances have been moved to a new §101.335.

The new §101.335, Allowance Banking and Trading, contains the general requirements for banking and trading of allowances. The requirements in this section are necessary to ensure consistency with TUC, §39.264(j). The new §101.335(a) specifies that allowances may only be used for the current or subsequent control period for which they were allocated. Any surplus allowances not used during a control period may be banked for use in subsequent control periods. Allowances may only be used within the same region. The new §101.335(b) specifies that allowances may be traded at any time during a control period by authorized account representatives. Notification of trades must be made to the commission within 30 days of the trade. The new §101.335(c) specifies that trades are prohibited prior to May 1, 2003. The new §101.335(d) specifies that traded allowances held in compliance accounts must have originated from EGFs in the same region, and the new §101.335(e) specifies that

allowances held in broker accounts may only be transferred to compliance accounts for EGFs located in the region where the allowances were originally allocated.

Section 39.264 allows EGFs the flexibility to decide when and where to make reductions or to add on controls. EGFs should consider local impacts of allowance trades specifically on those counties which are nonattainment and near-nonattainment. For example, most near-nonattainment areas have EGFs that are in close proximity to these areas. These EGFs emit significant amounts of NO_x, which has been shown to heavily influence local ozone levels. Other EGFs located a greater distance from these areas have regional impacts on background ozone levels, but do not impact near-nonattainment areas to the extent the closer facilities can.

While the commission believes that the trading program will result in emission reductions throughout the East Texas Region, emission reductions, rather than allowance trades, at the nearby EGFs should be thoroughly considered before investments are made for emission control equipment at more distant plants. In making these economic decisions, it is incumbent on businesses to weigh the environmental consequences of their actions. Prior to making an allowance trade to a nonattainment or near-nonattainment area, EGFs must be aware that such trades might jeopardize the status of a near-nonattainment area. For example, at this time the Tyler/Longview/Marshall area is operating under the terms of a flexible attainment region (FAR). If numerous trades occur into that area, the conditions of the FAR may be compromised. The FAR will expire in September 2001 and can be extended by the parties. During the term of the FAR agreement, EPA will treat the area under an approach similar to a maintenance plan area. However, EPA may designate the area as nonattainment, regardless of whether

a FAR agreement is in place. Designation of nonattainment could result in additional reductions of NO_x from EGFs in the Northeast Texas FAR area. Furthermore, a nonattainment designation would require additional reductions from industry sources and potential restrictions on trade into the new nonattainment area. The commission encourages EGFs to consider the long-term consequences of decisions to utilize allowances rather than the installation of controls at EGFs located close to nonattainment areas and in near-nonattainment areas.

The new §101.336 establishes compliance demonstration methods. All grandfathered and electing EGFs using the EBTA must comply with 30 TAC §116.914, Emissions Monitoring and Reporting Requirements. By June 30 of each year, grandfathered and electing EGFs participating in the EBTA shall report to the commission the amount of emissions of each allocated air contaminant during the preceding control period. The new §101.336(b) requires that at the end of each control period, the owner or operator of a grandfathered or electing EGF to report its emissions to balance the emissions with the allowances in its compliance account.

The new §101.337 will allow grandfathered or electing EGFs in the El Paso Region to meet emission allowances using credits from the City of Juarez, in the United States of Mexico and from EGFs located in Sunland Park, New Mexico. The reduction must be reviewed and approved by the executive director and must be surplus, permanent, quantifiable, enforceable by the commission, and not required by other rule or law. Under TUC, §39.264(q), §101.337 would also exempt the El Paso Region from the EBTA if either the EPA or the commission determines that reductions of NO_x will increase ambient levels of ozone. Currently, NO_x reductions are not required for facilities in the El Paso nonattainment area

because EPA has granted a waiver under FCAA, §182(f), concerning NO_x Requirements. Under this waiver, NO_x reductions are not required if the attainment demonstration for compliance with the ozone NAAQS can be made without a NO_x control strategy. The basis for this waiver does not satisfy TUC, §39.264(q) because it has not been demonstrated, under the §182(f) waiver or otherwise, that NO_x reductions would increase ambient ozone in El Paso County. The EGFs in the El Paso Region would still be required to obtain a permit under Chapter 116, Subchapter I regardless of the determination that NO_x reductions are counterproductive in controlling ambient ozone levels in the El Paso Region. The commission believes that this requirement is appropriate since TUC, §39.264(e) provides that EGFs without a permit may not operate after May 1, 2003, and TUC, §39.264(q) refers only to reduction requirements, not permitting requirements.

FINAL REGULATORY IMPACT ANALYSIS

The commission has reviewed the adopted rulemaking in light of the regulatory analysis requirements of Texas Government Code, §2001.0225, and has determined that the rulemaking is not subject to §2001.0225 because it does not meet the definition of a “major environmental rule” as defined in that statute. “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. Because the specific intent of the adoption is procedural in nature and specifies how and when emission allowances can be banked and traded; makes the trading and/or banking of emission allowances voluntary; and allows the EGFs the flexibility to decide the extent of banking and trading of allowances, the rulemaking does not

meet the definition of a "major environmental rule." The adopted sections only apply to grandfathered EGFs and electing EGFs. Finally, the adopted sections do not meet any of the four applicability requirements of a "major environmental rule." The adopted sections do not exceed a standard set by federal law, exceed an express requirement of state law, or exceed a requirement of a delegation agreement. In addition, the sections are adopted specifically to implement the requirements of TUC, §39.264.

TAKINGS IMPACT ASSESSMENT

The commission has prepared a takings impact analysis under Texas Government Code, §2007.043. The following is a summary of that analysis. While these amendments may result in capital costs for some EGFs, the amendments do not affect private property in a manner that restricts or limits an owner's right to the property that would otherwise exist in the absence of the governmental action. Consequently, this adoption does not meet the definition of a takings under Texas Government Code, §2007.002(5). These new sections implement the requirements of TUC, §39.264. EGFs are required to reduce emissions of NO_x by 50% and, if applicable, SO_2, by 25%. Although EGFs are required to make specific emission reductions, these facilities have alternatives available under the banking program that may allow the EGF to avoid installing add-on controls. Further, allowances can be transferred under the banking program so that EGFs have opportunities to buy and sell allowances in order to respond to business needs. This action is intended to reduce emissions of NO_x and SO_2. The action significantly advances this purpose by requiring substantial reductions in the emission of NO_x and SO_2 through a system of emission allowances. While requiring these reductions, these rules allow the trading of emission allowances so that EGFs may transfer allowances providing flexibility for

compliance with emission limits. This action is taken in response to a real and substantial threat to public health and safety and significantly advances the health and safety purpose and imposes no greater burden than is necessary to achieve the health and safety purpose.

COASTAL MANAGEMENT PROGRAM CONSISTENCY REVIEW

The commission has determined that this rulemaking relates to an action or actions subject to the Texas Coastal Management Program (CMP) in accordance with the Coastal Coordination Act of 1991, as amended (Texas Natural Resources Code, §§33.201 et seq.), and the commission's rules in 30 TAC Chapter 281, Subchapter B, concerning Consistency with Texas Coastal Management Program. As required by 31 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 has reviewed this action for consistency with the CMP goals and policies in accordance with the regulations of the Coastal Coordination Council. For the adopted sections relating to the authorization of emission allowances and the banking and trading of allowances, the commission has determined that the 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 that the commission protect air quality in coastal areas. This adoption is intended to reduce overall emissions of NO_x and SO_2 from EGFs. This action is consistent with 40 CFR because it does not authorize an emission rate in excess of that specified by federal requirements.

PUBLIC HEARINGS AND COMMENTERS

The commission conducted public hearings concerning this adoption in El Paso and Lubbock on October 1, 1999, in Austin on October 4, in Irving on October 5, in Houston on October 7, and in Beaumont on October 7.

The following commenters submitted written comments or provided testimony during the public comment period which closed on October 11, 1999: EPA - Acid Rain Division (EPA-ARD); EPA - Clean Air Markets Division (EPA-CAMD); EPA - Air Permits Division (EPA-APD); EPA - Air Planning Section (EPA-APS); University of Texas System, Office of General Counsel (UT); Enron, Central and South West Services, Inc. (CSW); TXU Business Services (TXU); Brazos Electric Power Cooperative, Inc. (Brazos); Baker & Botts, L.L.P. - Texas Industry Project (Baker & Botts); Clark & Seay, L.L.C. (Clark & Seay); Southwestern Public Service Company (SPS); Entergy Gulf States, Inc./Entergy Texas (Entergy); El Paso Electric Company (EPE); Lloyd, Gosselink, Blevins, Rochelle, Baldwin & Townsend, P.C. - City of Garland (Lloyd Gosselink); League of Women Voters of Texas (LWV-TX); The Center for Energy and Economic Development (CEED); Association of Electric Companies of Texas, Inc. (AECT); Reliant Energy (Reliant); Entergy Services Inc. (Entergy Services); Environmental Defense Fund (EDF); City of Austin/Austin Energy (AE); Sustainable Energy and Economic Development Coalition (SEED); Public Citizen, Texas Clean Water Action, and Texas Communities Project (PC); City Public Service of San Antonio (CPS); Sierra Club (Sierra); Bracewell & Patterson (B&P); Lubbock Power & Light & Water (LP&L); Clark, Thomas & Winters (CT&W); Central & South West Services, City of Austin, City Public Service, El Paso Electric, Entergy, Reliant Energy, Southwestern Public Service, and TXU (Group A); Mothers for Clean Air (MCA); Neighbors

for Neighbors (NFN); the Honorable Lon Burnam, State Representative, District 90; and 17 individuals.

ANALYSIS OF TESTIMONY

One individual commented that the commission should exercise its authority to require significant reductions at power plants in East Texas, while another individual added that the reductions should be permanent. Three individuals stated that the commission should enforce reduced emissions from grandfathered electric generating facilities, and two more individuals added that the commission should be as strict as possible in that enforcement.

While this adoption addresses grandfathered EGFs only, the commission is developing rules that will apply NO_x restrictions on all EGFs in the East Texas Region. The specific level of emissions required from these facilities will be determined on computer analysis that indicates what reductions should be required to assist the affected nonattainment areas in meeting the NAAQS. The net reductions required under this adoption are permanent. The commission will exercise its full enforcement power as authorized by statute, rule, or as governed by enforcement policy.

Four individuals stated that the commission should seek improvements that address SO_2, particularly to improve visibility in Big Bend. Another individual added that the commission must require a larger NO_x and SO_2 reduction to reduce acid rain and ozone in Texas nonattainment areas.

In cooperation with EPA and the National Park Service, the commission is analyzing the nature and location of required reductions to address reduced visibility in Big Bend National Park. This analysis is incomplete and therefore, the commission believes that requiring reductions specifically for their effect on the Big Bend area prior to the completion of this analysis is premature. The authority granted to the commission under TUC, §39.264 and other existing authority allows the commission to seek additional reductions in SO_2 as needed. As stated previously, the commission is addressing additional NO_x reductions that may be required to assist attainment of the NAAQS in a separate rulemaking. There are no areas in Texas that are nonattainment for SO_2, and the commission is not aware of any areas that are adversely affected by acid rain.

One individual stated that the commission should not allow a cap and trade or banking system because it avoids environmental justice issues and perpetuates emissions in low-income areas. The same individual suggested that the exclusion for individual units to be regulated under TUC, §39.264 be lowered to ten megawatts from 25 megawatts. This individual also stated that the commission estimate of cost of compliance with the requirements of the adoption is low, and it appears that the commission is allowing low-grade technology to be applied to the regulated units.

The trading and banking provisions of this adoption are required elements of the reduction program under TUC, §39.264. SB 7 provides that total annual emissions of NO_x from grandfathered EGFs will not exceed 50% of the NO_x emissions in 1997 as reported to the commission and that for coal-fired grandfathered EGFs, the total annual emissions of SO_2 will not exceed 75% of the emissions during 1997, as reported to the commission. SB 7 also provides that

the trades of allowances will only occur within the same region, either East Texas, West Texas, or El Paso. The effect of this will be an overall 50% reduction in NO_x and a 25% reduction in SO_2 within the region. SB 7 does not require a specific level of reduction at any individual grandfathered EGF. The exemption level for individual generating units of 25 megawatts is specified in TUC, §39.264(d). As discussed elsewhere in the adoption preamble, the commission has also excluded EGFs that generate power primarily for internal use, but that during 1997 sold one-third of their generated power or less than 219,000 megawatt-hours to the utility power distribution system. The commission believes that excluding these EGFs is consistent with SB 7 and will not negatively affect the overall emission reductions required by the program. Lowering the exemption to ten megawatts will require small generators to participate in the EBTA and permitting program and will achieve little environmental benefit in relation to the cost of compliance with the program. The commission has based its estimate of the cost of applying control technology to attain the 0.14 pounds/MMBtu on the February 1999 joint Public Utility Commission of Texas (PUCT) and TNRCC report, *Electric Restructuring and Air Quality: A Preliminary Analysis of Reductions and Costs of Nitrogen Oxides Controls from Electric Utility Boilers in Texas*. The estimate does not limit the amount EGFs must spend to meet the EBTA and accounts for technology of necessary sophistication to meet the requirements of this adoption.

The Honorable Lon Burnam, State Representative, District 90, commented concerning the implementation of SB 7 and its impact on consumers from an economic perspective. Mr. Burnam expressed his concerns that the commission implement the provisions of SB 7 free from the influence of

lobbyists. Mr. Burnam urged the commission to consider public health in the process of implementing SB 7.

The provisions of SB 7 concerning deregulation of the electric industry will be implemented by the PUCT. The commission conducted six hearings in order to seek the public comment of citizens, the regulated community, and environmental groups. The hearings were conducted in El Paso, Lubbock, Austin, Irving, Houston, and Beaumont. Prior to proposal, the commission held a stakeholder meeting to seek input from interested persons. Notice of this meeting was provided on the commission's web page. In addition, pre-proposal drafts of the rules were posted on the commissions's web page with a request for comments. The commission believes that the adopted rules are consistent with SB 7 and remains committed to implement the program in a fair and impartial manner. Since EGFs are being permitted under the requirements of TUC, §39.264, which does not require a health effects review, no review is included in this adoption. The commission believes that this program will reduce ambient levels of NO_x and SO_2 and improve the overall air quality of the state. These reductions will assist the commission in its efforts to attain the health-based NAAQS.

Clark & Seay and MCA commented that all power plants that are in or near an area with unsafe air should be required to meet the 0.14 pounds/MMBtu standard used in federal laws and to the level to which all grandfathered plants will be required to be cleaned up. In addition, LWV-TX commented that the rules in general should be expanded to require that all power plants in areas with unsafe air or that contribute to those nonattainment areas meet the same standard.

This adoption implements the requirements of TUC, §39.264 and application of this statute is limited to grandfathered EGFs and those EGFs that elect to participate in the permitting and trading program. The intent of SB 7 is not to achieve attainment with the NAAQS, but to permit and reduce emissions from grandfathered EGFs. While the implementation of SB 7 will provide emission reductions in areas near grandfathered EGFs, the commission recognizes that it will likely be necessary to adopt rules that will require air pollution control in attainment areas as well as additional rules for nonattainment areas. These controls would not only apply to emissions of NO_x from grandfathered EGFs, but permitted EGFs and other sources of NO_x as well. In addition, the commission will establish emission rates that it has determined are necessary to meet air quality standards. Rules implementing these additional controls are scheduled for proposal in late 1999 or early 2000. The commission is not aware of any federal standards that require EGFs to meet a NO_x emission restriction of 0.14 pounds/MMBtu.

EDF commented that TUC, §39.264(n)(1) includes two specific penalties for facilities that exceed their allowances. The commenters noted that the proposed rules did not include any administrative penalties, and recommended that they be added at a level sufficient to deter noncompliance. EDF recommended three times the current market value of allowances.

The commission does not typically address the amount of administrative penalties in specific rules. Rather, penalty amounts are established in accordance with the commission's penalty policy. All enforcement cases not referred to the Office of the Attorney General go through staff preparation of an administrative penalty recommendation in accordance with the commission's penalty policy.

Staff obtains an agreement or litigates to obtain an order against the respondent that requires the payment of penalties. The commission determines the amount of the penalty in accordance with the commission's enforcement rules and penalty guidance. The statutory language requires "enforcing an administrative penalty" and not "assessing" an administrative penalty.

Reliant requested that the published list of grandfathered EGFs should be revised by deleting the Cedar Bayou Units 1 and 2 (Account Number CI-0012-D) because the units are no longer grandfathered and are permitted under Permit Number 1532. In addition, Reliant provided heat input information for facilities that were missing from the proposed list. CPS commented that V.H.Unit 1 should be corrected from 2,946,936 MMBtu to 2,949,512 MMBtu, as was submitted to EPA in the Acid Rain Database.

The commission will make these corrections to the list entitled "Nitrogen Oxide and Sulfur Dioxide Allowances for Grandfathered Electric Generating Facilities" as requested.

EPE commented that the language in TUC, §39.102(c) and §39.264(i) illustrate EPE's exemption from Chapter 39 and EPE's ability to elect to designate a facility to become subject to §39.264, and the commenter noted that EPE is a "person" under TUC.

The commission agrees that EPE is a "person" under the TUC. The commission has not revised the rule to exempt EPE from the program requirements. TUC, Subchapter C, Retail Competition, §39.102, concerns retail customer choice, and exempts from TUC, Chapter 39, any

electric utility that has a system-wide freeze for residential and commercial customers that is in effect from September 1, 1997 and extends beyond December 31, 2001, that has been found by a regulatory authority to be in the public interest. Subchapter C also contains §39.264, which requires any EGF that existed on January 1, 1999, that is not subject to the requirement to obtain a permit under TCAA, §382.0518(g), to apply for and obtain a permit from the commission.

Section 39.264 was added to SB 7 during the final weeks of the 76th Legislative Session. Its very specific intent is to require grandfathered EGFs to obtain a permit from the commission and to obtain reductions of NO_x and SO_2 in the regions as defined by the bill. TUC, §39.264 contains several specific references to the El Paso area that make it clear that the Legislature intended EGFs in that area to be subject to the permitting and allowance program. TUC, §39.264(g) requires the commission to develop rules that define the "El Paso Region." TUC, §39.264(h) specifies an emission rate for the El Paso Region. TUC, §39.264(p) specifically requires the commission to develop rules to allow EGFs in the El Paso Region to meet emissions allowances by using credits from reductions made in Ciudad Juarez, United States of Mexico. Finally, TUC, §39.264(q) allows the commission to exempt EGFs in the El Paso Region if the commission determines that reductions in NO_x would result in an increased amount of ambient ozone levels in El Paso County.

The Code Construction Act, §311.021, Texas Government Code, provides that "In enacting a statute, it is presumed that: (1) compliance with the constitutions of this state and the United States is intended; (2) the entire statute is intended to be effective; (3) a just and reasonable result

is intended; (4) a result feasible of execution is intended; and (5) public interest is favored over any private interest." If TUC, §39.102 were read to exclude EGFs in the El Paso Region from the provisions of Chapter 39, the specific provisions of TUC, §39.264, concerning the El Paso Region, would be rendered ineffective. As prescribed by the Code Construction Act, the commission must interpret the provisions of Chapter 39 so that all sections can be given effect. To do otherwise would contravene the intent of the Legislature. Thus the commission agrees the EPE is exempt from the provisions regarding customer choice in TUC, Chapter 39. However, if EPE were exempted from the permitting and EBTA requirements, the provisions of TUC, §39.264, concerning the El Paso Region, would be meaningless. The commission agrees that EPE may use the provisions of §116.912, concerning Electing EGFs.

Lloyd Gosselink commented that the rules do not address the use of oil as a backup fuel at a gas-fired facility. The commenter stated that under certain curtailment situations, gas may not be available, and gas-fired facilities may be required to switch to oil as a fuel source, and that under these conditions, facilities should not be penalized for any additional NO_x emissions.

The commission believes that a facility has the latitude to use any fuel as long as actual emissions comply with its allotted allowances, and the use is authorized by the appropriate NSR authorization. The commission does not believe it is appropriate to revise the rules to include an exception to exceed allowances in the case of a curtailment, because SB 7 does not allow for this exception. If a curtailment occurs, and emissions of NO_x exceed an EGF's allowances, the commission will rely on its enforcement policy to determine the appropriate response. Use of

previously unused fuels may constitute a modification and require an NSR permit. The rules have not been revised in response to this comment.

LWV-TX commented that the TNRCC should restrict pollution trading in ways that assure significant reductions in air pollution.

SB 7 requires the commission to allocate allowances to grandfathered EGFs in defined regions of the state. The specific intent of SB 7 is that total annual emissions of NO_x from grandfathered EGFs will not exceed 50% of the NO_x emissions in 1997 as reported to the commission and that for coal-fired grandfathered EGFs, the total annual emissions of SO_2 will not exceed 75% of the emissions during 1997, as reported to the commission. The adopted rules provide the requirements for both the permitting of these grandfathered EGFs and an emission banking and trading program. Both of these programs are critical to the successful reduction of the NO_x and SO_2 emissions contemplated by SB 7. The EBTA contains restrictions on trading that will ensure that the regional emission reductions are enforceable. The commission believes the required reporting and monitoring, along with the statutorily defined enforcement provisions, will ensure that the program achieves the reductions intended by TUC, §39.264, and that no modification to the rule is necessary.

CEED commented that the preamble referenced adopting additional requirements for EGFs in nonattainment areas, indicating further reductions of 88% in DFW and 90% in HGA area. The commenter stated that the emissions inventory shows that these point sources only represent a minor

source of NO_x emissions, since the majority of emissions are generated by on-road and off-road mobile and area sources, and that the inclusion of these statements regarding the further need to reduce emissions from EGFs continues to focus attention on sources which will not solve nonattainment problems in these areas. CEED also commented that the proposal preamble statements that EGFs must consider local impacts of allowance transfers and that "EGFs emit significant amounts of NO_x, which has been shown to heavily influence local ozone levels" are comments without any qualifications to specific EGFs and perpetuate the opinion by some that all EGFs emit significant levels of emissions. CPS also disagrees with the cited statements from the proposal preamble. CPS commented further that the mandatory SB 7 program was designed to be flexible, and allow reductions to be made in the most cost-effective manner, adding that the utility plants in San Antonio, owned by CPS, do not contribute heavily to local ozone levels, as indicated by previous modeling performed by the Alamo Area Council of Governments (AACOG) under the direction of the TNRCC. The commenter stated that TNRCC's concern that SB 7 allowance trading will jeopardize the regional strategy is unwarranted, at least for the near-nonattainment area of San Antonio. CPS also supports the removal of all references to SIP requirements from the SB 7 regulations.

The reductions mandated by SB 7 only apply to grandfathered EGFs in the defined regions of Texas. These reductions from grandfathered EGFs will be significant; however, it is unlikely that the reductions will be sufficient to address the need to further reduce emissions in both attainment and nonattainment areas. The commission believes that to achieve attainment with the NAAQS, it will be necessary to reduce emissions from all sources, both stationary and mobile, in both attainment and nonattainment areas. The reductions that will be achieved under the adopted

rules will be significant towards reaching attainment. In addition, the commission believes that NO_x emissions from EGFs are not minor, but significantly contribute to ground-level ozone formation. The preamble comments regarding the potential impacts of trading on near-nonattainment areas were included to show the commission's recognition that emissions in near-nonattainment areas may have a negative effect on that area's ability to remain in attainment. Emission inventory information indicates that NO_x emissions from EGFs are approximately 47% of the stationary source NO_x emissions in the East Texas Region.

EPA-CAMD commented that in the proposed preamble, the cost-effectiveness numbers of $4,000 per ton of NO_x removed in the absence of emissions trading, or $2,000 per ton of NO_x removed with emissions trading, seem far too high. For example, in the May 25, 1999 Final Rule under §126 of the FCAA (64 FR 28300), EPA determined an average cost-effectiveness of $1,468 per ton of NO_x removed from electric generating units greater than 25 megawatts with emissions trading. Estimates for cost-effectiveness of NO_x control under the Ozone Transport Committee NO_x Budget Program range from $950-1,600 per ton. Furthermore, the commenter noted that some gas-fired units can achieve an average NO_x emission rate of 0.14 lb/MMBtu simply using combustion controls.

The commission supports the preamble language. The listed values were based on information developed for the joint Public Utility Commission of Texas (PUCT) and TNRCC report published in February 1999, entitled *Electric Restructuring and Air Quality: A Preliminary Analysis of Reductions and Costs of Nitrogen Oxides Controls From Electric Utility Boilers in Texas*. For simplicity in the report, the costs of emission reductions were analyzed on a unit-by-unit basis.

Thus, the potential for "over-compliance" for certain generating units in cases where it may be more cost-effective was not captured in the analysis. A subcommittee of the Ozone Transport Assessment Group (OTAG) has analyzed market-based emission trading options, such as the EBTA, estimating potential savings of as much as 50%, compared to the costs of unit-by-unit compliance. This analysis is applied to all utility generating units in the state, which may overstate the magnitude of the estimated compliance costs. The commission believes that, in practice, the costs of permitting and participation in the EBTA will be much less that what was estimated in the proposal.

EPA-APD commented on its understanding that the TNRCC will use the emission reductions which occur under these regulations to help demonstrate attainment and maintenance of NAAQS. The commenter further understood that the reductions will not be used for offsets and netting under NSR. With this understanding, EPA-APD supported the adoption of these regulations if the TNRCC adequately addresses the remaining comments.

The EBTA and electric generating facility permit (EGFP) programs will be submitted as a revision to the SIP. The resulting reductions will be used by the commission to further its attainment goals. Allowances cannot be used to satisfy emission offset requirements under federal NSR; thus, they will not be used as netting for PSD or for offsets under a nonattainment NSR permit.

PC recommended substituting renewable energy for electricity or energy used at a grandfathered facility, stating that this could provide a low-cost way to reduce emissions and result in the building of additional new clean energy sources. The commenter stated that concurrent rulemaking at the PUCT to implement the renewable portfolio standard in SB 7 has resulted in the development of capacity factors and other evaluation procedures that can be useful to the commission in converting renewable capacity to energy for purposes of calculating avoided emissions and providing for a periodic update for that factor. PC stated that these rules developed by the PUCT should be incorporated by reference into the commission's rules.

The purpose of this rulemaking is to obtain emissions reductions from EGFs based on the specific provisions of SB 7; in particular, the 50% NO_x reductions and the 25% SO_2 reductions, if applicable. These reductions are to be made based on certain emission rates set forth in TUC, §39.264(h). It is possible that a grandfathered or electing EGF could make reductions relying on the use of renewable energy and that the factors developed by the PUCT may be used to evaluate such a proposal. Since the commission can consider the rules of the PUCT among many sources of information to make such decisions, the commission does not believe it is necessary to incorporate the PUCT rules into Chapter 101 or Chapter 116. The commission agrees that using renewable energy to achieve emission reductions is a viable option and one that might result in cost savings to certain facilities. As the commission continues to develop the permitting and EBTA programs, issues concerning renewable energy can be considered. In addition, if a grandfathered or electing EGF substitutes renewable energy, the resulting emissions should be lower, requiring fewer allowances for compliance, thus creating an economic incentive.

PC believes that the proposed rules will fail to assure that emissions are actually reduced. PC believes that the utilities are unlikely to offer a reduction at any plant other than those that are oldest and used the least. Many of these plants are permitted as base-load plants which operate 60-80% of the time, but are kept only for peak use and are used infrequently, less than 20% of the year. Thus, a facility might be glad to modify its permit by reducing permitted emission that they would never really produce. PC recommends that the rules should be modified to require permit reductions based on the last five years of actual emissions.

The commission believes that the specified emission rates in the statute and the corresponding rules will achieve the target reductions. The intent of SB 7 is to achieve overall reductions of 50% NO_x emissions and 25% SO_2 emissions. An electing EGF would receive allowances equal to actual 1997 emissions, not permit allowable emissions, and would only be able to generate surplus allowances by reducing emissions below actual 1997 levels. Also, an electing EGF may not transfer or bank allowances that are conserved as a result of reduced utilization or shutdown unless the reduced utilization or shutdown results from the replacement of thermal energy from the electing EGF with thermal energy generated by any other EGF. Further, since SB 7 provides that 1997 is the base year for determining reductions, the commission does not believe it has the authority to require permit reductions based on the last five years of actual emissions. Therefore, the commission has not changed the rules in response to this comment.

PC commented that the rules adopted for the implementation of SB 7 should be structured in such a way as to allow the purchase and retirement of NO_x allowables issued under the SB 7 program to be used as

project emission reduction credits under SB 766. PC recommended two alternatives. First, the TNRCC could allow a retail electric provider (REP) to sell renewables to the owner of a grandfathered facility and assume that there will be a reduction in emissions per megawatt hour (MW) at the average rate of emissions per MW for the power plants in the area. The commenter stated that this is the least costly way to assure that the program will work, and since Texas is effectively an isolated electrical grid, will assure that emissions are reduced in the state. The EPA has recognized the Ozone Transport Assessment Group debates that add-on units that produce solar electricity or solar water heaters mitigate emissions. PC argued that a wind turbine, a solar water heater, or gases from landfills can similarly be rated based on capacity, converted into energy, and emissions reductions could thus be calculated. Secondly, TNRCC could allow the REP to buy and retire NO_x credits from the SB 7 trading program established in Chapter 101. This will assure that the emissions are actually reduced in the 60-county east Texas airshed, but it would add to the cost. The commenter further stated that since the transaction is on the open market, it may be far less costly than permit emission reductions purchased from the competitor; and the commission can significantly reduce the cost of the renewable energy used in the program by declaring that the renewable plants built to meet a contracted load under this program are pollution control devices as defined in Chapter 383 of the Health and Safety Code. If renewable energy installations are certified under Health and Safety Code, §383.004, the certification will exempt the owners from property taxes and allow them to qualify for pollution abatement bonds issued by local governmental units as provided by Health and Safety Code, §383.021. The combination of these two financial benefits could erase the premium price of renewable energy and make it the most cost-effective way to reduce emissions.

The commission will explore whether it has the authority to declare a renewable energy source, such as wind power, to be a pollution control device for the purposes of property tax exemptions and pollution abatement bonds. As the EBTA and permitting programs continue to develop, the commission can consider issues such as the use of add-on units that produce solar electricity or solar water heaters to reduce emissions. The commission agrees that REPs can buy and retire SB 7 allowances under Chapter 101 and that this transaction might be approved for use as a project emission reduction credit under the voluntary emission reduction permitting (VERP) program established by SB 766 as long as those allowances are not used to meet the requirements of SB 7.

One individual commented that electric utilities should be required to offer incentives to customers to replace inefficient appliances and light fixtures with cost-effective and energy saving equipment. The individual further commented that utilities should issue rebates to individuals and businesses that install renewable energy generating systems, and that utilities should be required to participate in any distributed generating project, public or private, that meets PUCT guidelines. Utilities should be required to pay a fair price for non-polluting power that they purchase from independent power producers. The commenter made several suggestions for how to increase competition among utilities, such as breaking up the distribution grid and making accessible to any qualified electric producer and having a large array of cogeneration industrial sites. The commenter urged the use of nonpolluting renewable electric energy.

These comments are beyond the scope of this rulemaking. Therefore, the commission has not made any changes in response to these comments.

One individual commented that gases from power companies could be used by oil companies to assist in the production of oil, and that these gases might not have to be reduced, they could be pumped into the ground. The commenter also noted that Russia has large gas fields and that gas could be used instead of coal.

These comments are beyond the scope of this rulemaking. Therefore, the commission has not made any changes in response to these comments.

One individual made several suggestions for how emissions could be reduced from utilities: school could be delayed to start after Labor Day when it is cooler; retail establishments could be closed on Sunday and Monday; the age for persons to obtain drivers license could be raised to take some cars off the road or persons without car insurance should be prohibited from driving; people should be required to buy insurance for six or 12-month periods; car inspection stations should be inspected to protect against fraud; busing of school children could be eliminated or the Dallas Area Rapid Transit buses should be used; teachers should be assigned to schools closest to their homes; the highways could be restructured to eliminate bottlenecks from four lanes when they merge into two or three lanes; cars from Mexico should be required to have a Texas inspection and insurance; limitations could be put on the use of fireplaces; IH-35 should be moved to the west and all trucks should be required to use IH-35 and the same for I-20; auto racing and drag racing strips should not allow the burning of fuels and car

manufacturers should be required to have overdrive transmissions that activate at 55 miles per hour; Texas needs to withdraw its bid for the Olympics to cut down on traffic and flights; and the federal government should increase highway funding to cut down on traffic congestion.

The comments raise issues that are beyond the scope of this rulemaking. Therefore, the commission has not made any changes in response to these comments.

EPA-APS commented that the allowance requirements of §§101.330-101.337 constitute a mass cap and trade program, and that existing guidance for discretionary economic incentive programs (EIPs) is found in 40 CFR Subpart U. The commenter stated that draft federal guidance for EIPs was published in the *Federal Register* on September 15, 1999, and that the 60-day public comment period ends on November 15, 1999. EPA stated that the proposed allowance allocation/trading program to meet SB 7 and the VERP program to meet SB 766 will be reviewed under EPA's existing guidance if applicable, and possibly under EPA's new guidance (if finalized before the state's SIP submittal).

TUC, §39.264 requires the commission to create a mass cap and trade system to distribute emission allowances for use by grandfathered and electing EGFs. TUC, §39.264(g) and (h) requires the commission to allocate allowances to grandfathered EGFs in defined regions of the state. The specific intent of SB 7 is that total annual emissions of NO_x from grandfathered EGFs will not exceed 50% of the NO_x emissions in 1997 as reported to the commission and that for coal-fired grandfathered EGFs, the total annual emissions of SO_2 will not exceed 75% of the emissions during 1997, as reported to the commission. The adopted rules provide the requirements for both

the permitting of these grandfathered EGFs, and an emission banking and trading program. These rules were proposed as a SIP revision to ensure that the reductions obtained from the program are federally enforceable and thus useful towards the reduction of criteria pollutant emissions necessary to assist nonattainment and near-nonattainment areas in meeting or continuing to meet the NAAQS. This program was designed to comply with the legislative mandate of SB 7 which in some ways is inconsistent with the requirements for discretionary EIPs. However, the commission anticipates adopting future SIP rules that will contain requirements that are more consistent with the EIP. The commission is committed to working with the EPA in its review and approval of the SB 7 program.

CPS commented that generally the proposed use and transfer of allowances is too restrictive and beyond the intent of SB 7. The commenter stated that the cap and trade program should be flexible and not have undue restrictions, which do not allow companies to make the necessary reductions in the most cost-effective and efficient manner.

Pre-proposal drafts of the EBTA contained several restrictions on trading to assist EGFs that are subject to 30 TAC Chapter 117 in meeting those SIP requirements. However, since the proposed rules eliminated the references to Chapter 117, the SIP-related restrictions were not proposed. The commission believes that the adopted rules provide flexibility for the successful implementation of the EBTA and the permitting program. The restrictions that are in the adopted rules are primarily requirements of TUC, §39.264, for example, the limitation on trading outside of the designated regions. Other restrictions, such as the monitoring provisions or the

reporting requirements, are intended to provide assurance that the mandated emission reductions are actually achieved. The commission does not believe that these minimum restrictions will inhibit free trading of allowances among EGFs.

EPA-ARD commented that the banking and trading system is too restrictive. EPA-ARD felt that greater freedom would result in greater flexibility and cost savings without undermining environmental goals. They recommended that the commission consider that allowances can be banked indefinitely; however, if banked emissions exceed 10% of capped emissions, then banked allowances must be used at a rate of two allowances per actual one ton emitted.

The rules have not been revised to make the suggested change in response to this comment. The proposed §101.335(b), now §101.335(a), provides that allowances not used for compliance may be banked for use in subsequent control periods. This program was designed to comply with the legislative mandate of SB 7 which in some ways is inconsistent with the requirements for discretionary EIPs. However, the commission anticipates adopting future SIP rules that will contain requirements that are more consistent with the EIP. The commission is committed to working with the EPA in its review and approval of the SB 7 program.

EPA-ARD commented that the definitions in §101.330 do not clearly define "electing" and "non-electing" EGFs and the relationship to "grandfathered" facilities. It commented that "grandfathered facility" is used without definition in Chapter 101.

The commission agrees, and has modified the definition of "Electric generating facility" in §101.330(14) to include the term "grandfathered." This modified definition now refers to electric generating facilities that are required to obtain an EGFP. The exemption in that definition has been moved to §101.331, Applicability. The commission has changed references to "grandfathered facilities" to "grandfathered EGFs." "Grandfathered facilities" is defined in Chapter 116. The definition of "nonelecting EGF" is not necessary, and it has been deleted. The rule was also revised to include a new definition of "electric generating facility" in §101.330(12) to be used for generic references to EGFs.

B&P commented that the definition of "Broker" in §101.330(4) should be revised because it is unnecessarily vague and recommended that a "Broker" be defined as "A person not required to participate in the requirements of this division who opens an account under this division for the sole purpose of banking and trading emissions allowances." B&P also recommended that the definition of "Broker account" be revised to read "The account where allowances held by a broker are recorded." The commenter also noted that conforming changes can be made to §101.331, if the suggested changes are made.

The proposed rule did not include a definition of "Broker" in §101.330(4); however, the commission agrees that a definition is appropriate and has included one in the adopted §101.330(4). Section 101.331(2) has been revised to reflect this new definition. The commission also agrees with the suggested change to the definition of "Broker account" in §101.330(5), but has retained the second sentence regarding the use of allowances held in a broker account.

B&P commented that the definition of "Compliance account" does not fully distinguish a "compliance account" from a "broker account." Therefore, the definition for "Compliance account" should be revised to "The account where allowances held by an EGF or multiple EGFs are recorded for the purposes of meeting the requirements of this Division and Chapter 116, Subchapter I of this title."

The commission agrees that the suggested language may clarify the rule and has revised the definition of "Compliance account" in §101.330(8) accordingly.

Baker & Botts commented that the definition of "Electric generating facility" should read as follows: "A facility that generates electric energy for compensation and is owned or operated by a person in this state, including a municipal corporation, or river authority. An EGF does not include a facility that generates electric energy for internal use and that during 1997 sold, to a utility power distribution system, less than one third of its potential electrical output capacity or less than 25 MW output, whichever is greater." Baker & Botts commented that this language more clearly eliminates those units that were not intended to be covered by SB 7, such as a 20 MW station that sells half of its generated electricity (10 MW). The commenter also stated that it is clearly not the intent of SB 7 to regulate this size/type of source. TXU commented that the definition of "Electric generating facility" in §116.18(8) excludes "a facility that generates electric energy primarily for internal use but that during 1997 sold to a utility power distribution system less than 1/3 of its potential electrical output capacity." TXU believes that if it were the Legislature's intent to exclude cogeneration facilities, language would have been included in the definition found in §39.264(2). In accordance with SB 7 any facility that generates electricity for compensation should be included in the definition.

The commission has not revised the rule in response to these comments. TUC, §39.264(a)(2) provides the definition of an "electric generating facility." The SB 7 definition, and the definition of EGF in §101.330 both contain the language concerning the generation of electricity for compensation. The commission believes that cogeneration facilities that sell less than one-third of potential electrical output capacity to the utility power distribution system are generating electricity primarily for internal use and that any electricity that is sold to the distribution system is surplus and not electric energy that was originally generated for compensation. The commission agrees that the definition of electric generating facility in SB 7 does not specifically exclude these cogeneration facilities from the requirements of SB 7, nor does it prohibit the commission from revising the definition to exclude certain EGFs based on the generation of electricity for compensation. The commission has also excluded EGFs that generate power primarily for internal use, but that during 1997 sold one-third of their generated power or less than 219,000 megawatt-hours to the utility power distribution system. The exemption was modified to also exclude EGFs that sold less than 219,000 megawatt hours to a utility power distribution system. This reference was added to exempt small cogenerators who may exceed the one-third limitation. The commission believes that excluding these EGFs is consistent with SB 7 and will not negatively affect the overall emission reductions required by the program. The commission believes that an exclusion based on these criteria is sufficient and is consistent with the EPA definition in 40 CFR §72.2.

AE questioned the reasoning of selecting May 1 - April 30 as the control period in §101.330(6). AE felt that this will lead to difficulties associated with the calendar year being used for emissions

inventories, and recommended development of a plan that transitions the control period to one that matches the calendar year.

The rule has not been revised in response to this comment; however, the definition of "Control period" is now in §101.330(9). TUC, §39.264(c) provides "for the 12-month period beginning on May 1, 2003, and for the 12-month period after the end of that period, total annual emissions of nitrogen oxides from facilities subject to this section may not exceed levels equal to 50% of the total emissions of that pollutant during 1997, as reported to the conservation commission, and total annual emissions of sulfur dioxides from coal-fired facilities subject to this section may not exceed levels equal to 75% of the total emissions of that pollutant during 1997, as reported to the conservation commission. The limitations prescribed by this subsection may be met through an emissions allocation and allowance transfer system described by this section." Because §39.264(c) specifically defines the period of time to be used as the control period, the commission does not believe it is appropriate to use any different control period. The rule has not been revised in response to this comment.

B&P commented that §101.330(9) does not clearly define EGFs that are physically located in Texas. The commenter stated that the definition, although consistent with TUC §39.264(a)(2), appears to encompass facilities not located in Texas so long as they are owned by a person in Texas, and that the rules should only apply to facilities that are physically located in Texas. The current definition only states "EGFs owned or operated by persons in this state." UT commented that §101.330(9) should further define "person," since this term is used in TUC, §39.264 as "individual, partnership, a

partnership of two or more persons having a joint or common interest, a mutual or cooperative association, and a corporation, but does not include an electric cooperative." UT also commented that the definition of "person" does not include state institutions of higher education.

The commission has not revised the rule in response to the comment from B&P. Therefore, it is not necessary to clarify that the rules only apply to EGFs that are physically located within Texas. However, if the commission were to include such a limitation, it might prohibit the commission from defining the "El Paso Region" as being consistent with the La Paz Agreement. The La Paz Agreement designated the Paso del Norte Air Shed as the contiguous air shed basin between El Paso, Texas, Sunland Park, New Mexico, and Ciudad Juarez, Chihuahua. The La Paz Agreement does not extend the commission's jurisdiction into the State of New Mexico. Elsewhere in this response to comments, the commission states its intent for revising the definition of "El Paso Region" to be consistent with the Paso del Norte Air Shed. If the commission were to limit participation in the EBTA to only those EGFs that are physically located in Texas, then it is unlikely, in spite of the La Paz Agreement, that the El Paso Energy facility in Sunland Park, New Mexico could obtain allowances.

The commission agrees that it is appropriate to use the definition of "person" in TUC, §11.003(14) and has included a new definition in §101.330(17) and §116.18(12). This definition will apply for purposes of initial issuance of EGFPs and for the allocation of allowances. By using this definition, the commission can ensure that it will not inadvertently require additional facilities

to comply with the program, since the definition of "person" in TCAA, §382.003(10) is more inclusive than the TUC definition.

B&P commented that §101.330(12), now §101.330(16), should define "NO_x allowance" consistently with the proposed definition of "SO_2 allowance," which states that an SO_2 allowance is valid only for the purposes of meeting the requirements of this division and Chapter 116, Subchapter I.

The commission agrees, and has revised the definition of "NO_x allowance" to be consistent with the definition of "SO_2 allowance."

Enron requested that §101.332(f) be revised to provide that neither a NO_x allowance nor an SO_2 allowance constitutes a security or property right, but that they may be used as collateral or security for indebtness.

The commission has not revised the rule in response to this comment. The commission believes that the use of allowances as collateral or to secure a debt is a matter best left to the owner of the allowances and the party with whom the owner is dealing. Since allowances can be reduced, such as when emissions exceed the allowances in any control period, to account for load shifting, or to invalidate allowances that were used by electing EGFs to meet SIP requirements, it is likely that this sort of provision would conflict with this statutorily based enforcement authority. Nothing in the adopted rule or TUC, §39.264 prohibits the use of allowances for collateral or security for

indebtedness; however, the commission does not believe that adding this language to the rule is appropriate.

CPS commented that §101.332 restricts the use of allowances for use only in the EBTA and prohibits the use of allowances for netting, offsets, or other credits. The commenter stated that it is unclear why these NO_x allowances created for EBTA cannot be used for other trading programs, and that it seems that allowances created for use by utilities and used only within the utility sector could be traded for any program designed to reduce NO_x from that sector. CPS further commented that for example, trading should be allowed for future utility offsets if they are not needed for the EBTA program, since the NO_x reductions are still reducing overall NO_x from the same utility sector.

The commission has not revised the rule in response to this comment. TUC, §39.264 contains several restrictions on the use of allowances. TUC, §39.264(j) provides that EGFs may only trade allowances with other EGFs in the same region. TUC §39.264(l) provides that an EGF may not trade an unused allowance for a particular air contaminant, for use as a credit for another air contaminant. TUC, §39.264(i) limits the use of allowances for electing EGFs. The pre-proposal draft of these rules did provide flexibility to EGFs that would also be subject to Chapter 117 SIP requirements; however, the proposal eliminated any links to Chapter 117. The general concern was that the limitations necessary to ensure that the allowances could be used for SIP purposes made the EBTA unwieldy and overly restrictive. Further, there are additional federal requirements that must be met in order for allowances to be used for netting or offsets. In order to ensure that the EBTA is implemented consistently with the requirements of TUC, §39.264, the

adopted rule contains the minimum restrictions on trading. In the near future, the commission will be proposing additional SIP reductions that will impact EGFs and other sources in the affected areas. If it is appropriate, a trading program could be developed for facilities affected by those rules or the EBTA could be modified to accommodate EGFs that are affected by the SIP rules at that time.

B&P commented that §101.332(a) states that allowances are valid only for meeting the requirements of "this division" and cannot be used to meet the limitations of a permit or applicable rule. However, the proposed definition of "SO_2 allowance" states that allowances can be used to meet the requirements of Chapter 116, Subchapter I. The commenter stated that §101.332(a) should be revised to reflect that allowances are valid for meeting the requirements of Chapter 116, Subchapter I.

The commission agrees with the suggested change and has corrected §101.332(a).

CSW, TXU, Entergy, AECT, CT&W, Group A, Entergy Services, and CPS recommended that §101.332(b) be revised to provide a 30-day period after the end of each control period for owners/operators of EGFs to reconcile the allowance accounts, by changing May 1 to June 1. Reliant requested a 60-day period and suggested that the rule be revised to extend the period to June 30. CSW and TXU also requested language clarifying that this section should only apply to EGFs that are subject to this division. SPS commented that the proposed language was not clear, consistent, or reasonable relating to reconciliation periods. SPS proposed that 60 days (consistent with Acid Rain Program)

would be acceptable for emission data to be quality assured and for transfer transactions to be completed if necessary.

The commission agrees that 30 days for EGFs to reconcile its allowance account is appropriate and §101.332(b) has been revised. The commission reminds EGFs that if additional allowances are necessary but unavailable, the EGF will be out of compliance with the requirements of the EBTA in the EGFP. EGFs now have until June 1 after every control period to sell or purchase allowances in order to reconcile the amount of allowances in their compliance account to ensure that the number of allowances in their account are equal to, or exceed, the amount of emissions from the prior control period.

Reliant commented that §101.332(c) should be revised to allow the creation of discreet emission reduction credits (DERC) for those facilities that have early implementation of reductions required under the EBTA program.

The commission agrees that early reductions that meet the requirements of §101.29 could be banked as DERCs. Section 101.332(c) does not eliminate this possibility.

EPA-APS noted that §101.332(c) states that emissions reductions used to satisfy the requirements of the EBTA cannot be used to generate emission reduction credits (ERC) or DERCs. EPA-APS commented that since allowances may be banked and traded annually, it would clarify the intent of this section to state that any emission control equipment installed or other measures undertaken to not exceed the

allowances in the compliance account cannot be used for ERCs or DERCs under TNRCC's emissions banking and trading program found in §101.29 or other banking/trading programs such as Chapter 117.

The commission has not revised the rule in response to this comment. The commission agrees that reductions cannot be used to meet the requirements of SB 7 and also be banked as DERCs or ERCs because the reductions cannot be counted twice. The commission will allow for reductions that are surplus to either be banked as allowances or DERCs or ERCs, as long as the reduction meets the requirements of §101.29, Emission Credit Banking and Trading.

EPA-ARD asked whether "the emission reduction credits or discrete emissions reductions credits are related to a particular rule such as Chapter 117, Subchapter B, Division 2."

The DERCs and ERCs are related to a variety of rules, such as 30 TAC Chapter 115, Control of Air Pollution from Volatile Organic Compounds, and Chapter 117, Control of Air Pollution from Nitrogen Compounds. Section 101.29 provides a complete listing of uses for ERCs and DERCs.

EPA-ARD commented that §101.332(h) mentions two cases where there would be one compliance account. It suggested that language may be needed to address situations where there are multiple EGFs at the same property, but not under common ownership and control.

The commission agrees with the comment and has revised the definition of "Compliance account" in §101.330(8) to clarify that EGFs not under common ownership or control may have separate compliance accounts.

Lloyd Gosselink commented under §101.332(h) that facilities with multiple EGFs should be allowed to have multiple compliance accounts, and that having one compliance account will present practical problems because different EGFs may be under different regulatory requirements. For example, permitted EGFs are currently required to report on an annual basis on January 1 of each year; however, grandfathered EGFs are required to report on an annual basis ending on May 1 of each year. The commenter stated that subsection (h) should be deleted because of these problems.

The commission believes that assigning one compliance account for multiple EGFs under common ownership or control will properly structure the allotment and tracking of allowances. The reporting requirements for the control periods for electing EGFs and grandfathered EGFs are the same. Any reporting requirements under Chapter 116, Subchapter B for electing EGFs are based on a calendar year and are not associated with the reporting requirements for the EBTA and Chapter 116, Subchapter I.

EPA-ARD commented that §101.332(i), while appropriate, may not be sufficient to spur sources to comply. EPA-ARD asked whether other penalty provisions apply.

The commission has not revised the rule in response to this comment; however, the commission has moved §101.332(i) to §101.333(4) for clarity. Section 101.330(i) is based on TUC, §39.264(n)(2) and authorizes the commission to reduce allowances for the next control period for an EGF that emits an air contaminant in excess of the EGF's allowances. In addition to that provision, subsection (n) provides that the commission may enforce administrative penalties in an amount determined by the commission for each ton of emissions by which the EGF exceeds its allowances. TUC, §39.264(o) states that the commission can penalize an EGF that exceeds its allowances by ordering the EGF to shut down or to take other enforcement action as provided by commission rules. The commission believes that these provisions are sufficient to ensure compliance with the EGFPs and the EBTA.

SPS and Entergy commented that the database used to obtain heat input values for calculation of NO_x allowances should reflect actual measurement of fuel combusted and added that the EPA Acid Rain Database contains values that are generally related to actual fuel consumption. SPS, Entergy, Group A, and CPS commented that the same database should be applied to both grandfathered and electing facilities. CT&W commented that the proposed method for calculating emission allowances using EPA's Acid Rain Database in §101.333 is the most accurate, and suggested that the commission make use of it for all allowance calculations. CSW, Reliant, Brazos Electric, Entergy Services, and AECT suggested that §101.333(2) be revised to specify that the amount of allowances allocated to electing EGFs will be equal to the actual emissions in tons in the 1997 EPA Acid Rain Database, provided that the number of tons do not exceed the allowable emissions in NSR permit for that electing EGF or the maximum annual emissions under any applicable state or federal requirement. CSW and Reliant

commented that this request is intended to make the calculation of allowances on a consistent basis for all EGFs.

TUC, §39.264(h) specifies the formula to be used for the calculation of allowances for grandfathered EGFs. That section also specifies emission rates to be met within each region. As stated in the proposal preamble, the 1997 Emissions Scorecard from EPA's Acid Rain Program is the basis of the emission rates specified in TUC, §39.264(h) for grandfathered EGFs. These emission rates are necessary to achieve the required 50% reductions in NO_x and 25% reductions in SO_2. The commission agrees that it would be appropriate to use the EPA Acid Rain Program Database as the basis for calculating allowances for electing EGFs and has revised §101.333(2) to include a reference to the 1997 Emissions Scorecard from EPA's Acid Rain Program.

Reliant commented that §101.333(1) should be clarified to state that "ER = emissions rate, as defined in subparagraphs (C) or (D) of this paragraph." Lloyd Gosselink commented that there are problems with the sentence structure of §101.333(1). A conjunction "or" follows the end of subparagraph (A), but not subparagraph (B). Also, the equation formula legend includes a reference to a subparagraph (E), which was not proposed. EPA-APS also commented that §101.333(E) does not exist and requested clarification by either adding the omitted paragraph (E) or changing the definition of ER as the emission rate defined in subparagraph (C) or (D). EPA-ARD commented that in §101.333(1)(E), emission rates referenced in Chapter 117 should be more specific.

The commission agrees that the proposed §101.333(1) contained typographical errors and an erroneous reference to a nonexisting subparagraph (E), and has revised the rule so that it has the appropriate conjunctions, numbering, and lettering. These changes are not substantive and have not changed the meaning of the section.

EPA-ARD commented that it is not clear in §101.333(1) which sources receive allocations under the first equation and asked if it would be used for grandfathered facilities. EPA-ARD also questioned whether the limits in §101.333(2) limit the allocation in 101.333(1).

The commission has revised the rule to clarify that grandfathered EGFs are the facilities that are given allowances under §101.333(1). The limits in §101.333(2) are applicable only to electing EGFs to ensure that emission reductions used for the EBTA are real and non-surplus.

EPA-ARD commented that §101.333(1)(A) and (B) is ambiguous when it refers to "Acid rain database." EPA-ARD suggested that it would be clearer if the language specified "1997 Emissions Scorecard from EPA's Acid Rain Program."

The commission agrees, and has revised the rule to refer to the "1997 Emissions Scorecard from EPA's Acid Rain Program." The proposed §101.333(1)(A) and (B) have been deleted, and the specification for the acid rain database is now in the formula in §101.333(1) for heat input.

EPA-ARD commented in §101.333(1)(C)(ii) that it is unclear if the 1.38 lb/mm BTU limit for SO_2 applies to all EGFs, or only coal-fired sources.

The commission agrees that this section was unclear and has revised §101.333(1)(C)(iii), now §101.333(1)(A)(ii), to clarify that the 1.38 lb/mm BTU limit for SO_2 applies to only coal-fired grandfathered EGFs.

EPA-ARD commented in §101.333(1)(D) that clarification is needed for the emission rate used for SO_2.

The commission has made no changes in response to this comment; however, §101.333(1)(D) has been moved to §101.333(1)(B) for clarity. TUC, §39.264 did not specify an SO_2 emission rate for grandfathered EGFs in the West Texas or the El Paso Region, because there are no coal-fired grandfathered EGFs in these regions.

AE and Lloyd Gosselink commented that there should be an alternative means for determining NO_x/SO_2 allowance allocations if the applicant can demonstrate that the base year (1997) was an abnormal year for system operation. AE offered a possible alternative scenario: if the applicant could demonstrate that the standard allocation, based on 1997 process values, was more than 20% less than the average of the three-year period of 1996 to 1998 inclusive, the average of these three years would be the base allocation for that unit. Lloyd Gosselink proposed that the final rules include a component, for example, the facility's capacity factor for the year, to take into account actual operating hours during the 1997 base year. The commenter stated that this component will allow the TNRCC and the operator

to extrapolate an annual emission rate based on the actual emissions level and the actual operating hours for the facility during 1997. Lloyd Gosselink proposed the following revision to §101.333(1)(A): "HI = total heat input (million British thermal units (MMBtu)) during 1997, determine by subparagraphs (a) or (b) of this paragraph which may be adjusted to an annualized figure to account for unit outages and load growth." LP&L commented that the use of maximum capacity during the past five years of emissions data would allow for more competitive flexibility while still meeting the intended emissions reduction goal, and that by using one year of emissions data (1997) the Legislature did not consider important aspects, such as load swing (when a utility can purchase electricity cheaper than it can produce it). The commenter stated that every generation source that did not produce or had fewer production hours in 1997 will have its operational ability restrained with a reduction in its ability to compete in a deregulated market. LP&L also acknowledged that the requirement to base allowances on one year of heat input data is a basic part of the legislation, and that the commission is bound by this requirement.

The commission has made no changes in response to these comments. TUC, §39.264(h) specifies that the commission shall allocate allowances based on a facility's total heat input in terms of MMBtu during 1997. The commission believes that the provisions of TUC, §39.264(h) do not provide the commission with the discretion to create a different formula or emission rates for the purpose of meeting the mandated reductions of 50% for NO_x and 25% for SO_2.

Lloyd Gosselink commented that §101.333(1)(A) conflicts with the Electric Reliability Council of Texas (ERCOT) designation of Garland's utilities as "must run" facilities. This designation requires

Garland's units to operate near capacity during the summer months in order to provide adequate and reliable electricity. The commenter stated that based on the proposed language, Garland may be forced to reduce electric generation in order to meet emission reduction mandates, possibly causing brownouts during the summer months.

The commission has made no changes in response to this comment. ERCOT-designated "must run" grandfathered EGFs are not among the exemptions from the requirements to operate in compliance with the EBTA as prescribed by TUC, §39.264. The commission does not believe that TUC, §39.264 requires reductions in electric generation, since each grandfathered EGF has the option of complying with SB 7 emission reduction requirements by installing emission controls, acquiring additional allowances, or reducing electric generation. Further, electing EGFs that are designated as "must run" facilities are not required to participate in the EBTA.

CSW, Entergy, AE, CEED, Entergy Services, Group A, AECT, and CPS commented that §101.333(2) should allow the owner/operator of electing EGFs to decide whether allowance(s) should be allocated for NO_x, SO_2, or both. By mandating that an electing EGF obtain allowances for both NO_x and SO_2, AE felt that participation will be severely limited. CPS commented that mandating electing facilities to obtain allowances for both NO_x and SO_2, will limit, rather than broaden, the range of cost-effective alternatives available to utilities to achieve the requirements of TUC, §39.264; and have no effect on achieving compliance with the emissions limitations prescribed by TUC, §39.264(c). CPS commented that it is not the intent of SB 7 to require additional limitations or reductions on emissions from permitted facilities.

The commission has not revised the rule in response to this comment. The commission believes that the language in TUC, §39.264(i) requires electing EGFs to be given allowances for both NO_x and if applicable, SO_2. TUC, §39.264(i) provides that "a person, municipal corporation, electric cooperative or river authority that is not covered by this section may elect to designate that facility to become subject to the requirements of this section and to receive emissions allowances for the purpose of complying with the emissions limitations prescribed by Subsection (c)." TUC, §39.264(i) refers to the emission limitations in TUC, §39.264(c). TUC, §39.264(c) provides "for the 12-month period beginning on May 1, 2003, and for the 12-month period after the end of that period, total annual emissions of nitrogen oxides from facilities subject to this section may not exceed levels equal to 50% of the total emissions of that pollutant during 1997, as reported to the conservation commission, and total annual emissions of sulphur dioxides from coal-fired facilities subject to this section may not exceed levels equal to 75% of the total emissions of that pollutant during 1997, as reported to the conservation commission. The limitations prescribed by this subsection may be met through an emissions allocation and allowance transfer system described by this section." TUC, §39.264(c) also refers to "facilities subject to this section." The phrase "this section" in TUC, §39.264(i) refers to TUC, §39.264 in its entirety and not to the specific requirements of subsection (i). Thus, if an owner or operator elects to designate an EGF to "become subject to the requirements of this section and to receive emissions allowances for the purpose of complying with the emissions limitations prescribed by Subsection (c)," the electing EGF is now subject to all of the applicable requirements of TUC, §39.264, including the requirements of TUC, §39.264(c). Since TUC, §39.264(c) requires specific reductions of NO_x and SO_2, electing EGFs will be given allowances consistent with the requirements of TUC, §39.264(i)

for the purpose of meeting the emission reductions required by TUC, §39.264(c). Because the commission believes that the language in TUC, §39.264(i) requires electing EGFs to be given allowances for both NO_x and if applicable, SO_2, the adopted rule has not been revised in response to the comments.

EPA-APS commented that §101.333(2)(C) should be revised to state that the amount of allowances for electing EGFs shall not exceed an applicable state or federal requirement. The commenter stated that a federal requirement may include, but not be limited to, reasonably available control technology (RACT) and/or reductions from sources in an ozone nonattainment area or any or all portions of the Texas Clean Air Strategy area contained in an emissions inventory utilized in an attainment demonstration which has been submitted to the EPA for approval as part of a SIP.

The commission agrees that the amount of allowances for electing EGFs may not exceed applicable state and federal requirements. The commission believes that the proposed language in §101.333(2)(c) addressed this issue. The adopted rule has not been revised in response to this comment; however, §101.333(2)(C) is now in §101.333(2)(B). Nothing in §39.264 limits the allowances for electing EGFs to ozone nonattainment area or any or all portions of the Texas Clean Air Strategy area contained in an emissions inventory utilized in an attainment demonstration which has been submitted to the EPA for approval as part of a SIP. Therefore, the commission does not believe that revising the rule to include these limitations is necessary.

EPA-APS commented that a new §101.333(2)(D) should be added to state that for electing EGFs located in ozone nonattainment areas, the amount of allowances shall not exceed the 1990 emissions inventory or the emissions reported in any Rate-of-Progress SIP submitted for the ozone nonattainment area, or the emissions based on limitations established by regulations in the attainment demonstration SIP.

The commission has not revised the rule in response to this comment. TUC, §39.264(i)(2) provides that allowances for electing EGFs shall be allocated in an amount equal to each facility's actual emissions in tons in 1997. TUC, §39.264(i)(4) allows emission reductions from electing EGFs to be used to satisfy emission reductions for grandfathered EGFs to the extent that reductions used to meet TUC, §39.264(c) are beyond the requirements of any other state or federal standard, or both. However, nothing in §39.264 limits the allowances for electing EGFs to 1990 emissions inventory or the emissions reported in any Rate-of-Progress SIP submitted for the ozone nonattainment area. Therefore, the commission does not believe that revising the rule to include these limitations is necessary.

CSW, Reliant, TXU, Entergy, Entergy Services, Group A, AECT, and CPS requested that §101.333(3) be deleted. CSW, TXU, AECT, and Entergy also requested that the statement in the preamble that future rulemakings addressing future ozone SIP reductions will reduce the allowances allocated under SB 7 be deleted. CSW and Reliant commented that these allowable reductions are contrary to the intent of §39.264 of SB 7, are unwieldy, and are unfair to grandfathered facilities. CSW and Reliant also commented that the allowance allocation and trading provisions in SB 7 are a

limited-purpose mechanism for implementing a cap and trade program to allow flexibility in achieving regional reductions of NO_x and SO_2, and not an all-purpose system for limiting emissions for grandfathered and electing EGFs. CSW and Reliant commented that the SB 7 allowance system should remain distinct from the ozone SIP and any other applicable requirement. Brazos Electric suggested substitute wording that would track the language of TUC, §39.264(s): "This section does not limit the authority of the conservation commission to require further reductions of nitrogen oxides, sulphur dioxides, or any other pollutant from generating facilities subject to this section or Section 39.263."

The commission has deleted the proposed §101.333(3) because the proposed rule did not provide for allowing facilities subject to Chapter 117 to use the EBTA program. The adopted §101.333(3) implements §39.264(i)(4) to prevent double counting of emissions reductions by allowing the commission to invalidate allowances, authorizing emissions in excess of applicable state or federal requirements that are allocated to an electing EGF. This is necessary to account for state and federal regulations that became effective during the prior control period and for regulations that specify emission rates instead of an emission cap. The commission has revised the adopted preamble to reflect the fact that the trading program for future ozone SIP requirements has not yet been developed. The proposed rule did not include limitations that would be necessary to allow the EBTA to be used as a SIP trading program. The commission believes the adopted rule is consistent with the requirements of §39.264.

EDF commented that §101.333(4)(B) requires the TNRCC to allocate allowances annually, but that TUC, §39.264(h) implies that the intent was to allocate allowances only once no later than January 1,

2000. EDF believes that allocating allowances every year is labor-intensive and unnecessary, since the allocation will always be based on 1997 values, regardless if allocated once or every year. EPA-ARD commented that §101.333(4)(C) is unclear on whether the allowance allocations are permanent, and recommended allocating allowances for a few years at a time to allow EGFs to plan for compliance.

The commission agrees that allowances should be allocated only one time and has revised §101.333(5)(C) to state that allowances for a grandfathered or electing EGF shall be the same as their initial allocations and that compliance accounts will be automatically updated at the beginning of each control period. However, §101.333(6) provides that after the annual update to the compliance accounts, the number of allowances may be adjusted after the commission reviews the final trading reports required by §101.336. The commission must be able to adjust allowances in order to implement certain provisions of TUC, §39.264. For example, §101.332(i), which is based on TUC, §39.264(n), provides that the penalty for exceeding allowances allocated in a prior control period is to reduce allowances for the next control period in an amount equal to the emissions exceeding the allowances in the compliance account. Other examples include a facility that volunteers to permanently reduce the number of annual allowances allotted to its compliance account in order to generate DERCs or ERCs, allowances for electing EGFs that are reduced to comply with other state and federal regulations, and allowances that are reduced for electing EGFs that reduce utilization or shut down.

CSW commented that §101.333(4)(C) should be revised to require the TNRCC to allocate allowances for electing EGFs through rulemaking rather than orders.

The commission has made no changes in response to this comment. TUC, §39.264(f) requires the commission to develop rules to provide for the allocation of allowances. It does not require the specific allowances for each affected EGF to be stipulated in the rules. The commission believes that it is sufficient to establish in the rule the procedure by which allowances will be allocated. Additionally, the commission's using an order to allocate allowances will provide a less resource-intensive method to allocate or revise as necessary allowances for affected EGFs.

TXU, Lloyd Gosselink, and CEED commented that §101.333(5) should be revised to eliminate the requirement that the registry include the price paid per allowance. Omitting the price paid for allowance is consistent with the EPA Acid Rain Program, and including the price on the registry could actually inhibit trading.

The commission has made no changes in response to this comment. The commission believes that including the price paid per allowance in the registry will improve trading and selling of allowances by providing an open and competitive market system. Providing as much information as possible in the registry will allow participants in the EBTA to make informed transactions. For organizational clarity, §101.333(5) has been renumbered to §101.333(7).

CPS commented that SB 7 language states that electing EGFs cannot transfer allowances created by "reduced utilization or shutdown." CPS believes that this language was included to prevent companies from reducing their power output to produce excess allowances. The commenter stated that the formulas provided in §101.334 are overly complicated and do not seem to accomplish this purpose.

The commenter further stated that the formulas include emission factors instead of just restricting the basis to utilization, and they do not account for generation that results from the replacement of thermal energy from other units as allowed in SB 7. CPS believes that the formulas should be deleted and each utility should be handled on a case-by-case basis, because each utility has unique circumstances under which it will replace lost energy. CSW, Entergy Services, and AECT commented that §101.334(e)(2) and §101.335(a) need to include the exception language from TUC, §39.264(i)(3). CSW commented that the formulas and remaining language in §101.334(e) conflict with §39.264(I)(3) and that §101.334(e) must be revised. TXU commented that SB 7 does not prohibit trading of allowances caused from reduced utilization or shutdown, but proposed that §101.334 and §101.335 have tighter restrictions. TXU recommended that §101.334 and §101.335 be revised to allow transfers and banking of allowances resulting from reduced utilization or shutdowns as long as the reduced utilization or shutdown results from the replacement of thermal energy from the electing EGF with thermal energy generated by any other EGF. Entergy, Group A, and CPS commented that the use and transfer of allowances should be in accordance with the requirements and language of SB 7 and should be no more restrictive than provided by law. EPA-APS commented that the term "reduced utilization" in §101.334(e) is not clearly defined. The commenter stated that for some, it may mean having less heat input to the emissions unit than in 1997, and for others, it may mean generating less electricity at the emission unit than in 1997. Still for others, it may mean operating for fewer hours during the year than in 1997. Others may consider that operating at a reduced load factor (say at 75% for the year compared to 85% in 1997) is reduced utilization. EPA-APS recommended including a definition of "Reduced utilization" in §101.330, or revising §101.334(e) to state that allowances at electing EGFs that result from reduced utilization, which means an emission unit operating for fewer hours during the

control period than it did in 1997 (or other appropriate meaning) or shutdowns, are ineligible for transfer.

TUC, §39.264(i)(3) specifies that an electing EGF may not transfer or bank allowances conserved as a result of reduced utilization or shutdown, unless the reduced utilization or shutdown results from the replacement of thermal energy from the electing EGF with thermal energy generated by any other EGF. The equations in the proposed §101.334(e) were to be used to calculate the number of the annual allowances allocated to an electing EGF that would be eligible for trading or banking. The commission agrees that these equations did not completely address the intent of SB 7 with regard to reduced utilization or shutdown of electing EGFs. Accordingly, the equations have been revised in the adopted §101.334(1), (2), and (3) to allow the calculation of the number of allowances that will be deducted from an EGF's compliance account for emissions that occurred during each control period.

The equation in §101.334(1) will be used for all grandfathered EGFs, and for electing EGFs with equal or increased utilization (i.e., the heat input for the control period equaled or exceeded the heat input for 1997). In this case, the number of allowances deducted from the compliance account will equal the number of tons of actual emissions during the control period.

The equations in §101.334(2) and (3) will be used for electing EGFs with reduced utilization for the control period (i.e., the heat input for the control period was less than the heat input for

1997). For these cases, the commission agrees that determining the appropriate equation to use should be done on a case-by-case basis.

The equation in §101.334(2) will be used for cases where the reduced utilization or shutdown was not replaced by thermal energy generated by another unit. In accordance with §39.264(i)(3), allowances will be deducted from the compliance account to reflect what emissions from the electing EGF would have been using 1997 heat input.

The equation in §101.334(3) will be used for cases where the reduced utilization or shutdown was replaced by thermal energy generated by another EGF. In these cases, allowances will be deducted from the compliance account for each ton of actual emissions, if any, from the electing EGF for the control period. In addition, allowances will also be deducted from the electing EGF's compliance account for each actual ton of emissions that result when the displaced thermal energy is generated by the other EGF. In cases where the EGF to which the thermal energy was transferred can be identified, the emission factor for that EGF will be used in determining the allowances to deduct. This allows the electing EGF to keep more allowances if the thermal energy is transferred to an EGF with a low emission factor. In those cases where the EGF to which the thermal energy was transferred cannot be identified, the thermal energy is assumed to be transferred to various EGFs in the state. As an estimate of emissions in this case, the equation uses the average emission factor for the state based on the 1997 Emissions Scorecard for the EPA Acid Rain Program. Using the state average emission factor encourages decreased utilization of electing EGFs that have a higher emission factor than the state average.

EPA-ARD asked, concerning §101.334(e)(1), whether the equation is necessary when the heat input for the control period is greater than that of 1997. EPA-ARD also asked whether the emission factor in §101.334(e)(1) and (2) is a measured emission rate in pounds/MMBtu and if so, from which sources of information. The commenter then asked if the equations could ever yield negative numbers and if so, what a negative result would mean.

The provisions of the proposed §101.334(e) were revised and are now in §101.334(2) and (3) for organizational clarity. The commission believes that because the heat input and emission factors can fluctuate, the formula is necessary to accurately determine the amount of allowances, if any, that can be transferred. A negative result indicates that actual emissions exceeded allocated allowances; therefore, no allowances are available for trading, unless additional allowances have been purchased. The commission agrees that clarification needs to be added as to the source of the emission factors and has revised §101.334(e)(1) and (2) and §116.914(e) accordingly.

Brazos Electric commented that §101.334 restricts transfer of allowances more than contemplated by the language of SB 7. The commenter stated that specifically, TUC, §39.264 makes no requirements for "authorized account representatives," prohibitions on transfers before May 1, 2003, or the tables of allowances set forth in §101.334(e)(1) and (2).

In order to ensure that the allowances allocated to each participating EGF are properly tracked and traded, the commission believes that it is necessary to designate an individual or individuals who have the recognized authority to transfer and manage allowances. This designation is

necessary for the commission to ensure that transfers are valid and not fraudulent. The commission does not believe that this is a restriction on the trading program that will inhibit trading. The proposal stated that the delay in the start of the trading program was necessary to allow sufficient time to develop a tracking system for the transfer of allowances. Further, the commission expects to adopt SIP revisions that will require additional emission reductions from EGFs in attainment and nonattainment areas. The commission anticipates that these future SIP reductions may impact the EBTA and that it would be premature to allow for actual trading to begin prior to the adoption of the SIP regulations. The commission understands the need to begin planning for trades and does not believe that the restriction on actual trading will prohibit EGFs from creating contracts or other agreements that will be used for trading after the start of the program. The commission's response concerning §101.334(e) is addressed elsewhere in this response to comments.

Brazos Electric commented that while TUC, §39.264(j) restricts transfer of allowances between regions (as proposed in §101.334(f)), an exception should be made for transfers within the same company:

The commission has made no changes in response to this comment. TUC, §39.264(j), states that allocations (allowances) can only be traded within the same region. Therefore, trading cannot be made between regions, even if they are within the same company. However, companies that have multiple locations within the same region are not prohibited from trading with each other.

Sierra Club commented that trading should be limited to the same airshed, the same nonattainment area, and the same area of influence affecting the nonattainment area so that the trades pass the "laugh test"

The restrictions on trading are consistent with the requirements of TUC, §39.264 which defines specific regions of the state and limits trading of allowances to EGFs within the same region. TUC, §39.264 does not include any restrictions on trading with regard to nonattainment areas or airsheds.

TXU commented the reductions from electing EGFs may be used only to the extent that they are beyond the requirement of any other state or federal standard and that this provision does not change the allowance allocation, it only restricts how many allowances can be transferred from electing EGFs to other EGFs. TXU suggested that §101.334 could be revised to add a restriction in the transfer of allowances from electing EGFs to other EGFs.

The commission has made no changes in response to this comment. TUC, §39.264(i)(4) allows emission reductions from electing EGFs to be used to satisfy emission reductions for grandfathered EGFs to the extent that reductions used to meet TUC, §39.264(c) are beyond the requirements of any other state or federal standard, or both. The commission believes that allowances that are allocated to an electing EGF that authorize emissions in excess of applicable state or federal requirements must be invalidated to prevent reductions from being counted twice.

Section 101.333(3) was revised to allow the commission to invalidate allowances allocated to electing EGFs that authorize emissions beyond state or federal requirements.

Reliant commented that §101.334(a) should be revised to read as follows: "Allowances may be transferred at any time after May 1, 2003," and suggested deleting the phrase "during the control period."

The adopted version of §101.334 is a new section called "Allowance Deductions." Some of the portions of the proposed §101.334 have been moved to §101.335, now called "Allowance, Banking, and Trading." The former §101.334(a) is now in §101.335(b). New §101.335(b) provides that allowances may be transferred at any time during a control period. This subsection is intended to define the time period for transfers, not the time period for the beginning of the EBTA program. That issue is addressed in the new §101.335(c).

EPA-ARD commented that there appears to be a contradiction in the required notification date for transfer of allowances. Section 101.334(b) allows a facility to document a transfer no later than June 30 following the control period. Section 101.334(d) requires notification within 30 days after the transfer, and §101.332(b) requires all transfers to be done by May 1. B&P commented that proposed language in §101.334(b) and (d) and §101.336(b) includes three separate documentation, notification, and reporting requirements. The commenter stated that TNRCC should delete §101.334(b), because TNRCC will already have received notification of all transfers under §101.334(d). If §101.334(b) is not deleted, it should be revised to allow documentation of final transfers and the emissions report be

submitted on June 30. EPA-ARD commented in §101.334(b) that 60 days is sufficient to finish transfers and submit notification. Reliant commented that §101.336(b) should be revised to allow the report to be submitted by August 1 of each year instead of June 1.

In the new §101.335(b)(2), the commission requires notification within 30 days of transfer for timely maintenance of compliance account records. The 60-day notification required in §101.334(b), now located in §101.336(b), will serve as confirmation that the transfers of which the commission received notification under §101.335(b)(2), formerly §101.334(d), occurred, and will allow the commission to timely reconcile all compliance accounts. The commission has modified §101.336(b) to allow final reports to be submitted no later than June 30 following the control period. The commission believes that submittal of these reports as quickly as reasonably possible is critical to expedite the review and reconciliation of compliance accounts to allot allowances for the next control period. The commission believes that 60 days is a reasonable time frame for this purpose.

EPE commented that the allowance mechanism under SB 7 should be consistent with the allowance transaction mechanism used under Part 75 and the Acid Rain Program. EPE also commented that the frequency of allowance reporting should match the reporting of allowances and emissions under the Part 75 rules.

The commission believes that the allowance and reporting requirements are consistent with the control period required by TUC, §39.264. Further, the requirement to report after each trade

and the reconciliation period will allow the commission to maintain an up-to-date registry consistent with the control period. The rules have not been changed in response to this comment.

EPA-ARD commented that subsections (a), (b), (d), and (e) in §101.334 could be reorganized or combined for clarity. EPA-ARD also commented that §101.334(a) and (d) do not clarify who may transfer allowances and who must notify whom of the transfers.

As stated previously, most of the provisions in §101.334 have been moved to §101.335 for clarity and organization. The commission agrees that the rule was unclear as to who may transfer allowances and who is being notified about transfers. The rule has been revised to clarify that allowances are transferred by authorized account representatives and that notification of transfers of allowances must be provided to the commission. Section 101.334(a) is now §101.335(b). Section 101.334(b) is now §101.336(b). Section 101.334(c) is now §101.335(b)(1). Section 101.334(d) is now §101.335(b)(2). Section 101.334(f) is now §101.335(d), and §101.334(g) is now §101.335(e).

B&P commented that §101.334(d) states that allowance transfers are prohibited prior to May 1, 2003, and that this is justified in the proposed preamble to allow the TNRCC to create the appropriate tracking system. The commenter stated that there does not appear to be any justification for prohibiting allowance transfers for more than three years after the initial allocation of allowances; thus, B&P recommended that §101.334(d) be modified to allow transfers soon after January 1, 2000 (recommended six months after).

The commission has not made changes in response to this comment; however, §101.334(d) is now §101.335(b)(2). The proposal stated that the delay in the start of the trading program was necessary to allow sufficient time to develop a tracking system for the transfer of allowances. Further, the commission expects to adopt SIP revisions that will require additional emission reductions from EGFs in attainment and nonattainment areas. The commission anticipates that these future SIP reductions may impact the EBTA and that it would be premature to allow for actual trading to begin prior to the adoption of the SIP regulations. The commission understands the need to begin planning for trades and does not believe that the restriction on actual trading will prohibit EGFs from creating contracts or other agreements that will be used for trading after the start of the program.

B&P commented that §101.334(f) should be revised to clarify that EGFs in the El Paso Region can use credits obtained from Juarez, Mexico, as provided in proposed §101.337(a).

The commission has not revised the rule in response to this comment. Section §101.334(f), now §101.335(d), provides that allowances may not be transferred between regions. Section §101.337(a) provides that an EGF in the El Paso Region can meet the emission allowances by using credits obtained from reductions in the City of Juarez, United States of Mexico. Elsewhere in the response to comments in this adopted preamble, the commission states its intent for revising the definition of "El Paso Region" to be consistent with the Paso del Norte Air Shed. The Paso del Norte Air Shed includes the City of Juarez and Sunland Park, New Mexico. Since the El Paso

Region will be defined to include the City of Juarez, it is not necessary to revise the new §101.335(d).

EPA-ARD commented that in §101.334(h)(1)(C) and (K), allowances will need to be tagged (region, nonattainment status, grandfathered, permitted, etc.), in order for brokers and buyers to know whether they are following the restrictions of trading.

The subparagraphs to which EPA-ARD refers were not included in the proposed rules. However, allowances will be tracked and recorded by the TNRCC. The allowance registry will note the original owner of the allowances, the location of the EGF, whether the allowance was allocated to a grandfathered or electing EGF, and all other pertinent information to support the EBTA.

SPS commented that if the TNRCC must reconcile emissions to an annual cap each year, there will have to be compensation for excess allowances that must be retired. The commenter also stated that the TNRCC would have to establish some type of buy-back program to limit the available allowances in any given year.

The commission has made no changes to the rules in response to this comment. Previous drafts of §101.335 limited the life of allowances to one year. The adopted §101.335(b) provides that allowances not used for compliance may be banked for use in subsequent years. Thus, the commission does not believe that the change would be needed because allowances do not expire.

PC commented that in §101.335 the commission should give an incentive to utilities to retire their oldest plants or to go further in reducing emissions by modifying §101.335 to allow owners of grandfathered power plants to bank for two years any reductions resulting from the retirement or extra cleanups. PC added that additional years of credit should be given for EGFs that make additional reductions, like three years for a permitted power plant and five years on a retired power plant.

Although electing EGFs may not transfer or bank allowances that are conserved as a result of reduced utilization or shutdown, grandfathered EGFs are not subject to the same limitation. Therefore, utilities have an incentive to shut down grandfathered EGFs, because they are allowed to keep the allowances in perpetuity. Section 101.335(a) already provides that allowances not used for compliance may be banked for use in subsequent years. There is no limitation in the adopted rule on the amount of time that allowances may be banked. The commission believes that the adopted rule contains the incentive for grandfathered EGFs to be retired or make additional reductions.

EPA-ARD commented that in §101.335(a), the term "electing facilities" should read "electing EGFs." B&P commented that there are several instances in the proposed rules where the undefined term "electing facilities" is used rather than the defined term "electing EGFs."

The commission agrees, and has revised all references to "electing facilities" throughout Chapter 101 to "electing EGFs." The provision in §101.335(a), concerning "electing facilities" and

"reduced utilization or shutdown" was deleted, because the new formulas in §101.334(2) and (3) address the issue.

EPA-ARD questioned why §101.335(b) limits banking to one year, and stated that this may reduce the incentives for over-complying with the program. SPS commented that no restrictions should be placed on allowances except those specifically mentioned in SB 7. The commenter also stated that SB 7 does not limit the life of an allowance; in fact, §39.264(k)(2) refers to using allowances in later years (plural). Reliant commented that §101.335(b) should be revised as: "Allowances not used for compliance during a control period may be banked for use in subsequent control periods." The commenter stated that this change clarifies that allowances may be banked and used in subsequent control periods. The word "years" may lead to confusion, since "control periods" is the term used throughout the proposal.

The proposed rule did not contain a limitation in §101.335(b), now §101.335(a), concerning the number of years the allowances could be banked. The commission agrees that the word "years" should be deleted from the new §101.335(a) and has revised the rule to refer to "control periods."

EPE and CT&W commented that in §101.337(a), the intent of the Legislature was to include Ciudad Juarez, Mexico, Sunland Park, New Mexico, and El Paso County as the contiguous geographic area where an EGF may meet the emission allowances by using credit from emissions reductions achieved anywhere in the contiguous airshed, provided that certain criteria are met.

The commission has revised the definition of "El Paso Region" in §101.330(13) to include Ciudad Juarez, Mexico, and Sunland Park, New Mexico. CT&W provided with its comments a copy of the May 20, 1999 House Journal, "CSSB 7 - Statement of Legislative Intent," in support of its contention that the Legislature considered the purpose of the La Paz agreement as supporting the legislative intent for SB 7. That statement says in part that "The Act officially designated the Paso del Norte Air Shed as the contiguous air shed basin between El Paso, Texas, Sunland Park, New Mexico, and Ciudad Juarez, Chihuahua." TUC, §39.264(g) provides that the El Paso Region includes El Paso County. There is no express prohibition in TUC, §39.264(g) that prevents the commission from defining the El Paso Region as also including Ciudad Juarez, Mexico, and Sunland Park, New Mexico. The inclusion of Sunland Park, New Mexico will give further effect to the specific provisions of TUC, §39.264 concerning the El Paso Region, since it will provide EPE with additional options for meeting the emission reductions required for the El Paso region.

EPE and B&P commented on §101.337(a) that creditable reductions from Juarez are not limited to reductions from EGFs and asked the commission to confirm this position.

The commission agrees that creditable reductions from Juarez are not limited to reductions from EGFs. Since the rule as proposed does not limit creditable reductions from Juarez to EGFs only, no changes were made to the adopted §101.337(a).

CT&W commented that §101.337(a)(1)(A) should be revised to add language to clarify how reductions in Mexico will be enforceable. The commenter suggested that this intent could be met by adding a

special provision to EPE's permit related to a contemplated or proposed emissions reduction from Ciudad Juarez. In that way, the commission will be able to enforce EPE's performance of that emission reduction project. CT&W stated that if the commission is unwilling or unable to interpret and apply the provision regarding Ciudad Juarez in this manner, it should be deleted.

The commission believes that the enforcement issues concerning ERCs from the City of Juarez would best be addressed on a case-by-case basis. This could be done through the use of special conditions in EGFPs as allowed by §116.913(b). By not including limitations in the adopted rule concerning the enforcement of emission reductions in the City of Juarez, EGFs in the El Paso Region can propose new and innovative strategies to obtain reductions from facilities in the City of Juarez. Thus, the commission does not believe that it is appropriate to revise or delete §101.337(a)(1)(A), since the reductions must be enforceable.

B&P commented that §101.337(a)(1)(B) requires emissions reductions in Juarez to be permanent, meaning that the emission reduction is unchanging for the remaining life of the source. The commenter stated that because an emission reduction could be "permanent" even though it changes (the emission reduction could increase), the definition should be revised by removing the statement that "permanent" means unchanging.

The commission has made no changes to the rule in response to this comment. If additional reductions are made, they would be considered to be a new reduction. Any reductions relied upon for an allowance would have to remain unchanged and permanent.

EPE, B&P, and CT&W commented that §101.337(b) exempts EGFs in the El Paso Region if the TNRCC determines that NO_x reductions in the area would result in an increased ambient ozone level. The TNRCC states in the proposed preamble that the NO_x waiver (§182(f)) that has been granted for the El Paso Region does not satisfy the criteria of this section. The commenter stated that this interpretation is not consistent with legislative intent and should be corrected.

TUC, §39.264(q) requires that the commission or EPA demonstrate that reductions in NO_x would result in an increase in ambient ozone levels in order to be exempt from the NO_x reduction requirements of §39.264. Neither the EPA nor the commission have made this determination. The §182(f) waiver indicates that NO_x reductions have not been shown in a SIP to be necessary for the attainment of the federal ozone standard. This is not equivalent to saying that NO_x reductions will cause an increase in ozone levels; therefore, the commission believes that the NO_x reduction requirements of TUC, §39.264 apply in El Paso County and has not changed the rule.

STATUTORY AUTHORITY

The new sections are adopted under TUC, §39.264, which authorizes the commission to develop rules for the allocation of emission allowances to EGFs and to make rules concerning the banking and trading of those allowances. The new sections are also adopted under Texas Health and Safety Code, TCAA, §382.011, which authorizes the commission to administer the requirements of the TCAA; §382.012, which provides the commission with the authority to develop a comprehensive plan for the state's air; §382.017, which authorizes the commission to adopt rules consistent with the policy and purposes of the TCAA; §382.023, which authorizes the commission to issue orders; and §382.061, which

authorizes the commission to delegate permitting authority to the executive director; and Texas Water Code, §5.122, which authorizes the commission to delegate uncontested matters to the executive director.

SUBCHAPTER H : EMISSIONS BANKING AND TRADING

DIVISION 2 : EMISSIONS BANKING AND TRADING OF ALLOWANCES

§§101.330-101.337

§101.330. Definitions.

The following words and terms, when used in this division, shall have the following meanings, unless the context clearly indicates otherwise.

(1) **Allowance** - The authorization to emit one ton of nitrogen oxides (NO_x) or sulfur dioxide (SO_2) during a control period.

(2) **Authorized account representative** - The responsible person who is authorized, in writing, to transfer and otherwise manage allowances.

(3) **Banked allowance** - An allowance which is not used to reconcile emissions in the designated year of allocation, but which is carried forward into future years and noted in the compliance or broker account as “banked.”

(4) **Broker** - A person not required to participate in the requirements of this division who opens an account under this division for the purpose of banking and trading emissions allowances.

(5) **Broker account** - The account where allowances held by a broker are recorded. Allowances held in a broker account may not be used to satisfy compliance requirements for this division.

(6) **Coal** - All solid fuels classified as anthracite, bituminous, subbituminous, or lignite by the American Society for Testing and Materials Designation ASTM D388–92 ''Standard Classification of Coals by Rank'' (as incorporated by reference in Title 40 Code of Federal Regulations, §72.13 (effective June 25, 1999)).

(7) **Coal-fired** - The combustion of fuel consisting of coal as defined in paragraph (6) of this section or any coal-derived fuel (except coal-derived gaseous fuels with a sulfur content no greater than natural gas), alone or in combination with any other fuel. The definition is independent of the percentage of coal or coal-derived fuel consumed during any control period.

(8) **Compliance account** - The account where allowances held by an EGF or multiple EGFs are recorded for the purposes of meeting the requirements of this division and Chapter 116, Subchapter I of this title (relating to Electric Generating Facility Permits). EGFs not under common ownership or control may have separate compliance accounts.

(9) **Control period** - The 12-month period beginning May 1 of each year and ending April 30 of the following year. Control periods begin May 1, 2003.

(10) **East Texas Region** - All counties traversed by or east of Interstate Highway 35 north of San Antonio or traversed by or east of Interstate Highway 37 south of San Antonio, and also including Bexar, Bosque, Coryell, Hood, Parker, Somerville, and Wise Counties.

(11) **Electing EGF** - An electric generating facility permitted under Chapter 116, Subchapter B of this title (relating to New Source Review Permits) which is not subject to the requirements of Texas Utility Code, §39.264 and elects to comply with Chapter 116, Subchapter I of this title (relating to Electric Generating Facility Permits).

(12) **Electric generating facility (EGF)** - A facility that generates electric energy for compensation and is owned or operated by a person in this state, including a municipal corporation, electric cooperative, or river authority.

(13) **El Paso Region** - All of El Paso County, Ciudad Juarez, Mexico, and Sunland Park, New Mexico.

(14) **Grandfathered EGF** - A facility that is not subject to the requirement to obtain a permit under TCAA, §382.0518(g), and that generates electric energy for compensation and is owned or operated by a person in this state, including a municipal corporation, electric cooperative, or river authority.

(15) **Heat input** - The heat derived from the combustion of any fuel at an EGF. Heat input does not include the heat derived from reheated combustion air, recirculated flue gas, or exhaust from other sources.

(16) **NO_x allowance** - An authorization to emit is valid only for the purposes of meeting the requirements of this division and Chapter 116, Subchapter I of this title.

(17) **Person** - For the purpose of initial issuance of permits under Chapter 116, Subchapter I of this title, and for the issuance of allowances under this division, a person includes an individual, a partnership of two or more persons having a joint or common interest, a mutual or cooperative association, and a corporation, but does not include an electric cooperative.

(18) **SO_2 allowance** - An authorization to emit SO_2 valid only for the purposes for meeting the requirements of this division and Chapter 116, Subchapter I of this title.

(19) **West Texas Region** - All counties not contained in the East Texas Region or El Paso Region.

§101.331. Applicability.

This division applies only to the following:

(1) electric generating facilities permitted under Chapter 116, Subchapter I of this title (relating to Electric Generating Facility Permits); and

(2) brokers.

§101.332. General Provisions.

(a) Allowances are valid only for the purposes of meeting the requirements of this division and for meeting the requirements of Chapter 116, Subchapter I of this title (relating to Electric Generating Facility Permits), and cannot be used to meet or exceed the limitations of any annual emission limitation authorized under Chapter 116, Subchapter B of this title (relating to New Source Review Permits) or any applicable rule or law.

(b) On June 1 after every control period, a grandfathered or electing electric generating facility (EGF) shall hold a quantity of allowances in its compliance account that is equal to or greater than the total emissions of that air contaminant emitted during the prior control period. Compliance with the allowance system will begin with the control period beginning May 1, 2003.

(c) Emission reductions used to satisfy the requirements of the Emissions Banking and Trading of Allowances (EBTA) program cannot be used to generate emission reduction credits or discrete emission reduction credits.

(d) Allowances cannot be used for netting requirements to avoid the applicability of federal and state new source review (NSR) requirements.

(e) Allowances cannot be used to satisfy offset requirements for new or modified sources subject to federal nonattainment NSR requirements.

(f) An allowance does not constitute a security or a property right.

(g) All allowances will be allocated, transferred, or used as whole allowances. To determine the number of whole allowances, the number of allowances will be rounded down for decimals less than 0.50 and rounded up for decimals of 0.50 or greater.

(h) One compliance account shall be used for multiple EGFs permitted under Chapter 116, Subchapter I of this title located at the same property and under common ownership or control.

§101.333. Allocation of Allowances.

Allowances will be allocated according to the requirements of this section.

(1) Except as provided in paragraphs (2) and (3) of this section, allowances will be calculated for grandfathered electric generating facilities (EGF) using the following equation: Figure: 30 TAC §101.333(1)

$$A = \frac{ER * HI}{2000 \text{ lb / allowance}}$$

Where:

A	=	Number of allowances
HI	=	Total heat input (million British thermal units (MMBtu)) as listed in the 1997 Emissions Scorecard from EPA's Acid Rain Program, or if not listed in the 1997 Emissions Scorecard, by a method approved by the executive director, consistent with the emission reduction requirements of this division.
ER	=	Emission rate, as defined in subparagraphs (A) and (B) of this paragraph;

(A) In the East Texas Region:

(i) 0.14 pound nitrogen oxides (NO_x) per MMBtu; and

(ii) 1.38 pounds sulfur dioxide (SO_2) per MMBtu only for coal-fired grandfathered EGFs.

(B) In the West Texas and El Paso Regions, 0.195 pound per MMBtu.

(2) For electing EGFs, the amount of allowances is equal to emissions as listed in the 1997 Emissions Scorecard from EPA's Acid Rain Program, or if not listed in the 1997 Emissions Scorecard, by a method approved by the executive director, consistent with the emission reduction requirements of this division; and in both cases, shall not exceed any of the following:

(A) any annual emission limitation authorized under Chapter 116, Subchapter B of this title (relating to New Source Review Permits);

(B) an applicable state or federal requirement.

(3) The commission may invalidate any allowances allocated to an electing EGF that authorize emissions in excess of applicable state or federal requirements.

(4) If emissions of NO_x or, if applicable, SO_2, exceed the amount of allowances for a given control period, allowances for the next control period will be reduced in an amount equal to the emissions exceeding the allowances in the compliance account.

(5) Allowances will be allocated:

(A) initially, by:

(i) January 1, 2000, for grandfathered EGFs;

(ii) January 1, 2001, for electing EGFs; and municipal corporations, electric cooperatives, and river authorities that choose to obtain a permit under Chapter 116, Subchapter I of this title (relating to Electric Generating Facility Permits) for any grandfathered or electing EGFs previously exempted under §116.910(d) of this title (relating to Applicability);

(B) subsequently, by May 1 of each year, beginning in 2004.

(C) allowances will be allocated:

(i) initially by commission order for all grandfathered and electing EGFs;

(ii) notwithstanding clause (iii) of this subparagraph, at the beginning of each control period, the commission will deposit the same amount of allowances into each grandfathered or electing EGF's compliance account;

(iii) for electing EGFs, the annual deposit for any control period may be adjusted to reflect new state or federal requirements.

(6) Allowances may be deducted from compliance accounts following the review of trading reports required under §101.336(b) of this title (relating to Emission Monitoring, Compliance, Demonstration, and Reporting.)

(7) The commission shall maintain a registry of the allowances in each compliance account. For each transfer, the registry shall include the price paid per allowance. The registry shall not contain proprietary information.

§101.334. Allowance Deductions.

Allowances will be deducted from a grandfathered or electing electric generating facility's (EGF) compliance account for a control period based upon the following.

(1) The following will have deducted from their compliance accounts allowances equal to the number of tons of air contaminant emitted during the control period as reported in compliance with §101.336 (relating to Emission Monitoring, Compliance Demonstration, and Reporting.

(A) grandfathered EGFs; and

(B) electing EGFs whose heat input for the control period is equal to or greater than its heat input for 1997;

(C) electing EGFs whose heat input for the control period is less than its heat input for 1997 where the reduced utilization or shutdown has been replaced by another EGF permitted under Chapter 116, Subchapter I of this title (relating to Electric Generating Facility Permits).

(2) For electing EGFs whose heat input for the control period is less than the heat input for 1997 and whose reduced utilization or shutdown has not been replaced by another EGF, allowances will be deducted from the compliance account according to the following equation: Figure: 30 TAC §101.334(2)

$$A = \frac{HI_{1997} \times EF_{CP}}{2000 \text{ lbs / allowance}}$$

Where:

A = Allowances to be subtracted from the compliance account

HI_{1997} = Heat input from 1997

EF_{CP} = The emission factor for the control period in terms of lbs/MMBtu,or if an emission factor for the control period is not available, the most recently available emission factor for that EGF.

(3) For electing EGFs whose heat input for the control period is less than the heat input for 1997 and whose reduced utilization or shutdown has been replaced by another EGF not permitted under Chapter 116, Subchapter I of this title, allowances will be deducted from the compliance account according to the following equation: Figure: 30 TAC §101.334(3)

$$A = \frac{(HI_{CP} \times EF_{CP}) + [(HI_{1997} - HI_{CP}) * EF_{new}]}{2000 \text{ lbs / allowance}}$$

Where:

A	=	Allowances to be subtracted from the compliance account
HI_{CP}	=	Heat input for the control period.
EF_{CP}	=	The emission factor for the control period in terms of lbs/MMBtu.
HI_{1997}	=	Heat input from 1997
EF_{new}	=	The emission factor in terms of lbs/MMBtu for the EGF that replaced the thermal energy from the reduced utilization or shutdown. If the specific EGF that replaced the thermal energy is not identifiable, the emission factor shall be equal to the average emission factor for all EGFs in the state as listed in the 1997 Emissions Scorecard from EPA's Acid Rain Program.

§101.335. Allowance Banking and Trading.

(a) Allowances not used for compliance during a control period may be banked for use in subsequent control periods. Allowances may only be used for the control period for which they were allocated or subsequent control periods, and may only be used within the same region where they were originally allocated.

(b) Allowances may be traded at any time during the control period.

(1) Only authorized account representatives may trade allowances.

(2) Notification of trades must occur within 30 days after the trade.

(c) Allowance trades are prohibited prior to May 1, 2003.

(d) Traded allowances held in compliance accounts must have originated from electric generating facilities in the same region.

(e) Allowances may be held only in compliance accounts for use by EGFs located in the region in which the allowances were originally allocated or in broker accounts.

§101.336. Emission Monitoring, Compliance Demonstration, and Reporting.

(a) Emission monitoring and reporting shall be conducted in accordance with §116.914 of this title (relating to Emissions Monitoring and Reporting Requirements).

(b) For each control period, grandfathered or electing electric generating facilities (EGF), must submit a report to the commission by June 30 of each year detailing the following:

(1) the amount of emissions of each allocated air contaminant during the preceding control period.

(2) a summary of all final trades for the preceding control period.

§101.337. El Paso Region.

(a) A grandfathered or electing electric generating facility (EGF) in the El Paso Region may meet the emissions allowances by using credits from emissions reductions achieved in the City of Juarez, United States of Mexico and from EGFs located in Sunland Park, New Mexico. Emission reductions under this section must meet the following criteria.

(1) The emission reduction must be:

(A) enforceable by the commission;

(B) permanent, meaning that the emission reduction is unchanging for the remaining life of the source;

(C) quantifiable, so that the emission reduction can be measured or estimated with confidence using replicable techniques;

(D) surplus, such that the emission reduction is not otherwise required of a facility by a state or federal law, regulation, or agreed order; and

(E) a real reduction in which actual emissions are reduced.

(2) The emission reduction must be reviewed and approved by the executive director prior to converting the credits into allowances under this program.

(b) Grandfathered and electing EGFs in the El Paso Region are exempt from the requirements of this division if either EPA or the commission determines that reductions of nitrogen oxides in the El Paso Region that would otherwise be required under this division would result in an increased ambient ozone level in El Paso County.