

Texas Commission on Environmental Quality

Interoffice Memorandum

To: Commissioners **Date:** May 3, 2013

Thru: Bridget C. Bohac, Chief Clerk
Zak Covar, Executive Director

From: Steve Hagle, P.E., Deputy Director
Office of Air

Docket No.: 2009-1400-RUL

Subject: Commission Approval for Rulemaking Adoption
Chapter 101, General Air Quality Rules
Severe Ozone Nonattainment Area Failure to Attain Fee
Rule Project No. 2009-009-101-AI

Background and reason(s) for the rulemaking:

The Federal Clean Air Act (FCAA), §182(d)(3) and (e), Plan Submission and Requirements, and §185, Enforcement for Severe and Extreme Ozone Nonattainment Areas for Failure to Attain, requires each state implementation plan (SIP) for ozone nonattainment areas classified as severe or extreme to impose a penalty fee for major stationary sources of volatile organic compounds (VOC) located in the area if the area fails to attain the ozone National Ambient Air Quality Standard (NAAQS or standard) by the applicable attainment date. FCAA, §182(f), Plan Submissions and Requirements, requires all SIP requirements that apply for VOC emissions to also apply for nitrogen oxides (NO_x) emissions. This rulemaking assesses a fee for each calendar year after the rule adoption until the area is redesignated to attainment, the United States Environmental Protection Agency (EPA) issues a finding of attainment, or until any other action is taken by the EPA to end the fee program. In addition, these rules give the executive director the discretion to hold collection of the penalty fee in abeyance from the time that certified data demonstrating attainment of the one-hour ozone standard are submitted to the EPA until the EPA publishes a finding.

The fee is \$5,000 per ton, as adjusted by the consumer price index (All Urban Consumers, Not Seasonally Adjusted, base period 1982-84 = 100), of VOC, NO_x, or both emitted in excess of 80% of a stationary source's baseline emissions. For 2012 emissions, the fee rate would be \$9,169 per ton. A stationary source that is major for VOC is subject to fees on VOC; a stationary source that is major for NO_x is subject to fees on NO_x; and a stationary source that is major for both VOC and NO_x would be subject to the fee on both VOC and NO_x. If the state does not collect the fees that are due, then the EPA must collect the fees and may collect interest. Fees and interest would not be returned to the state.

The Texas Commission on Environmental Quality (TCEQ) proposed rules to comply with FCAA, §185 requirements under 30 TAC Chapter 101, Subchapter B in November 2009. The 2009 proposed rules reflected the explicit FCAA, §185 fee-based calculation and equivalent alternatives under FCAA, §172(e).

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In January 2010, the EPA issued a guidance memo (Guidance on Developing Fee Programs Required by Clean Air Act Section 185 for the 1-hour Ozone NAAQS, from Stephen D. Page) indicating that states could meet the one-hour ozone FCAA, §185 obligation through a SIP revision containing either the fee program or an equivalent alternative program. The memo further stated that an area showing attainment of the 1997 eight-hour ozone standard, based on permanent and enforceable reductions, would no longer be required to submit a fee program SIP revision to satisfy the anti-backsliding requirements associated with transition from the one-hour ozone standard to the 1997 eight-hour ozone standard. The executive director withdrew its proposed rules from commission consideration in May 2010 and simultaneously submitted a request for termination of the fee program for the Houston-Galveston-Brazoria (HGB) one-hour ozone nonattainment area (Brazoria, Chambers, Fort Bend, Galveston, Harris, Liberty, Montgomery, and Waller Counties) based on data showing that the area was monitoring attainment of the 1997 eight-hour ozone standard. On July 25, 2011, the EPA denied the termination request based on preliminary 2011 data indicating that the HGB area was no longer monitoring attainment of the 1997 eight-hour ozone standard and due to a July 2011 District of Columbia Circuit Court of Appeals decision vacating its 2010 guidance.

The one-hour ozone design value for the HGB area for 2009 through 2011 was 125 parts per billion (ppb), which exceeds the standard by 1 ppb. A final notice of finding of failure to attain was published in the *Federal Register* on June 19, 2012 effective July 19, 2012, for the HGB one-hour ozone nonattainment area. The attainment date for the one-hour ozone standard for the HGB area was November 15, 2007.

The TCEQ re-initiated the rulemaking process under Chapter 101, Subchapter B to implement the FCAA, §185 fee requirement. The commission approved the proposed rules for publication, public hearing, and public comment on November 14, 2012, and the rules were published in the *Texas Register* on November 30, 2012. The public comment period closed January 14, 2013.

Scope of the rulemaking:

A.) Summary of what the rulemaking will do:

This rulemaking reflects the FCAA, §185 fee-based calculation on emissions in excess of 80% of an affected stationary source's baseline emissions of VOC, NO_x, or both, depending upon a source's major source determination. The baseline amount may be calculated as the lower of the average baseline emissions or average allowable emissions. This rulemaking reflects the FCAA, §185 required penalty of \$5,000 per ton as adjusted by the consumer price index. The adjusted penalty amount for 2012 is \$9,169 per ton. This rulemaking includes a source applicability determination, an emission baseline amount calculation methodology, criteria for determining the required fee, and due dates for certain program requirements, including fee payment. This rulemaking also includes a provision to place the penalty fee in abeyance when the area's design value shows attainment of the NAAQS.

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This rulemaking includes emissions-based alternatives to the FCAA, §185 fee, which include the ability to take credit for emissions reductions that are surplus to those relied upon in the applicable attainment demonstration SIP, the ability to use emissions reduction credits to offset a source's penalty fee, and the ability to fund Supplemental Environmental Projects (SEP) to offset a source's penalty fee. This rulemaking also provides the ability to offset the HGB area's fee obligation with revenue collected in the HGB nonattainment area for the state's Texas Emissions Reduction Plan (TERP), the Low-Income Vehicle Repair Assistance, Retrofit, and Accelerated Vehicle Repair Program (LIRAP), and the Local Initiative Project (LIP). This rulemaking provides flexibility in establishing a baseline amount for VOC and NO_x emissions. Sites may aggregate VOC with NO_x emissions. Sites under common ownership or control may aggregate VOC and NO_x emissions at one or more sites or may aggregate pollutants across multiple sites.

This rulemaking would be created in Chapter 101, new Subchapter B and is organized to implement the provisions of the FCAA, §185 requirements as well as provide for equivalent alternative options to meet the fee obligation under FCAA, §172. This organization is intended to allow the EPA to approve all or part of the rules and to minimize the possibility of FCAA, §185 fees being imposed and collected by the federal government.

B.) Scope required by federal regulations or state statutes:

- FCAA, §185 requires that major stationary sources in severe or extreme ozone nonattainment areas be subject to the FCAA, §185 fee program if the area does not attain the standard by the applicable attainment deadline.
- As required by FCAA, §185, a baseline amount is defined as the lower of actual or authorized emissions on the unmet attainment date.
- FCAA, §185 describes the manner in which the penalty fee would be calculated, and the fee calculation methodology adopted with this rulemaking is based on that description.
- Per to FCAA, §185, a major stationary source is subject to the penalty fee on emissions of VOC, NO_x, or both (depending on a source's major source determination) that exceed 80% of that source's baseline amount.
- FCAA, §185 indicates that an area's fee program would end when the area is redesignated as attainment for the applicable standard.

C.) Additional staff recommendations that are not required by federal rule or state statute:

- Due dates are established for baseline amount determinations and annual fee invoices.
- TERP and LIRAP/LIP program revenue collected from the HGB nonattainment area may be used to offset a portion of the area's fee obligation.

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- For sources that are cyclic, irregular, or have significantly varying emissions, a historical perspective may be used to determine baseline amounts, as allowed in a 2008 guidance memo from the EPA.¹
- Additional flexibility is allowed in baseline amount and fee determinations by allowing VOC and NO_x aggregations at a site or across multiple sites.
- The first fee period would be based on 2012 emissions inventory data, which would be the most recent emissions inventory data after the rule adoption date.
- In addition to ending the \$185 fee program upon redesignation to attainment of the applicable standard, as stipulated under FCAA, §185, the rulemaking further defines the program as ending upon a finding of attainment by the EPA or other action by the EPA to end the program.
- The executive director may place fee collection for the program in abeyance if three years of quality-assured data are submitted to the EPA showing a design value that did not exceed the NAAQS.
- A major stationary source that did not exist on the required 2007 attainment date or had been operating fewer than 12 months as of the required 2007 attainment date, may determine its baseline amount based on the first calendar year of actual emissions.
- A source that was minor as of the required 2007 attainment date, but subsequently became major, may be allowed to pay the \$185 fee based on emissions during its first 12-consecutive months operating as a major source.
- This rulemaking allows a source to reduce its fee obligation by retiring allowances or emissions credits on a ton-for-ton and pollutant-by-pollutant basis.
- This rulemaking allows SEP payments that are not used to offset an administrative penalty to be used to offset a source's fee obligation (dollar-for-dollar or ton-for-ton).

Statutory authority:

State authority: Texas Clean Air Act, Texas Health and Safety Code (THSC), §382.011, General Powers and Duties; THSC, §382.012, State Air Control Plan; THSC, §382.017, Rules; and Texas Water Code (TWC), §5.102, General Powers; and TWC, §5.105, General Policy.

Federal authority: FCAA, §§172(e), 182(d)(3), (e), and (f); and 185.

Effect on the:

A.) Regulated community:

The FCAA, §185 penalty fee is imposed exclusively on the regulated community, those major stationary sources that are in a severe or extreme nonattainment area that has failed to attain the ozone NAAQS. At this time, only the HGB one-hour ozone area has failed to attain the standard by its 2007 deadline; therefore, it is the only area in the state that is

¹ *Guidance on Establishing Emissions Baselines under Section 185 of the Clean Air Act (CAA) for Severe and Extreme Ozone Nonattainment Areas that Fail to Attain the 1-hour Ozone NAAQS by their Attainment*

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subject to the FCAA, \$185 fee requirement in Texas. While as many as 260 HGB-area major stationary sources emitting VOC and NO_x emissions would be directly affected by this rulemaking to comply with the FCAA, \$185 fee requirement, this rulemaking provides those affected sources with flexibility to meet the fee requirement.

An affected source will be charged a penalty fee for every ton of VOC, NO_x, or both (depending on the pollutants for which the source is considered major) that exceeds 80% of the baseline established as part of this rulemaking. A baseline amount is based on the lower of actual emissions or authorized emissions for the 2007 attainment year. This rulemaking provides flexibility in determining a baseline for affected sources that are cyclic, irregular, or have significantly varying emissions. Specifically, a source that is not an electric utility steam generating unit (EGU) would be able to use a historical time period of ten years to determine its baseline, and a source that is an EGU would be able to use a historical time period of five years.

In addition to providing flexibility in determining a source's baseline, this rulemaking also provides equivalent alternative programs that may offset a portion of the area's total annual FCAA, \$185 fee requirement and allows an affected source to offset its annual fee through relinquishing emissions reduction credits or through participation in a SEP. In order to benefit from this flexibility, a source is required to comply with certain program deadlines, which include the baseline determination due date of 120 days after the rule is effective, the annual July 31 deadline for reporting fee offsets, and the annual December fee invoice date.

The first fee would be calculated using the 2012 emissions inventory. However, because this inventory is not yet available, a potential fiscal impact was calculated based on 2010 emissions and the \$8,967 per ton rate applicable to the 2010 emissions. Depending upon the aggregation options chosen by individual regulated entities, this penalty fee could generate revenue up to \$90 million without any TERP and LIRAP/LIP funds used to offset the area's fee obligation. If no TERP and LIRAP/LIP funds are available, then the potential fiscal impact could be as high as \$7.4 million for an affected source, with an average fee between \$266,000 and \$347,000 if not reduced by an equivalent obligation.

B.) Public:

Citizens may be impacted if companies, to account for FCAA \$185 fee obligations, further reduce emissions to reduce fee obligations, raise prices for goods and services, or curtail or cease operations.

C.) Agency programs:

Staff would be required to review and enter baseline amount information into a database. The most significant effort would be undertaken in the first two years of the program to establish the initial baseline amount, develop reporting forms and processes, develop fee reporting processes, and develop database requirements. Most of this effort would be required of staff from the Emissions Assessment Section of the Air Quality Division. Additional effort would be required from the Air Quality Division to verify that sites have

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the banking allowances that they choose to relinquish to offset their fee obligation and determine the quantity of TERP funds available in the HGB area and LIRAP/LIP revenue collected in the HGB area. Ongoing support would be required of staff from the Emissions Assessment Section to verify, update, and maintain baseline amount emissions and annual fee assessments for as long as an area remains subject to the fee. Support would be required from the Financial Administration Division of the Office of Administrative Services to undertake the fee billing process, and support from the Information Resources Division in the Office of Administrative Services would be needed for modification of an existing database to support the adopted program. Staff from the Office of Legal Services, the Office of Compliance and Enforcement, and the Office of Air would be required for review of additional SEPs undertaken to offset a fee obligation.

Stakeholder meetings:

No stakeholder meetings were held in association with this rulemaking; however, two stakeholder meetings were held during the 2009 proposal, March 4, 2009 and June 12, 2009. A number of stakeholders at those meetings requested flexibility in calculating baseline amounts, options to offset the fee amount, and starting the first fee based on emissions after the adoption of the rulemaking. A number of other stakeholders emphasized the penalty nature of the fee and did not support alternative options to a simple fee program. During development of this current rulemaking, a number of stakeholders requested and participated in meetings with commission staff. In addition to reiterating their desire for flexibility, stakeholders representing regulated sources also requested that the fee program cease in an expeditious manner based on any action by the EPA ending the program, after the HGB area monitors attainment for the one-hour ozone standard or allow the fee to be placed in abeyance by the executive director if the design value demonstrates attainment of the one-hour ozone standard. This rulemaking allows equivalent alternative options as well as other flexible elements for use by sources affected by the FCAA, §185 fee requirement.

Public comment:

Comments were received from the EPA, eight companies (including one consulting company), seven industry groups, four environmental groups and 487 public citizens. Of the public citizen comments, there were 460 form letters (80 of which contained additional comments to those in the original form letter). All comments received from public citizens and environmental groups were generally opposed to the proposed rules. EPA submitted comments that supported some aspects of the proposed rules and suggested changes for those aspects of the rules it did not support. All other comments, those received from affected sources and groups representing affected sources, generally supported the rulemaking. Changes were made to the rules as a result of some of the comments received.

The most significant issues addressed in the comments on this rulemaking involve the flexibility offered in determining a source's baseline; limiting the use of TERP and LIRAP/LIP offsets to annual, area expenditures or allocations rather than annual revenue collected from the area; and abeyance of the fee by the executive director. Commenters also suggested that the HGB area be recognized as attaining the one-hour ozone standard

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but for exceptional events (e.g., wildfires) and/or foreign transport. This would preclude the need to implement a one-hour ozone \$185 fee program for the area. Other significant comments received include the following.

- The vehicle inspection and maintenance program (I/M) revenue is not surplus to the HGB one-hour ozone SIP, thus it cannot be used as an alternative revenue source.
- The penalty fees may not be placed in abeyance by the TCEQ upon the submittal of data demonstrating compliance with the revoked standard, but they would continue to be due annually until an action is undertaken by the EPA to end the fee.
- The design value may exclude days submitted by the executive director that exceeded the NAAQS because of exceptional events.
- A company may not use revenue from a SEP to offset the fee if the project is used to offset an enforcement penalty.
- MSS allowable emissions may not be included in the baseline amount because they are dependent upon an earlier state rule that was disapproved.
- A company that selects a baseline year other than 2007 must adjust the baseline emissions amount downward to reflect any legally enforceable emissions limits applicable to the source by 2007. The source must also adjust the baseline amount in consideration of any NO_x or highly-reactive VOC emission allowances held by the source in 2007.

Significant changes from proposal:

Removal of Consideration of MSS Emissions in Baseline Amount Determination - Under the proposal, staff recommended adding language that allowed MSS emissions permitted after the attainment date be considered if the permit was issued according to §101.222 and if the emissions were reported in the emissions inventory for the attainment year. EPA stated it could not support a rule that relied on a rule section that it had disapproved. As a result, this recommendation was removed.

Removal of Using Inspection and Maintenance (I/M) Fees in Fee Equivalency Account - Under the proposal, staff recommended using the I/M revenue collected from the HGB one-hour ozone area in the Fee Equivalency Account. EPA and some stakeholders commented that the I/M program is a component of the HGB one-hour SIP revision and cannot be used as an equivalent program. However, the EPA suggested that the LIRAP portion of the revenue might be considered surplus to the SIP. As a result, staff removed crediting the Fee Equivalency Account with the entire I/M revenue and only used the LIRAP/LIP portion of the revenue from the HGB area. The Fee Equivalency Account would also be credited with revenue beginning in 2012.

Withdrawal of proposed §101.119 - The EPA commented that the proposed rule language specifically exempting sources from paying a \$185 Failure to Attain fee during any year that was determined to be an extension year was not necessary because the one-hour standard has been revoked. This section was removed as a result of this comment.

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Potential controversial concerns and legislative interest:

EPA has not provided final on alternative methods to meet fee obligations guidance after the revocation of its 2010 guidance. These rules include equivalent alternatives to the fee requirements outlined in FCAA, §185 under FCAA, §172(e). However, the EPA has signaled, through approving the San Joaquin Valley's (SJV) rule (77 FedReg 50021) and the South Coast Air Quality Management (SCAQMD) rules (77 FedReg 7432) in California, that it would accept on a case-by-case basis alternative options to obligating major sources to pay the penalty fee. The approved SJV rule assesses a fee on mobile sources. For its FCAA, §185 fee program, the SCAQMD assigns an equivalent fee from programs surplus to the one-hour ozone SIP. That equivalent option is used to offset the fee obligation of major stationary sources. In the SCAQMD case, sufficient funding is allocated from alternative programs to fully offset the fee obligation.

For 2012, \$40 million was identified from HGB-area TERP revenue that may be used to partially offset the area's §185 fee obligation. An additional \$18 million was collected from HGB-area motorists for LIRAP/LIP. These alternative options are supported by staff; however, they are not expressly required by federal rule and could be denied by the EPA. Other concerns include the following.

- *Timing of the First Fee* - According to FCAA, §185, an affected area's penalty fee would be assessed beginning the calendar year after the nonattainment area's unmet attainment date. Although the attainment deadline for the HGB one-hour ozone nonattainment area was November 15, 2007, these rules set the beginning of fee assessment after rule adoption using the 2012 emissions inventory, which would be the most current. This year was selected because assessing the fee for years prior to adoption of this rulemaking could lead parties to challenge it as a retroactive rulemaking. A number of commenters did argue, however, that the retroactivity issue is misplaced and that the statute indicates that fee assessment should begin for the year following attainment.
- *Termination of the Fee* - The FCAA requires the fee to be paid until the area is redesignated as attainment; however, when the one-hour ozone standard was revoked, the EPA stated that it will no longer designate areas under that standard. This rulemaking would allow the fee program to be terminated upon redesignation to attainment, upon a finding of attainment by the EPA, or upon any other action by the EPA to end the fee program. In addition, this rulemaking gives the executive director the discretion to hold collection of the penalty fee in abeyance from the time that certified clean data are submitted to the EPA demonstrating attainment until the EPA publishes a finding.
- *Additional Baseline Amount Flexibility* - These rules allow sites under common control to aggregate baseline amounts for VOC, NO_x, or both. Aggregation allows consistency for companies that heavily reduced emissions at one site or for one ozone precursor to cost effectively reduce ozone in support of the one-hour ozone

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SIP objectives. However, aggregation is not supported by some environmental groups because it may reduce fees.

- *TERP/LIRAP Appropriations* – The potential impact of TERP/LIRAP appropriation on alternative revenue credit has been of interest to elected officials and stakeholders during the legislative session.

Does this rulemaking affect any current policies or require development of new policies?

To implement these rules, procedures must be developed for determining the annual fee amount and for collection and maintenance of program-related data. It is expected that staff from the Financial Administration Division of the Office of Administrative Services would bill the affected stationary sources and collect the revenue.

What are the consequences if this rulemaking does not go forward? Are there alternatives to rulemaking?

If the state does not collect the fees that are due, then under FCAA §185(d), the EPA must collect the fees and may collect interest. Fees and interest would not be returned to the state.

Key points in the adoption rulemaking schedule:

***Texas Register* proposal publication date:** November 30, 2012

Anticipated *Texas Register* publication date: June 7, 2013

Anticipated effective date: June 13, 2013

Six-month *Texas Register* filing deadline: May 30, 2013

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