Form: TH- 03

Virginia Regulatory Town Hall

Final Regulation
Agency Background Document

Agency Name:	State Air Pollution Control Board
Regulation Title:	Regulation for Emissions Trading
Primary Action:	9 VAC 5 Chapter 140 (9 VAC 5-140-10 et seq.)
Secondary Action(s):	None
Action Title:	NO_X Emissions Budget Trading Program (Rev. D98)
Date:	May 28, 2002

Please refer to the Administrative Process Act (§ 2.2-4000 et seq. of the Code of Virginia), Executive Order Twenty-Five (98), and the Virginia Register Form, Style and Procedure Manual for more information and other materials required to be submitted in the final regulatory action package.

Summary

Please provide a brief summary of the new regulation, amendments to an existing regulation, or the regulation being repealed. There is no need to state each provision or amendment or restate the purpose and intent of the regulation.

The regulation establishes a NO_X Budget Trading Program as a means of mitigating the interstate transport of ozone and nitrogen oxides including the following provisions: permitting allowance methodology, monitoring, banking, compliance supplement pool, compliance determination and opt-in provisions for sources not covered by the regulation.

Beginning May 31, 2004, electric generating units with a nameplate capacity greater than 25 MWe and non-electric generating units above 250 mmBtu will be subject to the provisions of the regulation. NO_X emissions from subject units shall be subject to a specific limited budget (measured in tons) during the summer months of May 1 through September 31, otherwise know as the control period. The NO_X budget shall be determined through a methodology based upon emission rates multiplied by heat input. If a unit does not use all of it's allowances for a specific control period, those extra tons may be banked for future use or sold. If a unit exceeds the budget limit, additional allowances may be purchased or the source may use banked allowances to offset the amount of NO_X generated above the budget limit.

An allocation set-aside budget is available to accommodate new sources that receive permits and commence operation after the distribution to the qualifying units (those in operation at least two years before the distribution date).

Emissions will need to be monitored according to 40 CFR Part 75 for all sources subject to the regulation and for any sources wishing to opt-in to the program.

A compliance supplement pool is provided for sources that generate early reduction credits or demonstrate “undue risk”. The allowances from the pool are good for only two years and cannot be banked after that two-year period.

Substantial Changes Made Since the Proposed Stage

Please briefly and generally summarize any substantial changes made since the proposed action was published. Please provide citations of the sections of the proposed regulation that have been substantially altered since the proposed stage.

- The applicability definitions and criteria have been changed to use the provisions from 40 CFR Part 97 for non-EGUs, as opposed to those found in 40 CFR Part 96. [9 VAC 5-140-20 and 40 A]

- The 25 ton exemption has been changed to limit its use to only those units that burn gas or oil and to use the allocation methodology in 40 CFR Part 97 to allocate allowances. [9 VAC 5-140-40 B]

- The values of the emissions budgets for both EGUs and non-EGUs and the compliance supplement pool have been changed to use the EPA numbers from 40 CFR Part 97. [9 VAC 5-140-910, 920 and 930]

- The method for promulgating the emissions budget for EGUs and the compliance supplement pool has been changed to incorporate the EPA numbers (from 40 CFR Part 97) by reference, as opposed to including the budget numbers in the regulation. [9 VAC 5-140-910 and 920]

- The initial allocations for the individual units are not included in the regulation. The initial and subsequent allocations will be accomplished outside the regulatory process. [9 VAC 5-140-940 and 950]

- The allocation periods have been changed to use the periods in 40 CFR Part 97, as opposed to the initial allocation period of ten years and subsequent period of one year. 40 CFR Part 97 provides the same initial and subsequent allocation periods (five years) for both EGUs and non-EGUs. [9 VAC 5-140-410 A through C and 420 A through C]

- The basis for the allocations for new sources (those commencing operation after May 1, 1998) has been changed to provide that the allocation be based on the lesser of the most stringent state or federal emission limitation or the core emission rate, as opposed to the lesser of the permit limit or core emission rate. In cases where a unit is subject to a permit which provides for the use of multiple fuels, the primary fuel shall be used as the basis to determine the most stringent state or federal NO_X emissions limitation. [9 VAC 5-140-20 and 420 B, C and D]

- Provisions for a new source allocation set aside for have been added to the regulation. The set aside is formed by withholding allowances from both (EGU and non-EGU) source categories. The set aside from the EGU budget is five percent for the years

2004 through 2008 and two percent for the years 2009 & later. The set-aside from the non-EGU budget is the difference between the sum of the initial allocations for the individual units and the non-EGU emissions budget in 40 CFR Part 97. [9 VAC 5-140-20 and 420 D and E]

- The methodology in 40 CFR Part 97 is used for distribution of the new source set-asides for both EGUs and non-EGUs. Although the set aside comes from the emissions budget for each of the two source categories, there is only one set-aside that may be distributed to any unit regardless of source category. The set-aside is distributed pro-rata to all requesting a portion of the set-aside. This provides a system whereby any unit is eligible for the set-aside if it did not receive an initial allocation and was issued a first time permit prior to January 1 of the year of distribution of the set-asides. EPA will confiscate the allocations for any control period, or portion thereof, during which the unit does not operate. [9 VAC 5-140-420 D, E and F]

- The regulation (which is based on 40 CFR Part 96) has been changed to be consistent with some of the more flexible provisions of 40 CFR Part 97. [throughout]

Statement of Final Agency Action

Please provide a statement of the final action taken by the agency, including the date the action was taken, the name of the agency taking the action, and the title of the regulation.

On May 21, 2002, the State Air Pollution Control Board adopted a final regulation entitled "Regulation for Emissions Trading" (9 VAC 5 Chapter 140). The regulation is to be effective as provided in § 2.2-4012 B of the Code of Virginia.

Basis

Please identify the section number and provide a brief statement relating the content of the statutory authority to the specific regulation adopted. Please state that the Office of the Attorney General has certified that the agency has the statutory authority to adopt the regulation and that it comports with applicable state and/or federal law.

Section 10.1-1308 of the Virginia Air Pollution Control Law (Title 10.1, Chapter 13 of the Code of Virginia) authorizes the State Air Pollution Control Board to promulgate regulations abating, controlling and prohibiting air pollution in order to protect public health and welfare. Section 10.1-1322.3 of the Code of Virginia indicates that the Board may promulgate regulations to provide for an emissions trading program to achieve and maintain the NAAQS. The banking and trading program shall result in net air emission reductions, create economic incentive for reducing air emissions and allow for economic growth. In developing the regulations, the Board shall consider (i) the definition and use of emissions reduction credits from mobile and stationary sources, (ii) offsets, (iii) interstate or regional trading, (iv) mechanisms needed to facilitate trading and banking, and (v) emissions allocations. However, no regulation shall prohibit the direct trading of credits or allowances between private industries provided such trades do not adversely

impact air quality in Virginia. Written assurance from the Office of the Attorney General that (i) the State Air Pollution Control Board possesses the statutory authority to promulgate the proposed regulation and that (ii) the proposed regulation comports with the applicable state and/or federal law is available upon request.

Purpose

Please provide a statement explaining the rationale or justification of the regulation as it relates to the health, safety or welfare of citizens.

The purpose of the regulation is to establish general provisions addressing applicability, permitting, allowance allocation, excess emissions, monitoring, and opt-in provisions to create a Virginia NO_X Budget Trading Program as a means of mitigating the interstate transport of ozone and nitrogen oxides in order to protect public health and welfare. The regulation is being proposed to create an enforceable mechanism to assure that collectively, all affected sources will not exceed the total NO_X emissions budget established by regulation for the year 2007 ozone season and to provide the regulatory basis for a program under which the creation, trading (buying and selling) and registering of emission credits can occur.

Substance

Please identify and explain the new substantial provisions, the substantial changes to existing sections, or both where appropriate. Please note that a more detailed discussion is required under the statement providing detail of the changes.

1. The regulation applies to electric generating units (EGUs) with a nameplate capacity greater than 25 MWe and non-electric generating units (non-EGUs) above 250 mmBtu, hereafter referred to as the core source categories. A “unit” is defined as a fossil fuel-fired stationary boiler, combustion turbine, or combined cycle system.

2. Core source units smaller than 25 tons per control period (t/cp) that burn gas or oil are exempt.

3. State wide NOx emissions budgets for both EGUs (17,091 t/cp) and non-EGUs (4,104 t/cp) are included, derived from the EPA numbers in 40 CFR Part 97.

4. Sources must be in compliance by May 31, 2004. Trading is allowed anywhere in EPA’s NOx emissions trading domain. A unit’s emissions during the control period cannot exceed the number of allowances in its account. A true up takes place at the end of each control period.

5. Initial allocations for core source categories are based on the baseline heat input multiplied by the core emission rate normalized over the state budget. The core emission rate for EGUs is 0.15 lb/mmBtu; for non-EGUs, 0.17 lb/mmBtu. The baseline

heat input (used to calculate allocations) for existing core sources is determined by averaging the two highest years of the immediate preceding 5 years.

6. Initial allocations for units in operation on May 1, 1998 are issued on July 1, 2002 for the control periods 2004 - 2008.

7. Subsequent allocations are issued every five years beginning April 1, 2006 for a block of five control periods.

8. Provisions for a new source allocation set aside are included. The set aside is formed by withholding allowances from both (EGU and non-EGU) source categories. The set aside from the EGU budget is five percent (855 t/cp) for the years 2004 through 2008 and two percent (342 t/cp) for the years 2009 & later. The set-aside from the non-EGU budget is the difference between the sum of the initial allocations for the individual units and the non-EGU emissions budget (1,000 t/cp).

9. The methodology for distribution of the new source set-asides for both EGUs and non-EGUs is included. Although the set aside comes from the emissions budget for each of the two source categories, there is only one set-aside that may be distributed to any unit regardless of source category. The set-aside is distributed pro-rata to all requesting a portion of the set-aside. This provides a system whereby any unit is eligible for the set-aside if it did not receive an initial allocation and was issued a first time permit prior to January 1 of the year of distribution of the set-asides. EPA will confiscate the allocations for any control period, or portion thereof, during which the unit does not operate.

10. Baseline allocations for new sources (commencing operation after May 1, 1998) are based on the more stringent of the core emission rate or the most stringent state or federal emissions limitation. In cases where a unit is subject to a permit which provides for the use of multiple fuels, the primary fuel shall be used as the basis to determine the most stringent state or federal NO_X emissions limitation.

11. Sources may bank or trade any allowances not used during a specific control period.

12. A compliance pool is established which allows for allocations from the pool for early reductions and on a "needs" basis. Allocations from the pool (5,504 tons) will be distributed to the sources prior to May 1, 2004. Allocations from the pool are valid for two years (2004 and 2005).

13. Smaller sources within the core source categories are not mandated to be included in the program; however, smaller sources within the core source categories are allowed to opt-in to the program. Sources that opt-in the program have a separate budget. Baseline determined for opt-ins is based upon the previous year's emissions.

14. All sources participating in the program, including those that chose to opt-in, must meet the monitoring requirements of 40 CFR Part 75 of the Code of Federal Regulations.

15. Sources found to be out of compliance will be forced to surrender allowances for the next year on a ratio of 3:1, i.e. for every ton over their budget, three tons will be forfeited from the next year's allocation.

Issues

Please provide a statement identifying the issues associated with the regulatory action. The term "issues" means: 1) the primary advantages and disadvantages to the public of implementing the new or amended provisions; and 2) the primary advantages and disadvantages to the agency or the Commonwealth. If there are no disadvantages to the public or the Commonwealth, please include a sentence to that effect.

1. Public: The primary advantage to the general public is that air quality will improve through a program designed to maximize market forces to reduce pollution in the most cost-effective manner. The cost of compliance is a key issue for the citizens of the Commonwealth since the utility industry is affected by this regulation. If the cost of control is excessive, the additional costs may be passed on to the consumer in the form of rate hikes.

This regulation provides for the trading of NO_X allowances to offset the cost of compliance. This approach provides more flexibility for compliance options for the sources affected while still protecting air quality. A compliance demonstration is required at the end of the ozone season. Sources must demonstrate that they have operated equipment such that the NO_X emissions are either equal to or below the allocations. Tons of NO_X may be purchased or sold according to the need of the source owner; NO_X credits can also be generated as early reduction credits or the source may choose to bank credits to be used for compliance demonstrations in future years. Sources not subject to the regulation may participate in the program as opt-in sources provided specific conditions are met.

Disadvantages to the regulated sources are in the areas of costs for control and monitoring. Sources will need to monitor emissions with continuous emission monitors (CEMs). If sources do not currently have CEMs they will need to install the monitoring equipment to participate in the program. The total state budget for NO_X allowances may not be sufficient to meet the needs if all sources were operating at maximum capacity. Some sources may need to install control equipment. In addition, new sources may need to purchase NO_X allowances for several years until they are included into the allocation system as the regulation provides only a limited set-aside budget for new sources.

2. Department: The advantages for the Department are in the area of effective compliance and reduced inspections. The regulation provides procedures for continuous or process parameter monitoring of emissions for determining compliance with the NO_X emissions standard. This will result in very accurate data to be used for compliance demonstrations or enforcement actions when necessary. EPA will

administer the trading and banking aspects of the regulation thereby avoiding any additional costs that would be associated with that activity.

Disadvantages include the need for the Department to review the compliance demonstrations and monitoring plans. More time may be involved if a source chooses to utilize early reduction credits (ERCs), credits from other states or banked credits. Every five years a new NO_X allocation will need to be computed and distributed. Each year a new NO_X allocation will need to be computed and distributed for new sources. The new NO_X allocations will need to be incorporated into either the source's Title V permit at the appropriate time.

Public Comment

Please summarize all public comment received during the public comment period and provide the agency response. If no public comment was received, please include a statement indicating that fact.

A summary and analysis of the public testimony, along with the basis for the decision of the Board, is attached. The summary and analysis addresses those comments received pursuant to the opportunity for oral and written comments under § 2.2-4007 J of the Code of Virginia.

Detail of Changes

Please detail any changes, other than strictly editorial changes, made since the publication of the proposed regulation. This statement should provide a section-by-section description of changes.

1. Article 1 establishes the general provisions covering the NO_X budget trading program, specifically: purpose; definitions; measurements, abbreviations, and acronyms; applicability; retired unit exemptions; standard requirements; and computation of time.

- The 25 ton exemption has been changed to limit its use to only those units that burn gas or oil and to use the allocation methodology in 40 CFR Part 97 to allocate allowances.

- The applicability definitions and criteria have been changed to use the provisions from 40 CFR Part 97 for non-EGUs, as opposed to those found in 40 CFR Part 96.

2. Article 2 establishes the provisions covering NO_X authorized account representatives for NO_X budget sources, specifically: authorization and responsibilities of the authorized account representatives; alternate authorized account representatives; changing the authorized account representative and the alternate authorized account representative; changes in the owners and operators; account certificate of representation; and objections concerning the authorized account representative.

3. Article 3 establishes the provisions covering NO_X budget permits, specifically: general permit requirements; submission of permit applications; information requirements for the permit applications; permit contents; effective date of initial permits; and permit revisions.

4. Article 4 establishes the provisions covering compliance certification, specifically: compliance certification reports; and action of the board and EPA on compliance certifications.

5. Article 5 establishes the provisions covering NO_X allowance allocations, specifically: state trading program budget; timing requirements for allowance allocations; allowance allocations; and compliance supplement pool.

- The allocation periods have been changed to use the periods in 40 CFR Part 97, as opposed to the initial allocation period of ten years and subsequent period of one year. 40 CFR Part 97 provides the same initial and subsequent allocation periods (five years) for both EGUs and non-EGUs.

- The basis for the allocations for new sources (those commencing operation after May 1, 1998) has been changed to provide that the allocation be based on the lesser of the most stringent state or federal emission limitation or the core emission rate, as opposed to the lesser of the permit limit or core emission rate. In cases where a unit is subject to a permit which provides for the use of multiple fuels, the primary fuel shall be used as the basis to determine the most stringent state or federal NO_X emissions limitation.

- Provisions for a new source allocation set aside for have been added to the regulation. The set aside is formed by withholding allowances from both (EGU and non-EGU) source categories. The set aside from the EGU budget is five percent for the years 2004 through 2008 and two percent for the years 2009 & later. The set-aside from the non-EGU budget is the difference between the sum of the initial allocations for the individual units and the non-EGU emissions budget in 40 CFR Part 97.

- The methodology in 40 CFR Part 97 is used for distribution of the new source set-asides for both EGUs and non-EGUs. Although the set aside comes from the emissions budget for each of the two source categories, there is only one set-aside that may be distributed to any unit regardless of source category. The set-aside is distributed pro-rata to all requesting a portion of the set-aside. This provides a system whereby any unit is eligible for the set-aside if it did not receive an initial allocation and was issued a first time permit prior to January 1 of the year of distribution of the set-asides. EPA will confiscate the allocations for any control period, or portion thereof, during which the unit does not operate.

6. Article 6 establishes the provisions covering the NO_X allowance tracking system, specifically: allowance tracking system accounts; establishment of accounts;

responsibilities of authorized account representatives; recordation of allowance allocations; compliance; banking; account error; and closing of general accounts.

7. Article 7 establishes the provisions covering NO_X allowance transfers, specifically: scope and submission of allowance transfers; EPA recordation; and notification.

8. Article 8 establishes the provisions covering monitoring and reporting, specifically: general requirements; initial certification and recertification procedures; out of control periods; notifications; recordkeeping and reporting; petitions; and additional requirements to provide heat input data for allocations purposes.

- Some of the less burdensome provisions of 40 CFR Part 97 have been incorporated.

9. Article 9 establishes the provisions covering individual NO_X unit opt-ins, specifically: applicability; general; authorized account representative; applying for budget opt-in permit; opt-in process; budget opt-in permit contents; withdrawal from NO_X budget trading program; change in regulatory status; and allowance allocations to opt-in units.

10. Article 10 establishes the tons per control period of NO_X allowances and credits for the state trading program budget and compliance pool, specifically: state trading program budget allowances; compliance supplement pool credits; total electric generating unit allowance allocations; total non-electric generating unit allowance allocations; individual electric generating unit allowance allocations; and individual non-electric generating unit allowance allocations.

- The values of the emissions budgets for both EGUs and non-EGUs and the compliance supplement pool have been changed to use the EPA numbers from 40 CFR Part 97.

- The method for promulgating the emissions budget for EGUs and the compliance supplement pool has been changed to incorporate the EPA numbers (from 40 CFR Part 97) by reference, as opposed to including the budget numbers in the regulation.

- The initial allocations for the individual units are not included. The initial and subsequent allocations will be accomplished outside the regulatory process.

11. Throughout:

- The regulation (which is based on 40 CFR Part 96) has been changed to be consistent with the more flexible provisions of 40 CFR Part 97.

Family Impact Statement

Please provide an analysis of the regulatory action that assesses the impact on the institution of the family and family stability including the extent to which the regulatory action will: 1) strengthen or erode the authority and rights of parents in the education, nurturing, and supervision of their children; 2) encourage or discourage economic self-sufficiency, self-pride, and the assumption of responsibility for oneself, one's spouse, and one's children and/or elderly parents; 3) strengthen or erode the marital commitment; and 4) increase or decrease disposable family income.

It is not anticipated that this regulation will have a direct impact on families. However, there will be positive indirect impacts in that the regulation will ensure that the Commonwealth's air pollution control regulations will function as effectively as possible, thus contributing to reductions in related health and welfare problems.

**COMMONWEALTH OF VIRGINIA
STATE AIR POLLUTION CONTROL BOARD**

**SUMMARY AND ANALYSIS OF PUBLIC TESTIMONY FOR
REGULATION REVISION D98
CONCERNING**

**EMISSIONS TRADING, VIRGINIA NOX BUDGET TRADING PROGRAM
(9 VAC 5 CHAPTER 140)**

INTRODUCTION

On July 16, 2001, the Board published for public comment a proposal to adopt a regulation concerning Emissions Trading, Virginia NOx Budget Trading Program. In response to that request, comments were submitted that resulted in several changes being made to the original proposal, primarily to meet new legislative changes. On February 27, 2002, the Board adopted the final regulation concerning Emissions Trading, Virginia NOx Budget Trading Program, with an effective date consistent with the Administrative Process Act. The final regulation as adopted was published in the Virginia Register on March 25, 2002. Because of the substantive nature of these additional changes, the proposal was reopened for public comment on those changes to the final regulation.

A public meeting was advertised accordingly and held in Richmond on April 24, 2002 and the public comment period closed on the same day. The substantive changes made to the proposed regulation subject to the meeting are summarized below followed by a summary of the public participation process and an analysis of the public testimony, along with the basis for the decision of the Board.

SUMMARY OF CHANGES TO ORIGINAL PROPOSAL

Below is a brief summary of the substantive changes made to the original proposal.

1. The applicability definitions and criteria have been changed to use the provisions from 40 CFR Part 97 for non-EGUs, as opposed to those found in 40 CFR Part 96. [9 VAC 5-140-20 and 40 A]

2. The 25 ton exemption has been changed to limit its use to only those units that burn gas or oil and to use the allocation methodology in 40 CFR Part 97 to allocate allowances. [9 VAC 5-140-40 B]

3. The values of the emissions budgets for both EGUs and non-EGUs and the compliance supplement pool have been changed to use the EPA numbers from 40 CFR Part 97. [9 VAC 5-140-910, 920 and 930]

4. The method for promulgating the emissions budget for EGUs and the compliance supplement pool has been changed to incorporate the EPA numbers (from 40 CFR Part 97) by reference, as opposed to including the budget numbers in the regulation. [9 VAC 5-140-910 and 920]

5. The initial allocations for the individual units have been removed from the regulation. The initial and subsequent allocations will be accomplished outside the regulatory process. [9 VAC 5-140-940 and 950]

6. The allocation periods have been changed to use the periods in 40 CFR Part 97, as opposed to the initial allocation period of ten years and subsequent period of one year. 40 CFR Part 97 provides the same initial and subsequent allocation periods (five years) for both EGUs and non-EGUs. [9 VAC 5-140-410 A through C and 420 A through C]

7. The basis for the allocations for new sources (those commencing operation after May 1, 1998) has been changed to provide that the allocation be based on the lesser of the most stringent state or federal emission limitation or the core emission rate, as opposed to the lesser of the permit limit or core emission rate. In cases where a unit is subject to a permit which provides for the use of multiple fuels, the primary fuel shall be used as the basis to determine the most stringent state or federal NO_X emissions limitation. [9 VAC 5-140-20 and 420 B, C and D]

8. Provisions for a new source allocation set aside for have been added to the regulation. The set aside is formed by withholding allowances from both (EGU and non-EGU) source categories. The set aside from the EGU budget is five percent for the years 2004 through 2008 and two percent for the years 2009 & later. The set-aside from the non-EGU budget is the difference between the sum of the initial allocations for the individual units and the non-EGU emissions budget in 40 CFR Part 97. [9 VAC 5-140-20 and 420 D and E]

9. The methodology used for distribution of the new source set-asides for both EGUs and non-EGUs in 40 CFR Part 97 has been added. Although the set aside comes from the emissions budget for each of the two source categories, there is only one set-aside that may be distributed to any unit regardless of source category. The set-aside is distributed pro-rata to all requesting a portion of the set-aside. This provides a system whereby any unit is eligible for the set-aside if it did not receive an initial allocation and was issued a first time permit prior to January 1 of the year of distribution of the set-asides. EPA will confiscate the allocations for any control period, or portion thereof, during which the unit does not operate. [9 VAC 5-140-420 D, E and F]

10. The regulation (which is based on 40 CFR Part 96) has been changed to be consistent with some of the more flexible provisions of 40 CFR Part 97. [throughout]

SUMMARY OF PUBLIC PARTICIPATION PROCESS

A public meeting was held in Richmond, Virginia on April 24, 2002. Five persons attended the meeting, with none of those offering testimony; and four written comments were received during the public comment period. As required by law, notice of this meeting was given to the public on or about March 25, 2002 in the Virginia Register. In addition, personal notice of this meeting and the opportunity to comment was given by mail to those persons on the Department's list to receive notices of proposed regulation revisions. A list of meeting attendees and the complete text or an account of each person's testimony is included in the meeting report which is on file at the Department.

ANALYSIS OF TESTIMONY

Below is a summary of each person's testimony and the accompanying analysis. Included is a brief statement of the subject, the identification of the commenter, the text of the comment and the Board's response (analysis and action taken). Each issue is discussed in light of all of the comments received that affect that issue. The Board has reviewed the comments and developed a specific response based on its evaluation of the issue raised. The Board's action is based on consideration of the overall goals and objectives of the air quality program and the intended purpose of the regulation.

1. **SUBJECT:** Support for the regulation

COMMENTER: Leonard R. Dupuis, Manager, Environmental Policy, Dominion Generation

TEXT: Dominion supports the Department of Environmental Quality's (DEQ) actions it has taken to amend the portions of the Virginia NOx SIP rule as it relates to electric generating units (egu's) in order to incorporate the changes to the Code of Virginia mandated by the State Legislature (during the 2001 legislative session), and to address EPA concerns with the rule that may have resulted in an EPA disapproval of the rule. We also support the NOx allowance allocation methodology and unit-specific allocations related to electric generating units proposed in the March 25th notice. We believe these actions will allow the State to finalize its NOx SIP rule and to submit a timely and approvable Virginia NOx SIP revision to U.S. EPA. Accordingly, we urge the DEQ to proceed with the NOx SIP rule as currently proposed as expeditiously as possible.

RESPONSE: Support for the regulation is appreciated.

2. **SUBJECT:** Inadequate allocation

<u>COMMENTER</u>: Thomas W. Kinnane and the law firm of Kinnane & Associates, Ltd., and Andrew N. Chau, Regulatory Counsel, Tractebel North America

<u>TEXT</u>: The Hopewell Cogeneration Facility ("Hopewell" or "the facility") is a 365 MW combined cycle, cogeneration facility located in Hopewell, Virginia, and is owned and operated by Tractebel. Hopewell produces electricity for Dominion Virginia Power ("DVP"), and steam for use by a subsidiary of Hercules Chemical in its manufacturing operations. Hopewell is fully dispatchable; that is, DVP determines the operation of the power facility. Hopewell contributes approximately $12 million annually to the Hopewell-area economy, and serves the energy needs of approximately 250,000 households.

The facility operates three ABB-Type 11N Combustion Turbines with steam injection for NOx control. Per the facility's permit (No. PRO-50967) each combustion turbine is allowed to emit up to 675.6 tons per year while burning natural gas, and 1,036.9 tons per year while burning No. 2 fuel oil. As part of the NOx Emissions Trading Budget Program described in the proposed regulation, 9 VAC 5-140, Hopewell has been allocated 200 tons of NOx allowance for the three combustion turbines combined, which is less than 24% of the permitted allowance solely when burning natural gas. The inadequate allocation represents a significant operational impact and cost to the facility.

<u>RESPONSE</u>: The federal NOx Budget Trading is designed so that a 60 percent reduction from 1990 baseline emissions is achieved prior to the start of the program. The total NOx state trading budget for EGU units subject to this program has been reduced from approximately 55,000 tons of NOx per season to just over 17,000 tons. All existing sources operating in Virginia are facing significant emissions reductions. That is the point of the program.

The issue of how to distribute the remaining tons to the existing sources has been the focal point of discussion during the entire development of this regulation, which began in 1998. Over three years of work and compromise has resulted in what is believed to be a fair and equitable distribution process. Looking at historical emission data to compute heat input is, currently, the only readily available tool that can be used, more importantly, it is the method chosen through the ad hoc regulation development process.

The federal program, which will be implemented if the state doesn't submit its own program within the designated time frame, only looks at the previous four years. The consensus of the ad hoc group was that some of the volatile ups and downs of production cycles may be alleviated by using a longer widow to evaluate how a source has actually been operating. Therefor, heat input for the Virginia program, will be determined by the average of the two highest years in a five-year period.

The comment that "...Hopewell has been allocated 200 tons of NOx allowance for the three combustion turbines combined, which is less than 24% of the permitted allowance solely when burning natural gas" on the surface appears like a very drastic reduction. However, there is a very big difference between potential to emit, i.e. what is in a permit,

verses how a source actually operates, i.e. the actual emissions. Allocations for the Virginia program are based on actual emissions data, not the potential to emit.

No changes have been made to the regulation based on this comment.

3. **SUBJECT:** Allocation of allowances is discriminatory

COMMENTER: Thomas W. Kinnane and the law firm of Kinnane & Associates, Ltd., and Andrew N. Chau, Regulatory Counsel, Tractebel North America

TEXT: The proposed allocation of allowances is discriminatory and will have an adverse impact on merchant generation in the Commonwealth. Under the proposed regulation, Hopewell's allocations are based on a capacity factor of approximately 15%. Baseload facilities, those formerly regulated generating facilities under the control of utilities or their affiliates, are allocated allowances based on a capacity factor of approximately 80%. Thus, on its face, the proposed allocations are discriminatory.

Moreover, the capacity factor that serves as the basis for credit allocation, at least in the case of the Hopewell facility, fails to incorporate projected increases in demand. Thus, not only is the initial capacity factor inadequate, it becomes more so as time moves forward and demand increases. While such a formula might, arguably, have had some justification in the past, its application in the instant matter is wholly inappropriate. In addition, peaking facilities, like Hopewell, will suffer the greatest adverse impact under the proposed regulation as load growth increases, since such facilities must serve the incremental load over and above baseload generation.

Generation in the Commonwealth is now deregulated. Thus, the construction of additional generation and the recovery of costs therefor are no longer matters of regulatory determination. Generation will be built and operated only to the extent that it is economically justifiable to do so for companies engaged in that business. By permitting formerly regulated generation facilities to obtain NOx allowances based on a particular allocation that will enable them to operate more cost effectively by having to purchase fewer allowances, or to face fewer non-compliance penalties, the Department would in effect be favoring the generation of certain companies over the generation of others. There is no compelling justification for such overt discrimination.

All generation is now on an equal footing with regard to its regulatory treatment and necessity for cost-effective operation. The proposed allocation will eliminate the level playing field upon which generating facilities must operate in the Commonwealth, which will have a detrimental impact on the ability for competitive merchant generation developers to enter the market, to drive down energy prices and support local economies.

RESPONSE: The allocation method in the regulation is not based on some formula to permit some facilities to operate more cost-effectively than others. Nor is the allocation method based upon how a source may operate in the future. The allocation is based on heat-input data of how a source has operated during the previous five year

period. This approach was recommended by the regulatory ad hoc group. Historic heat input is also the used in the federal program. At some future date, a better method may be determined, however, this is the method that will be utilized at this time to assure compliance with the federal program and to avoid federal sanctions.

As stated in the second comment, all existing sources must reduce approximately 60 percent from their 1990 base year emissions. For EGUs, the core rate for allocations will be 0.15 lbs per mm/BTU. This is the rate mandated in the federal program. To meet that rate sources will either reduce emissions through the addition of control technology or the purchase of allowances to meet their emission levels. How a source chooses to operate or whether to operate is solely within the purview of the company.

No changes have been made to the regulation based on this comment.

4. **SUBJECT:** Allocation of allowances is inadequate for dispatchable facilities

COMMENTER: Thomas W. Kinnane and the law firm of Kinnane & Associates, Ltd., and Andrew N. Chau, Regulatory Counsel, Tractebel North America

TEXT: Hopewell is a fully dispatchable facility. In other words, Hopewell has no control over when or how the facility is operated, i.e., 1/3, 2/3 or full capacity, base loaded or on automatic generation control. The facility's operation is determined by DVP, the utility in which the facility is located. Since Hopewell cannot itself determine the needs of DVP, it must operate when dispatched. While Tractebel might otherwise determine when and how to most costeffectively operate the facility, and control its expenditure of NOx allowances, it does not possess this capability as a dispatchable facility.

The proposed regulation does not account for the difference between dispatchable and non-dispatchable units. Non-dispatchable units, which have absolute control over the facility's operation, have a distinct economic and competitive advantage over dispatchable units under the proposed regulation. Non-dispatchable units can operate at different times and for different durations in order to maximize the efficient use of their allocated NOx allowances. Because power demand is expected to increase in the future, Hopewell will likely be dispatched at a much higher rate. The facility's annual capacity factor is expected to increase toward base load levels in coming years, particularly during the summer months. The proposed NOx allocation for the facility is inadequate for anticipated future operations and much less than currently permitted, and will result in a significant operational and financial impact. Under the proposed regulation, the facility will have to purchase a substantial number of NOx allowances or install additional NOx controls at a significant and previously unanticipated cost.

Despite the utilities' reliance upon dispatchabie facilities to provide energy when needed, the proposed regulation does not address the uncertainty associated with the operation of these facilities, and the accompanying inability of such facilities to control, in a rational and cost effective manner, the expenditure of NOx allowances. In addition, the proposed allocations may incent [sic] utilities to shift cost burdens to dispatchable units like

Hopewell, permitting the utilities to conserve NOx allocations for their own baseload facilities. The proposed regulation thus creates a discriminatory and anti-competitive mechanism arising from the potential for utility manipulation of facility dispatch priorities to conserve costs.

RESPONSE: The commenter is correct that that the regulation doesn't take into account the difference between dispatchable and non-dispatchable facilities. Nor does the regulation take into the account the difference between gas-fired and coal-fired facilities. All sources within a specific source category are treated the same.

Following the logic presented by the commenter, one could argue that the regulation is discriminatory to coal-fired facilities because coal-fired facilities will need to reduce more emissions to reach the emission rate of 0.15lbs/mmBtu than gas-fired units. Therefore, some special compensation should be afforded coal facilities. The federal program, and consequently the state program, do not distinguish between types of EGUs nor the fuel they use but rather treats them the same. The source can use the marketplace to determine the best method for achieving the necessary pollution reductions.

In fact, the regulation only looks at past heat input, i.e. past operational history. The heat input is then multiplied by an emissions rate mandated by federal regulation. An allocation for the control period is determined. A source is free to operate above, below or at the allocation limit. The only condition is that at the end of the control period, the source must have sufficient NOx allocations in its budget to cover the amount of NOx emitted during the control period. The methods used to accomplish that are completely at the discretion of the facility.

No changes have been made to the regulation based on this comment.

5. **SUBJECT:** Regulation thwarts federal energy policies

COMMENTER: Thomas W. Kinnane and the law firm of Kinnane & Associates, Ltd., and Andrew N. Chau, Regulatory Counsel, Tractebel North America

TEXT: Among the purposes of the Public Utility Regulatory Policies Act ("PURPA") are to encourage the (i) the optimization of the efficiency of use of facilities and resources by electric utilities; and (ii) equitable rates to electric consumers. (PURPA, 16 USCS § 2611).

The regulation as proposed will thwart the "optimization of the efficiency of use of facilities" and will have the ultimate impact of depriving consumers of "equitable rates" in contravention of the statute. In addition, the proposed regulation impairs the objectives of the Federal Power Act ("FPA") by unnecessarily increasing costs for qualifying cogeneration facilities ("QFs"), like Hopewell. The FPA requires, in pertinent part, that the rates prescribed for mandatory utility offers to purchase the output of QFs shall "be just and reasonable to the electric consumers of the utility" and "shall not discriminate against qualifying cogenerators . . . ." (FPA, 16 USCS § 824a-3).

It is not possible to successfully introduce the drastically reduced NOx allocations and added costs of penalties and compliance into this complex scheme of federal ratemaking and power production. No power producer will be able to comply with the reduced allocations under the proposed regulation and simultaneously comply with its obligations to efficiently deliver energy to the utilities and their customers while maintaining the justness and reasonableness of rates. Compliance with the proposed regulation is unduly onerous and burdensome-it is simply too much too soon.

RESPONSE: This regulation will, in fact, achieve just the opposite of what the commenter speculates.

First, it should be pointed out that this regulation is very similar to the 40 CFR Part 97. That federal regulation went through extensive public review. The federal program affects sources from Mississippi to Main, Michigan to New York. It covers a very large geographic area that contains many cogeneration facilities. During the regulation development process, EPA received hundreds of comments. The federal agency responsible for the implementation of PURPA also had an opportunity to comment on the regulation. No determination was made by EPA that the federal NOx SIP Call rule “thwarted federal energy policies.”

The Virginia final regulation also went through extensive public comment. It has been in the development process since 1998. It is not targeted to begin until the ozone season of 2004. It is not “too much too soon”. It incorporates the power of the marketplace to reduce pollution costs instead of the more costly process of command and control. By involving the marketplace, it ensures the most cost efficient reduction of NOx pollution, which will be reflected in the cost to electric consumers.

No changes have been made to the regulation based on this comment.

6. **SUBJECT:** Exempt dispatchable facilities from the regulation

COMMENTER: Thomas W. Kinnane and the law firm of Kinnane & Associates, Ltd., and Andrew N. Chau, Regulatory Counsel, Tractebel North America

TEXT: Tractebel recommends the following revision to the regulation, which is consistent with its arguments set forth comment number 4: exemption from the NOx Emissions Trading Budget Regulation (9 VAC 5-140) for all dispatchable facilities. Dispatchable facilities can "opt-in" to the program, if they so choose.

RESPONSE: The federal program requires that electric generating units over 25 MWe be included in the program. It does not differentiate between dispatchable and non-dispatchable facilities. To include such a differentiation could result in the disapproval of the program and result in federal sanctions.

No changes have been made to the regulation based on this comment.

7. **SUBJECT:** New formula for computing initial allocation

COMMENTER: Thomas W. Kinnane and the law firm of Kinnane & Associates, Ltd., and Andrew N. Chau, Regulatory Counsel, Tractebel North America

TEXT: Alternatively, if the exemption described in comment number 6 is not approved, Tractebel requests revision to the unadjusted allocation methodology for EGUs that factors in the expected increase in power demand for dispatchable facilities as follows**:**

Allocation(unadjusted) =(H1(1st highest) + HI(2nd highest)) / 2 x ER(controlled) x CF(80%) / [(CF(lst highest) +' CF(2nd highest)) / 2] / 2000

Where:
HI = Heat Input
ER = Emission Rate of 0.15 lbs of NOx per mmBtu
CF = Capacity Factor = Ratio of Operating Hours to Potential Operating Hours (Note: CF(1st highest) corresponds to the HI(1st highest) operating year
CF(80%) = Capacity Factor of 80% to be consistent with base loaded units

Example Calculation for Hopewell, DEQ Point-Id 1, which currently has an unadjusted allocated of 76 tons:

Allocation(unadjusted) = (1,067,598 + 964,880) / 2 x 0.15 x 80 / [(27+ 23.5) / 2] / 2000 = 242

No revision to the adjusted allocation methodology is proposed.

RESPONSE: The unadjusted methodology posed by the commenter assumes a capacity factor of 80 percent. There is no data to justify that level of capacity except that the source has a permit with a potential to emit at a level significantly higher than their historical operational data indicates. To use such an inflated capacity factor for all sources subject to the regulation would create a larger shortfall of NOx allowances than currently exists.

This example demonstrates why the ad hoc group spent several years developing the methodology in the final regulation, attempting to establish a consensus among all stakeholders in the process. The current method has been through the public participation process and has been deemed appropriate by EPA. To change methodology at this point would require additional public comment and review by EPA. Such a process would put the program behind the timeframe for submittal to and approval by EPA. The sanctions clock expires in July of this year. Any delay would result in a disapproval of the SIP and subsequent sanctions. Such a situation must be avoided.

No changes have been made to the regulation based on this comment.

8. **SUBJECT:** Permit pooling of unused allowances

COMMENTER: Thomas W. Kinnane and the law firm of Kinnane & Associates, Ltd., and Andrew N. Chau, Regulatory Counsel, Tractebel North America

TEXT: Unused allocations as determined in suggested comment number 7 could be returned either to the Virginia DEQ for redistribution at its discretion, or to a "pool" of allocations for dispatchable facilities in the Commonwealth. This mechanism would reduce the risk of having to purchase emissions or install costly NOx controls for dispatchable plants that have no control over the frequency, duration, or time of operation.

RESPONSE: All sources subject to this program would like to reduce the risk of having to purchase emissions or install costly NOx controls. The trading element of the program, as demonstrated by the success of Title IV of the Clean Air Act, greatly reduces the costs associated with pollution control.

No changes have been made to the regulation based on this comment.

9. **SUBJECT:** Adverse impact

COMMENTER: Thomas W. Kinnane and the law firm of Kinnane & Associates, Ltd., and Andrew N. Chau, Regulatory Counsel, Tractebel North America

TEXT: Implementation of the regulation as proposed will have a significant, adverse impact on Tractebel and the Hopewell community. Furthermore, the proposed allocation creates an increased economic burden and risk for Hopewell relative to other generators, and is therefore discriminatory and anti-competitive. The costs associated with the regulation's implementation in its current form will likely result in increased prices for the operation of the facility that must necessarily be borne by Tractebel or DVP. Moreover, should Tractebel be required to reduce operation of the plant, such reductions may have an economic impact on the residents of Hopewell and the surrounding community.

Tractebel believes the adoption of its suggested revisions will help to eliminate the adverse impacts on itself and the community, while maintaining the Commonwealth's compliance with federal requirements for NOx trading programs. Tractebel urges the Department to adopt these changes in order to ensure that the communities and industries it impacts will not be adversely affected.

RESPONSE: Significant changes to the allocation methodology at this time in the process will result in significant, adverse impact to the entire Commonwealth of Virginia. The delay would cause the Commonwealth to miss the federal timeframe for submitting its State Implementation Plan revision. The Commonwealth would be subject to federal sanctions. Every source subject to this regulation would have to comply with the 40 CFR Part 97 and would be under federal oversight.

No changes have been made to the regulation based on this comment.

10. **SUBJECT:** Initial allocations not included in the regulations

COMMENTER: Stevenson T. Walker, President and CEO, Virginia Manufacturers Association

TEXT: The Board changed the regulations so that initial allocations of NOx allowances for the individual units subject to the budget trading program are not included in the regulation itself. DEQ says the initial and subsequent allocations will be accomplished outside the regulatory process. VMA supports this change.

As VMA commented previously, we believe it is important for certainty's sake to list the baseline units receiving initial allocations in the regulation. However, we do not advocate including the actual numerical allocations in the regulations. EPA may well change the budget for Virginia's EGUs and may adjust the non-EGU allocations in 40 CFR Part 97 upward or downward as well. To effectuate these changes in the allocations, the Board would have to undertake a long and laborious rulemaking to change the numerical values included in Virginia's regulations. To avoid this, VMA agrees the Board should not fix the numerical EGU and non-EGU allocations in Virginia's NOx SIP call regulations.

RESPONSE: Support for the final regulation is appreciated.

11. **SUBJECT:** New source set-asides

COMMENTER: Stevenson T. Walker, President and CEO, Virginia Manufacturers Association

TEXT: The Board's proposed regulations did not provide for any special pool of NOx allowances that would be dedicated to new sources that begin operating in Virginia. Such a separate pool of allowances is commonly referred to as a new source "set-aside." Basically, a set-aside would comprise a pool of NOx allowances that would be taken from the budgets for the existing EGUs and non-EGUs and reserved for distribution to "new" regulated units that need NOx allowances to operate.

Since the Board's proposal, the General Assembly mandated a set-aside program for EGUs. Thus, the regulations had to be changed to create a set-aside pool of allowances in the first five years of Virginia's NOx budget trading program, i.e., 2004 through 2008, equal to S% of the total NOx allowances in the EGU budget. Each year after that, the EGU new source set-aside must equal 2% of the EGU budget. However, the General Assembly did not mandate a new source set-aside pool created from allowances for non-EGUs. Nevertheless, the final regulations the Board adopted establish a single new source set-aside pool created from allowances taken from both the EGUs and non-EGUs subject to the budget and trading program.

One of the major questions the DEQ raised in the preamble to the proposed regulations was whether there should be a new source set-aside for non-EGUs. The VMA believes there should be no such set-aside. Simply put, we do not believe new source set-asides are fair or economically efficient. We commented extensively on this issue in our prior comments on the proposed regulations.

We do not think it is fair to take NOx allowances away from the existing (baseline) units that are responsible for their very existence and give them as a windfall to new (non-baseline) units. More importantly, we doubt that taking NOx allowances from the existing baseline units and giving them new units would be economically efficient for the citizens and businesses of the Commonwealth.

The Department of Planning and Budget ("DPB") addressed set-asides in a detailed analysis included in the preamble to the proposed regulations. The DPB concluded, in no uncertain terms, that Virginia's NOx SIP call regulations should not include new source set-asides. As DPB explained: "This set-aside is equivalent to a cash subsidy for firms bringing new NOx sources on line; paid for by a tax on the owners and users of existing sources. A set-aside program such as this would do substantial violence to the operation of the market."

A new source set-aside is unquestionably without merit as a method of encouraging new manufacturers to locate in Virginia. Virginia's manufacturing sector is extremely diverse and responsive to a myriad of factors that determine competitiveness in the global marketplace. It is very unlikely that any owner would choose to locate a new manufacturing facility in the Commonwealth because the new source gets some free NOx emission allowances. There are simply too many other factors in making such a decision that are far more important to manufacturers than a few free NOx emission allowances.

Non-EGU sources in Virginia will be required to spend millions of dollars to make the 60% reduction in NOx emissions required by the rule. These retrofits of equipment are expensive and result in units that are less efficient to operate. Providing a set-aside from the non-EGU budget reduces the allocations for each non-EGU source even further and penalizes the owners of non-EGUs who are already faced with these large compliance costs.

In short, the VMA believes the Board should retain the approach taken in the proposed regulations. No allowances should be taken from existing (baseline) non-EGUs and dedicated as a set-aside for new (non-baseline) units that come into Virginia.

RESPONSE: The reasons for adopting consistent provisions has not changed. A consistent regulation is still an objective that will benefit the regulated community. In the interest of attempting to maintain a comprehensive and, where possible, simplified approach to regulation development and implementation, it will be most cost-effective to maintain one system for NOx trading for large EGU and non-EGU sources under this particular regulation. Ensuring that the regulation is no more complex than absolutely necessary will reduce administrative and implementation costs.

It should also be noted that additional emissions trading programs may be established in the future for other source categories and other pollutants. This particular regulation is the first of potentially several trading regulations that may be crafted in a similar manner, or may be crafted in a very different way. Additional databases may need to be developed to support these additional programs. It will be critical to ensure that the programs do not conflict or overlap. The allocation process, trading parameters and recordkeeping for both DEQ and the sources should not be complex and cumbersome, but rather, as streamlined as possible.

It is interesting to note that the commenter states: "It is very unlikely that any owner would choose to locate a new manufacturing facility in the Commonwealth because the new source gets some free NOx emission allowances". That is precisely the nature of the comments received from new EGU sources wanting to locate in Virginia and was part of . the argument used to revise the law to create a set-aside in the first place. One can only speculate that had a number of non-EGU permits been pending at DEQ the wording of the law may have, indeed, included non-EGU facilities. It is anticipated that any source, non-EGU or EGU, wanting to locate in Virginia will be very interested in a new source set-aside pool of NOx allowances.

Given the significant increase to the non-EGU sector once allocations are normalized, it is prudent to keep some in reserve to accommodate new economic development. Any unused portion of the allocations in the pool will be returned to the existing sources prior to compliance true-up at the end of the compliance period.

No changes have been made to the regulation based on this comment.

12. **SUBJECT:** Allowances set-aside from non-EGUs should be no more than 5% for the initial allocation and 2% thereafter.

COMMENTER: Stevenson T. Walker, President and CEO, Virginia Manufacturers Association

TEXT: If the Board rejects VMA's recommendation offered in comment number 11 and continues to include provisions in the final regulations establishing a new source set-aside from the non-EGUs allocations, the Board should take no more than 5% of the initial non-EGU allowances. The set-aside for control periods after the initial allocation period should be no more than 2% of the total allowances in the non-EGU budget. This would be in keeping with the set-asides mandated by the General Assembly for EGUs subject to the regulations.

Unfortunately, that is not the approach the Board takes in the final regulations. Instead, the regulations call for taking 5% of the non-EGU allowances not only for the initial allocation period, but also for all subsequent allocations. While the EGU contribution to the new source set-aside pool decreases to 2% after the initial allocation period, the non-EGU contribution (which wasn't even mandated by legislation) stays at 5%. VMA strenuously

objects to this uneven treatment and urges the Board to correct this inequity by reducing the non-EGU contribution to the set-aside pool to 2% of the non-EGU's allocations after the initial allocation period.

RESPONSE: The set-aside from the non-EGU budget was 1,177 tons. One thousand twenty-three tons of the set-aside came from a Virginia source that was double counted in the EPA allocations under the Section 126 final rule. The source was listed as both an EGU and a non-EGU. Discussions with EPA confirmed the mistake; however, EPA indicated that the total budget numbers would not change as a result of their mistake.

It should be noted that the allocations for non-EGUs when normalized, result in a 193 percent increase in NOx allocations for the non-EGU sources subject to this program. The "extra" 1023 tons were placed in the set-aside pool because the need to ensure continued growth and economic development is vital to the future of the citizens of Virginia and given the significant increase in the non-EGU budget allocations after adjustment this was a prudent thing to do. However, the non-EGU sources suggest that the previous approach is inappropriate. Therefore, the regulation has been modified such that the amount from the non-EGU budget for the set-aside will be 1000 tons rather than 1,177 tons.

One hundred fifty-four tons is five percent of the total non-EGU budget minus the "extra" 1023 tons. By returning 177 tons to the existing source allocation pool, the non-EGU sector gets more than the five- percent originally taken from the non-EGU trading budget. Twenty-three tons from the "extra" 1023 will also transfer for distribution from the existing source pool. This is an appropriate compromise when balancing the need for continued economic growth with the need for existing sources to achieve the appropriate pollution reduction targets.

13. **SUBJECT:** Any EGU and non-EGU set-asides should come from their respective budgets.

COMMENTER: Stevenson T. Walker, President and CEO, Virginia Manufacturers Association

TEXT: VMA has commented previously that if the Board changed the proposed regulations to include a set-aside for new non-EGUs, the NOx emission allowances for the set-aside should come only from the non-EGU budget. Correspondingly, the allowances for the EGU set-aside mandated by the General Assembly should come only from the EGU budget. The penalty of the set-aside for each sector, electric generation and manufacturing should be borne only by the owners of units in their respective sector. Owners of non-EGUs should not have to bear the penalty of forfeiting NOx allowances to fund the new source set-aside for EGUs, and vice versa.

The Board rejected VMA's advice and instead created a single new source set-aside pool. Allocations from this pool are available to EGUs and non-EGUs alike. It appears the Board

created a single new source set-aside pool in order to be able distribute to new EGUs a "windfall" of several hundred excess allowances EPA mistakenly included in Virginia's non-EGU budget. The Board's final regulations include these "excess" non-EGU allowances in the single new source set-aside pool. VMA understand the DEQ's interest in having these excess non-EGU allowances available to new EGUs as well as new non-EGUs. However, should the excess non-EGU allowances go away, e.g., be confiscated by EPA, before May 2004, VMA advocates the establishment of separate EGU and non-EGU new source set-aside pools "funded" separately by taking initially 5% and subsequently 2% of the allowances from the EGU and non-EGU budget units, respectively, to "fund" the separate EGU and non-EGU new source set-aside pools.

RESPONSE: Please see response to comments number 11 and 12.

14. **SUBJECT:** Support for the program

COMMENTER: Stevenson T. Walker, President and CEO, Virginia Manufacturers Association

TEXT: The VMA generally supports the Board's adoption of the NOx Budget Trading Program regulations. However, we believe the regulations would be improved by making the few changes we advocate in these comments.

RESPONSE: Support for the program is appreciated.

15. **SUBJECT:** New source set-asides

COMMENTER: Richard Langford, Regulatory Affairs Manager, Cellanese Acetate LLC

TEXT: Celanese believes that the Board inappropriately applied the provision for new source set-asides to non-EGU sources. Celanese understands that the Board added the set-aside provision because of legislation passed last year. However, the General Assembly mandated a set-aside program only for EGUs and that law did not mandate a set-aside program for non-EGUs. The Board took it upon itself to expand the set-aside program to the non-EGU sector when the public record clearly indicated that such a set-aside program would be detrimental to the NOx trading market.

The Department of Planning and Budget ("DPB") addressed set-asides in a detailed analysis included in the preamble to the proposed regulations. The DPB concluded, in no uncertain terms, that Virginia's NOx SIP call regulations should not include new source set-asides. As DPB explained:

"This set-aside is equivalent to a cash subsidy for firms bringing new NOx sources on line; paid for by a tax on the owners and users of existing sources. A set-aside program such as this would do substantial violence to the operation of the market."

Celanese agrees with the position of DPB and strongly requests the Board to limit the set-aside program strictly to the EGU sector as provided by Virginia law.

RESPONSE: Please see response to comment number 11.

16. **SUBJECT:** Apportionment of NOx allocations

COMMENTER: Richard Langford, Regulatory Affairs Manager, Cellanese Acetate LLC

TEXT: We believe that one reason the Board included non-EGU sources along with the EGU sources in a single set-aside was to provide a mechanism to "move" a "windfall" portion of the non-EGU trading budget away from existing sources and provide those allocations as additional allowances for new units. Board staff have stated that EPA has told the Commonwealth that the budgets cannot be changed. This is not consistent with EPA's public statements on the NOx SIP call. EPA has repeatedly said that states have the right to apportion their trading budgets between sources in any way they wish. Therefore, the Board is free to equitably apportion or reduce the allowances in the final rule. This would eliminate the need to use mechanisms such as the set-aside budget to accomplish this. Celanese believes that if adjustments are necessary because of any "windfall", these should be made by adjustment of the sector trading budgets rather than the use of set-asides.

RESPONSE: Please see response to comment number 12. It should also be noted that the non-EGU budget when normalized results in a 193 percent increase in NOx allocations for the non-EGU sources subject to this program. In other words, the unadjusted allocation for non-EGUs increases by almost 200 percent. For example, under this allocation process two units at Celanese go from an unadjusted allocation of 75 tons and 27 tons to 145 tons and 52 tons respectively.

17. **SUBJECT:** Apportionment of NOx allocations

COMMENTER: Richard Langford, Regulatory Affairs Manager, Cellanese Acetate LLC

TEXT: Not only did the Board expand the set-aside program beyond that required by law, it chose to make the set-aside program more onerous for the non-EGU sector than the EGU sector. While, both sectors were included in the set-aside program at a level of 5% for initial allocations, the Board chose to maintain the higher level of set-aside for the non-EGU sector for subsequent periods where Virginia law required a lower level of 2% for the non-EGU sector. This discriminatory treatment of non-EGUs is very unfair and not warranted.

Celanese is strenuously opposed to this unfair and uneven treatment of sources in Virginia. In the event the Board continues to require a set-aside for the non-EGU sector,

Celanese strongly urges the Board to not make these requirements more onerous than those required of EGUs.

In short, Celanese believes the Board should retain the approach taken for non-EGUs in the proposed regulations. That is; no allowances should be taken from existing (baseline) non-EGUs and dedicated as a set-aside for new (non-baseline) units that come into Virginia.

RESPONSE: Please see response to comment number 12.