

requirements for Publisher's Printing, Inc., for completeness and found that both conform to the completeness criteria in 40 CFR part 51, appendix V (criteria for plans submitted explicitly for parallel processing). EPA issued a letter regarding completeness to Kentucky on June 18, 2001.

With the negative declaration, Kentucky is asserting that an evaluation has found that there are no sources within the Bullitt and Oldham Counties' portion of the Louisville 1-hour ozone nonattainment area that would be subject to a CTG rule for aerospace, SOCFI, shipbuilding, or wood furniture. Through its negative declaration, the APCDJC is asserting that an evaluation has found that there are no sources within the Jefferson County portion of the Louisville 1-hour ozone nonattainment area that would be subject to a CTG rule for aerospace, shipbuilding, or wood furniture. Therefore, EPA is proposing to approve the negative declaration from Kentucky for the CTG categories of aerospace, SOCFI, shipbuilding, and wood furniture, and the negative declaration from the APCDJC for the CTG categories of aerospace, shipbuilding, and wood furniture as meeting the section 184(b) VOC RACT requirement for these source categories in the Kentucky portion of the Louisville 1-hour ozone nonattainment area.

The EPA has reviewed Kentucky's requested revisions of the federally-approved SIP for conformance with the provisions of the 1990 amendments enacted on November 15, 1990. The Agency has determined that this action conforms with those requirements.

Nothing in this action should be construed as permitting or allowing or establishing a precedent for any future implementation plan. Each request for revision to the SIP shall be considered separately in light of specific technical, economic, and environmental factors and in relation to the relevant statutory and regulatory requirements.

#### IV. Administrative Requirements

Under Executive Order 12866 (58 FR 51735, October 4, 1993), this proposed action is not a "significant regulatory action" and therefore is not subject to review by the Office of Management and Budget. This action merely proposes to approve state law as meeting federal requirements and imposes no additional requirements beyond those imposed by state law. Accordingly, the Administrator certifies that this proposed rule will not have a significant economic impact on a substantial number of small entities under the Regulatory Flexibility Act (5 U.S.C. 601

*et seq.*). Because this proposed rule approves pre-existing requirements under state law and does not impose any additional enforceable duty beyond that required by state law, it does not contain any unfunded mandate or significantly or uniquely affect small governments, as described in the Unfunded Mandates Reform Act of 1995 (Public Law 104-4). This proposed rule also does not have a substantial direct effect on one or more Indian tribes, on the relationship between the Federal Government and Indian tribes, or on the distribution of power and responsibilities between the Federal Government and Indian tribes, as specified by Executive Order 13175 (65 FR 67249, November 9, 2000), nor will it have substantial direct effects on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government, as specified in Executive Order 13132 (64 FR 43255, August 10, 1999), because it merely proposes to approve a state rule implementing a federal standard, and does not alter the relationship or the distribution of power and responsibilities established in the CAA. This proposed rule also is not subject to Executive Order 13045 (62 FR 19885, April 23, 1997), because it is not economically significant.

In reviewing SIP submissions, the EPA's role is to approve state choices, provided that they meet the criteria of the CAA. In this context, in the absence of a prior existing requirement for the State to use voluntary consensus standards (VCS), the EPA has no authority to disapprove a SIP submission for failure to use VCS. It would thus be inconsistent with applicable law for the EPA, when it reviews a SIP submission, to use VCS in place of a SIP submission that otherwise satisfies the provisions of the CAA. Thus, the requirements of section 12(d) of the National Technology Transfer and Advancement Act of 1995 (15 U.S.C. 272 note) do not apply. As required by section 3 of Executive Order 12988 (61 FR 4729, February 7, 1996), in issuing this proposed rule, the EPA has taken the necessary steps to eliminate drafting errors and ambiguity, minimize potential litigation, and provide a clear legal standard for affected conduct. The EPA has complied with Executive Order 12630 (53 FR 8859, March 15, 1988) by examining the takings implications of the rule in accordance with the "Attorney General's Supplemental Guidelines for the Evaluation of Risk and Avoidance of Unanticipated

Takings" issued under the executive order. This proposed rule does not impose an information collection burden under the provisions of the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*).

#### List of Subjects 40 CFR Part 52

Environmental protection, Air pollution control, Intergovernmental relations, Ozone, Reporting and recordkeeping requirements, and Volatile organic compounds.

**Authority:** 42 U.S.C. 7401-7671q.

Dated: July 12, 2001.

**A. Stanley Meiburg,**

*Acting Regional Administrator, Region 4.*

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## ENVIRONMENTAL PROTECTION AGENCY

### 40 CFR Part 52

[TX-133-1-7499; FRL-7016-9]

#### Approval and Promulgation of Implementation Plans; Texas; Emissions Banking and Trading Revisions for the Mass Emissions Cap and Trade Program for the Houston/Galveston Ozone Nonattainment Area

**AGENCY:** Environmental Protection Agency (EPA).

**ACTION:** Proposed rule.

**SUMMARY:** Through parallel processing, the EPA is proposing to approve a revision to the Texas State Implementation Plan (SIP). We are proposing approval of the NO<sub>x</sub> Mass Cap and Trade program for the Houston/Galveston (HGA), one-hour ozone nonattainment area. If the State makes significant changes between the versions being parallel reviewed and the final adopted versions, other than those changes resulting from issues discussed in this proposed rulemaking, EPA will issue an additional proposed rulemaking prior to taking final action. If there are no significant changes (other than changes resulting from issues discussed in this proposed rulemaking) to the parallel-processed versions and Texas submits the final versions by October 1, 2001, the EPA will proceed with final rulemaking. The MECT program will contribute to attainment of the 1-hour ozone National Ambient Air Quality Standard (NAAQS) in the HGA ozone nonattainment area.

**DATES:** Written comments must be received on or before August 22, 2001.

**ADDRESSES:** Written comments should be addressed to Mr. Thomas H. Diggs,

Chief, Air Planning Section (6PD-L), at the EPA Region 6 Office listed below. Copies of documents relevant to this action including the Technical Support Document (TSD) are available for public inspection during normal business hours at the following locations. Anyone wanting to examine these documents should make an appointment with the appropriate office at least two working days in advance.

Environmental Protection Agency, Region 6, Air Planning Section (6PD-L), 1445 Ross Avenue, Dallas, Texas 75202-2733. Texas Natural Resource Conservation Commission, Office of Air Quality, 12124 Park 35 Circle, Austin, Texas 78753.

**FOR FURTHER INFORMATION CONTACT:**

Merrit Nicewander, Air Planning Section (6PD-L), EPA Region 6, 1445 Ross Avenue, Dallas, Texas 75202-2733, telephone (214)665-7519.

**SUPPLEMENTARY INFORMATION:**

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Throughout this document "we," "us," and "our" means EPA.

**I. Mass Emissions Cap and Trade Program**

*A. Proposed Action*

**What Action Are We Taking?**

The EPA is proposing to approve the NO<sub>x</sub> Mass Cap and Trade program for the Houston/Galveston one-hour ozone nonattainment area. The HGA ozone nonattainment area is required to attain the one-hour ozone standard of 0.12 parts per million (ppm) by November 15, 2007.

The rule adopted and submitted as this SIP revision by letter of the Governor dated December 22, 2000 is one element of the control strategy for the HGA nonattainment area to comply with the requirements of the Clean Air Act (CAA) and achieve attainment for ozone. The HGA ozone nonattainment area will need to reduce nitrogen oxides (NO<sub>x</sub>) to reach attainment with the one-hour standard. The MECT emissions banking rule was evaluated as an integral component of the HGA control strategy to reduce NO<sub>x</sub> emissions.

*B. MECT EIP Contents*

**What Is the TNRCC MECT Program That Has Been Submitted for Approval as Part of the Texas SIP?**

The proposed SIP revision submitted by the TNRCC is the Mass Emission Cap & Trade Program (30 Texas Administrative Code (TAC) Chapter 101, Subchapter H, Division 3). The MECT regulation is found at sections 101.350 through 101.363. The MECT program is mandatory for stationary facilities that emit NO<sub>x</sub> in the HGA ozone nonattainment area (at sites that have a collective design capacity of 10 tons per year or more) and which are subject to the TNRCC NO<sub>x</sub> rules as found at 30 TAC Chapter 117. NO<sub>x</sub> is a precursor gas that reacts with volatile organic compounds (VOCs) in the presence of sunlight to form ground-level ozone. The program sets a cap on NO<sub>x</sub> emissions beginning on January 1, 2002 with a final reduction to the cap occurring in 2007.

Facilities are required to meet NO<sub>x</sub> allowances on an annual basis. Facilities may purchase, bank or sell their allowances. The program has a provision to allow a facility to use discrete emission reduction credits (DERCs) and mobile discrete emission reduction credits (MDERCs) in lieu of allowances if they are generated in the HGA area. Although EPA is today proposing to approve the MECT rules, EPA notes that the MECT rules were submitted along with rules authorizing the generation and use of DERCs and MDERCs. These rules are found in 30 TAC Chapter 101, Subchapter H, Division 4. The MECT rules authorize use of DERCs and MDERCs generated pursuant to the rules in Division 4 to meet the cap. EPA is not today proposing action on the rules in Division 4, but intends to act on them in a separate rulemaking at a later date. This schedule of action on the submitted Emissions Banking and Trading rules has been discussed with and is acceptable to the State.

The MECT EIP is mandatory for facilities in that if they meet the above conditions they must participate in the cap. However, the MECT program is a discretionary EIP since it is not a requirement of the Clean Air Act that it be adopted by the State.

TNRCC proposed revisions to the MECT rule on May 30, 2001. The EPA is proposing through parallel processing to approve the State's proposed revisions to the MECT rule submitted by the Governor on June 15, 2001. The proposed rule revision contains the inclusion of emission quantification protocols, the inclusion of an annual

compliance summary report to EPA and the public, and a revised schedule of emission reduction factors. The proposed changes strengthen certain elements of the MECT SIP submittal.

**What Is Parallel Processing?**

Parallel processing means that EPA proposes action on a state rule before it becomes final under state law. Under parallel processing, EPA takes final action on its proposal if the final, adopted state submission is substantially unchanged from the submission on which the proposed rulemaking was based, or if significant changes in the final submission are anticipated and adequately described in EPA's proposed rulemaking or result from needed corrections determined by the State to be necessary through review of issues described in EPA's proposed rulemaking.

We cannot finalize action on the MECT EIP program unless and until the Governor submits the finally adopted regulation. The State has begun its rulemaking process and submission of the final rule is anticipated in September 2001. Significant changes between the versions being parallel reviewed and the final adopted versions, other than those changes resulting from issues discussed in this proposed rulemaking, will result in a new EPA proposed rulemaking. If there are no significant changes to the parallel-processed versions and they are submitted by October 1, 2001, the EPA will proceed with final rulemaking.

**Has the MECT Rule Been Revised by TNRCC Since It Was Submitted To EPA as a SIP Revision?**

Yes, the MECT rule was revised by TNRCC after it had been submitted to EPA as part of the Texas SIP on December 22, 2000. Rule Log # 2001-015-101-AI which clarified the applicability requirements of the rule at § 101.351 was adopted on May 23, 2001. This rule revision was effective on June 13, 2001. A SIP revision incorporating this clarification was submitted by the Governor on July 2, 2001. The TNRCC clarified section 101.351 to specify that the requirement to operate under the cap and trade program applied to all NO<sub>x</sub> emitting facilities in the HGA area with emission standards under Chapter 117, Control of Air Pollution from Nitrogen Compounds, and which are located at a site where their collective design capacity to emit NO<sub>x</sub> is ten tons or more per year. We are also proposing to approve this minor revision in this action.

What Areas of Texas Will Be Affected by the MECT Program?

The HGA ozone nonattainment area contains Brazoria, Chambers, Fort Bend, Galveston, Harris, Liberty, Montgomery, and Waller counties in Texas.

What Is an Economic Incentive Program?

An economic incentive program is a regulatory program that achieves an air quality objective by providing market-based incentives or information to emission sources. A uniform emission reduction requirement, based for instance on installation of a required emission control technology, does not take account of variations in processes, operations, and control costs across sources even of the same type, such as electric utilities, or petroleum refiners. By providing flexibility in how sources meet an emission reduction target, an EIP empowers sources to find the means that are most suitable and most cost-effective for their particular circumstances.

What Is a CAP?

A cap is the total emission limitation for all participating sources in the EIP. The NO<sub>x</sub> cap will be established at levels demonstrated as necessary and feasible to allow HGA to attain the NAAQS for ozone. The cap will consist of the summation of individual allowances allocated to each facility in the MECT EIP. The cap will be enforced by the allocation, trading, and banking of allowances. Each facility will be required to hold allowances in its compliance account on March 1 of each year equal to or greater than the total emissions of NO<sub>x</sub> emitted during the previous control period.

What Sources Are Subject to the MECT Program?

The MECT program is mandatory for stationary facilities that emit NO<sub>x</sub> in the HGA ozone nonattainment area and which are subject to the emission specifications under sections 117.106, 117.206 and 117.475 and which are located at a site where they collectively have a design capacity to emit of 10 tons per year or more of NO<sub>x</sub>. If an individual stack is not subject to or is exempt from the requirements of 30 TAC Chapter 117, that stack is not subject to the MECT program regardless of its design NO<sub>x</sub> capacity. Other stacks at the same facility may be subject to the MECT program if they are subject to Chapter 117.

It should be noted that section 117.203(a)(1) historically provided exemptions for any new units that were placed in service after November 15,

1992, since these sources would have been subject to Best Available Control Technology (BACT) and /or Lowest Achievable Emission Reduction (LAER) new source review (NSR) requirements. These NSR requirements are typically more restrictive than the section 117 requirements. However, new section 117.203(b) revokes the exemption and the sources are subject to the MECT program. EPA approved 117.203(b) on September 1, 2000.

What Is the Definition of the Term, Facility?

The MECT regulation states that it applies to stationary facilities. The term, facility, however, is not defined in the rule. Facility is defined in at least two different places in the permitting regulations. TNRCC defines facility at 30 TAC 116.10(4) as "a discrete or identifiable structure, device, item, equipment, or enclosure that constitutes or contains a stationary source, including appurtenances other than emission control equipment. A mine, quarry, well test, or road is not a facility." TNRCC further defines "building, structure, facility, or installation" at 30 TAC 116.12(4) as "All of the pollutant-emitting activities which belong to the same industrial grouping, are located in one or more contiguous or adjacent properties, and are under the control of the same person (or persons under common control) except the activities of any vessel. Pollutant-emitting activities shall be considered as part of the same industrial grouping if they belong to the same "major group" (i.e., which have the same two-digit code) as described in the Standard Industrial Classification Manual, 1972, as amended by the 1977 supplement." The technical review and proposed approval of the MECT rule is based upon the definition of the term, facility, as defined in 30 TAC 116.10(4). Facility within the context of the MECT rule is interpreted by the State and EPA to mean equipment that is vented to a stack.

What Is an Allowance?

Allowance means the authorization to emit one ton of NO<sub>x</sub> per year. One compliance account shall be used for multiple sources located at the same site and under common ownership or control. The commission will maintain a registry of the allowances in each compliance account.

What Is a Control Period?

A control period or a compliance period is the 12-month period beginning January 1 and ending December 31 of

each year. The initial control period will begin January 1, 2002.

When Will the cap Be Implemented?

The cap will be implemented on January 1, 2002 at historical emission levels, with three mandatory reductions increasing over time until achieving the final cap by January 1, 2007. These sections also require all new or modified sources in HGA to obtain unused allowances from other sources already participating under the cap to offset any increased NO<sub>x</sub> emissions.

How Will the cap Be Determined?

The MECT rules at section 101.353 describe how allowances will be allocated to individual facilities. Initially, for any facility operating prior to January 1, 1997, allowances will be based on the average of its actual level of activity from 1997, 1998, and 1999 multiplied by the facility's actual emission factors from 1997, 1998, and 1999 (not to exceed any applicable federal or state regulation, rule, or permit limit).

How Will the cap Be Adjusted to the Level Relied Upon in the Attainment Demonstration?

All facilities in the MECT EIP program will have periodic reductions in allowances until 100% of the reductions is achieved in 2007. There are two categories of sources for which the reduction schedule has been developed. The first category is boilers, auxiliary steam boilers, and stationary gas turbines within an electric power generating system. The second category is all other sources. Beginning April 1, 2007 and for all subsequent control periods, allowances will be reduced by 100% of the required reductions.

TNRCC proposed revisions to the MECT rule on May 30, 2001 which is being parallel processed by this document. The proposed rule revision contains a potential revised schedule of emission reduction factors depending upon the results of a TNRCC study that is to be completed by 2002 and requires EPA approval. The EPA is proposing approval of the revisions to the MECT rule submitted to us on June 15, 2001 which we are parallel processing but not that portion of the proposed rule containing a potential modification to the reduction schedule. Specifically, we are not taking action on section 101.353(a)(3)(B) and (D) in this document.

Are There Allowances for New Sources in the cap?

No, any new or modified facility will not be allocated any allowances if that

facility has submitted a NSR permit application which has determined to be administratively complete on or after January 2, 2001.

#### How Will New Sources Participate in the MECT cap?

The new or modified facilities will be required to obtain allowances from other facilities already participating in the cap and trade program or by obtaining DERCS or MDERCS.

#### Can Allowances Be Used in Other Programs?

Allowances are valid only for MECT program purposes. An allowance does not constitute a security or a property right. Allowances cannot be used to exceed any NSR permit limitation or any other applicable rule or law. Allowances can be used for the 1:1 portion of NSR offsetting under section 101.352(e). Allowances can not be used for netting under the NSR program.

#### What Happens to a Facility That Has Less NO<sub>x</sub> Emissions Than Allowances for a Compliance Period?

Allowances may generally be banked for future use or traded during the control period for which they are allocated or the following control period.

#### What Happens to a Facility That Has More NO<sub>x</sub> Emissions Than Allowances for a Compliance Period?

If a facility emits more NO<sub>x</sub> than was held in the compliance account on March 1 following the control period, allowances for the next control period will be reduced by the amount equal to the emissions exceeding the compliance account plus an additional 10%. This does not preclude additional enforcement action by the TNRCC and/or EPA.

#### Can Unused Allowances Be Banked for Future Use?

Yes, allowances may generally be banked for future use or traded during the control period for which they are allocated or the following control period. Any allowance not used for compliance may be banked or traded for use in the following control period. Allowances that are not expired or used can be traded at any time after they have been allocated.

#### How Are Trades of Allowances Conducted?

Only authorized account representatives may trade allowances. Trade requests are to be made through the submittal of a completed ECT-2 Form, Application for Transfer of

Allowances. The completed form, including the price paid per allowance, will be submitted to TNRCC 30 days prior to the allowances being deposited into the account. Trades will be completed through the TNRCC executive director and will be considered complete when the executive director issues a letter finalizing the trade.

#### Will the Program Be Audited?

Yes, an audit of the cap and trade program will be conducted by TNRCC every three years. The audit will evaluate the impact of the program on the state's attainment demonstration, the availability and cost of allowances, compliance by the participants, and other elements. The TNRCC Executive Director will recommend measures to remedy any problems identified in the audit. The trading of allowances, discrete emission reduction credits, and/or mobile discrete emission reduction credits may be discontinued as a remedy for problems identified in the program audit. The audit data and results will be completed and submitted to the EPA and made available for public inspection within six months after the audit begins.

#### How Will Emissions Be Monitored by the Facilities in Order To Determine Compliance With the cap?

The proposed revision to the MECT EIP rule which is being parallel processed contains a revision to section 101.354 Allowance Deductions. The revision requires allowance deductions to be based upon the emission quantification protocols established in 30 TAC Chapter 117. The EPA is proposing to approve the Chapter 117 monitoring methodology in this action as the emission quantification protocols for the MECT program.

#### How Will a Facility Report Compliance With the Cap?

Facilities are required by March 31 of each year to submit a completed ECT-1 Form to TNRCC with the amount of actual NO<sub>x</sub> emissions for the preceding control period. Also included are the methods used in determining the emissions and a summary of all final trades.

#### C. EPA's Analysis

##### How Did EPA Review and Evaluate the TNRCC MECT EIP SIP Submittal?

The document, Improving Air Quality with Economic Incentive Programs, (EPA-452/R-01-001) January 2001 is the EPA guideline for reviewing and approving discretionary EIP submittals for SIP credit. It will be referred to as

the EPA EIP Guidance throughout this notice. The guidance pertains to discretionary EIPs that will be measures in State implementation plans. The guidance applies to the establishment of a discretionary EIP for attaining the NAAQS for criteria pollutants. The EPA technical review of the MECT SIP submittal against the expectations of the EPA EIP Guidance is contained in the Technical Support Document for the TNRCC Mass Emissions Cap and Trade Program for the HGA Nonattainment Area dated April 2001. The technical support document is available as specified in the section of this document identified as **ADDRESSES**.

#### What Does the EPA Mean by Guidance?

The EPA stated that the EIP guidance applies to discretionary EIPs, but does not represent the EPA's final action regarding discretionary EIPs. Final action occurs when the EPA has approved or disapproved the discretionary EIP submitted as a SIP revision. Congress did not address specific requirements for EIPs in the CAA. Consistent with our mandate, the EPA has interpreted what an EIP should contain in order to meet the requirements of the CAA. The document is a guidance document that sets forth EPA's non-binding policy for EIPs. The document does not represent final EPA action on the requirements for EIPs. Rather, the document identifies several different types of economic incentive programs, and proposes elements for each type that, if met, EPA currently believes would assure that the program would meet the applicable CAA provisions.

The guidance phrases these elements in the imperative—that is, using the terms “must” or “shall.” This is done only to signify that EPA would propose to approve a SIP submittal of a program containing the indicated elements on grounds that under section 110(l) of the CAA, the SIP revision does not interfere with any applicable requirement concerning attainment, reasonable further progress, or any other applicable requirement.

#### Was the EPA EIP Guidance a Final Agency Action?

Because it is a guidance document, the EPA EIP Guidance does not represent the EPA's final action for any discretionary EIP. Final action occurs when the EPA has approved or disapproved the discretionary EIP submitted as a SIP revision.

Once an EIP SIP revision is submitted, EPA will take action through notice-and-comment rule making to determine if the statutory requirements have been

met. Only action taken after the conclusion of that rulemaking would constitute final Agency action. The EPA would take steps to expedite its proposed approval in the case of SIP revisions containing programs that contain the elements of the EPA EIP guidance.

If a program that does not contain the elements of the EPA EIP guidance for that type of program is submitted, EPA would still seek to determine whether the applicable CAA requirements were met, and, if so, EPA would approve the submission. The EPA would make the determination through notice-and-comment rulemaking.

What Criteria Did EPA Use To Analyze the MECT SIP Submittal?

There are three fundamental principles that apply to all EIPs; integrity, equity and environmental benefit. The MECT was evaluated against the Clean Air Act requirements for all three of these principles. The EPA EIP guidance contained elements for trading EIPs as well as provisions specific to mass cap and trade EIPs. Each of these principles, elements and provisions are addressed in this notice.

Fundamental EIP Principle One—Integrity

There are four elements that make up the EIP principle of integrity. The fundamental principle of integrity consists of the qualities of surplus, enforceable, quantifiable and permanent.

Integrity Element One—Surplus

The element of surplus as it applies to MECT EIPs provides that programmatic emission reductions are surplus as long as they are not otherwise relied on in any of the following air quality-related programs such as the SIP, SIP-related requirements such as transportation conformity, other adopted TNRCC air quality programs not in the SIP, and federal rules that focus on reducing precursors of criteria pollutants such as new source performance standards (NSPS), rules for reducing VOCs promulgated under section 183 of the CAA, and statutorily mandated mobile source requirements.

In multi-source emission cap-and-trade EIPs, the programmatic fundamental element of surplus, as used with reference to the EIP as a whole, has a special meaning. A program that conforms to the EIP Guidance will show that the cap on all emissions is below the threshold that would have been set before the program was implemented for the affected sources. It should be noted that the fundamental element of surplus

does not apply to sources participating in multi-source emission cap-and-trade EIPs, only to the programmatic emission reductions.

EPA concluded that the TNRCC MECT SIP submittal at section 101.353(a)(3) demonstrated declining reductions of NO<sub>x</sub> emissions over time in order to reach attainment. The cap is at least 80% lower than the emission level that existed prior to the implementation of the MECT EIP. In addition the MECT EIP will ensure lower NO<sub>x</sub> emissions than implementation of 30 TAC Chapter 117 emission standards for the HGA attainment demonstration will ensure, since the MECT program limits mass emissions based on historical activity levels, and reduces the mass cap over time based on emission rate specifications in section 117. The Chapter 117 Emission Specifications for Attainment Demonstrations (ESAD) limitations are rate based and do not limit mass emissions. Thus, the programmatic surplus provision for the MECT EIP that the cap on all emissions be below the threshold that would have otherwise been set for the affected sources has been met. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for the integrity element of surplus.

Integrity Element Two—Enforceable

Emission reduction use, generation, and other actions are enforceable on a programmatic basis, if they are independently verifiable, define program violations and identify those liable for violations. The EPA EIP expectation for enforceable also is that the state and the EPA maintain the ability to apply penalties and secure appropriate corrective actions where applicable. Citizens should also have access to all the emissions-related information obtained from the source so that citizens can file suits against sources for violations. Required actions are enforceable on a programmatic basis if they are practicably enforceable in accordance with other EPA guidance on practicable enforceability.

In multi-source emission cap-and-trade EIPs, the source-specific fundamental elements of enforceable, and quantifiable, as used with reference to the actions of the individual sources participating in the EIP, have special meanings. Source-specific actions are enforceable if each source owner/operator is responsible for owning enough allowances to cover its emissions for the given time period and for providing clear title to the allowances it transfers.

On a source specific basis as spelled out in § 4.1(b), actions, emission reductions or emission limits as required by the MECT EIP are enforceable if the source is liable for any violations, the liable party is identifiable and the state, the public, and the EPA can independently verify a source's compliance. The expectation for enforcement elements common to all trading EIPs is that certain enforcement elements will be incorporated into all trading EIP rules submitted as a SIP revision. These include provisions for assessing liability, provisions to assess penalties against participating sources, and provisions for sources with title V permits.

1. Enforceable Element—Liability Assessment

The expectation for provisions for assessing liability common to all trading EIPs is discussed at section 6.1(a) of the EPA EIP guidance document. A program that conforms to the EIP Guidance will include provisions for assessing liability. Unlike traditional CAA regulatory mechanisms, emission trading involves more than one party. These parties can include those who own or operate the sources participating in the trade and sometimes another party who facilitated the trade (such as a broker).

To ensure there is integrity in the trading system, parties are also normally responsible for ensuring the validity of the trades or their use of emission reductions. At a minimum, each party is responsible for the truth, accuracy, and recording of all the information it provides to make the trade happen. The TNRCC MECT EIP rule should contain provisions to make users responsible for ensuring the validity of their use of emission reductions.

Traded emissions reductions are valid if they are true and accurate, generally meet all requirements of the MECT EIP rule, are properly measured in keeping with quantification protocols, satisfy monitoring, recordkeeping and reporting (MRR) provisions, and adhere to all other provisions for trading, such as no double counting. Sources using traded emission reductions are the main parties which will be held liable for any violations of applicable emission limitations. However, to discourage any possible collusion between sources, generators, and third parties, EPA may also hold other parties liable as explained in the EIP Guidance.

The revision to the MECT rule which is being parallel processed by this notice submitted the emission quantification protocols in 30 TAC Chapter 117. EPA is reviewing the submitted protocols in

accordance with the principles discussed herein, and CAA requirements. The revised section 101.354 speaks to the Executive Director approving other methods instead of the protocols in Chapter 117. Any use of a method other than the Chapter 117 protocols must be submitted to, and approved by, EPA.

The EIP states that in any enforcement action, the parties bear the burden of proof on each of their respective responsibilities. The MECT EIP submittal did not specifically address the assessment of liability for generators, third parties and users. EPA concluded that the MECT EIP rule itself did not contain the EPA EIP guidance specific expectation for liability assessment.

However, the TNRCC enforcement statute & rule are not typically in individual rules but have their own codification elsewhere. The Texas Water Code Chapter 7 contains the statutory provisions for enforcement of the MECT EIP regulation. The TNRCC enforcement rule is found at 30 TAC section 70.5. It provides remedies found in the state statutes (Texas Water Code and the Texas Health and Safety Code). It includes referrals to the EPA for civil, judicial or administrative action. Nothing in chapter 70 shall preclude the TNRCC executive director from seeking any remedy in law or equity not specifically mentioned in the rules. The Office of the Attorney General of the State of Texas cited State laws and regulations that regulate, at a minimum, the same sources as the Clean Air Act and do so with standards that are no less stringent than those specified by the CAA. The cited laws and regulations are: Texas Health and Safety Code Ann. sections 382.016 (Monitoring Requirements, Examination of Records), 382.021 (Sampling Methods and Procedures), 382.0514 (Sampling, Monitoring and Certification); 30 TAC sections 122.132 (Application and Required Information for Initial Permit Issuance, Reopening, Renewal, or General Operating Permits), 122.134 (Complete Application), 122.136 (Application Deficiencies), 122.142 (Permit Content Requirements), 122.143 (General Terms and Conditions), 122.144 (Recordkeeping Terms and Conditions), 122.145 (Reporting Terms and Conditions), 122.146 (Compliance Certification Terms and Conditions), 122.165 (Certification by Responsible Official); 30 TAC sections 101.8 (Sampling), 101.9 (Sampling Ports).

The MECT rules do not establish the number of days of violation when the cap is exceeded. Although not specifically included in the MECT EIP

submittal, if the State can demonstrate to EPA's satisfaction that it has adequate authority regarding this issue, the enforcement expectations of the EPA EIP are met.

Other TNRCC programs requiring enforcement provisions consistent with the Clean Air Act have not been found deficient by EPA. The 40 CFR part 70, Title V operating permits program and the 40 CFR part 63, National Emission Standards for Hazardous Air Pollutants (NESHAPs) are two such programs. The Office of the Attorney General of the State of Texas has provided written opinions for these programs. The opinions state that TNRCC has the necessary legal authority to implement and enforce the programs. TNRCC has the authority to have reasonable requirements for measuring and monitoring air emissions and to require owners and operators of sources to make and maintain records of the emissions. The Attorney General has determined that TNRCC is allowed to prescribe sampling methods and procedures to be used to determine violations of and compliance with the TNRCC rules and orders. EPA concluded that the TNRCC MECT EIP SIP submittal will meet the Clean Air Act requirements and EPA EIP guidance expectations for liability assessment in the integrity element of enforceable if the State demonstrates to EPA's satisfaction adequate authority regarding the number of days of violation, and the rules are amended to provide that any use of monitoring protocols other than those specified in Chapter 117 will be approved by EPA.

## 2. Enforceable Element—Penalties and Corrective Action

The expectation for provisions for penalties and corrective actions common to all trading EIPs is that the monetary and non-monetary penalty provisions in the MECT emission trading EIP will include mechanisms that enable TNRCC to assess monetary penalties and impose corrective actions against the sources participating in the EIP. These mechanisms include making up any emission shortfall, paying a monetary penalty based on statutory penalties for source noncompliance, and surrender an additional punitive amount of emission reductions. They also include implementing corrective actions to ensure the violation will not occur in the future and to compensate for the environmental damage caused by an emissions violation. These corrective actions may consist of such items as better monitors, more effective emissions controls, more frequent monitoring and reporting and better monitoring procedures. The EIP

Guidance expectation for penalty policy is described in section 5.1(c) and section 6.1(b).

The EIP Guidance expectation for penalty provisions includes provisions for imposing penalties when a source is in violation of MECT allowances, and record keeping. A program that conforms with the EIP Guidance will define a violation, establish the procedure for determining the magnitude of a violation, set potential penalties, and maintain the ability to impose a maximum monetary penalty of at least \$10,000 per day per violation. Title V of the CAA currently requires States to have a maximum penalty authority of at least \$10,000 per day per violation. The Federal CAA maximum is \$27,500 per day per violation.

The MECT EIP SIP submittal at section 101.353(c) requires that if actual emissions of NO<sub>x</sub> during a control period exceed the amount of allowances held in a compliance account on February 1 following the control period, allowances for the next control period will be reduced by an amount equal to the emissions exceeding the allowances in the compliance account plus an additional 10%. This does not preclude additional enforcement action by the TNRCC executive director.

The MECT EIP submittal was silent with respect to the authority for monetary penalty provisions up to the CAA statutory maximum on a per day and per unit basis. The Office of the Attorney General of the State of Texas has provided written opinions for the Title V operating permits program and the NESHAP program. The opinions of the Texas Attorney General indicate that TNRCC has the necessary legal authority to implement and enforce the programs in accordance with the requirements of the Clean Air Act. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for penalties and corrective action in the integrity element of enforceable.

## 3. Enforceable Element—Monitoring, Recordkeeping and Reporting

The expectation for monitoring, recordkeeping and reporting procedures is to ensure source compliance and State and Federal enforceability. Monitoring ensures the operator of the source that compliance is being achieved at all times. It also ensures an inspector that compliance has been achieved at times when the inspector is not on site to observe behavior. Retention of monitoring records ensures that the records are available for review by inspectors or source supervisors who are determining compliance.

Periodic and annual reports are also essential to summarize the compliance picture for State planning purposes, for review by the EPA and the public, as well as by source managers who wish to oversee the progress of their participation in the EIP. The EIP guidance provides the following as examples of MRR procedures: Continuous or periodic monitoring of emissions, production, activity levels, or emission control equipment operation; measurement devices to verify emission rates and operating conditions; measurement of mass emissions or emission rates using the EPA-approved reference test methods; operating and maintenance procedures or other work practices and record keeping of material usage, inventories, or throughput.

The MECT EIP SIP submittal at section 101.358 requires sources conducting compliance monitoring to use emission quantification methods. A condition for all sources in the MECT program is that they be subject to 30 TAC Chapter 117. For each source category in Chapter 117, there is a corresponding section covering the requirements for the initial demonstration of compliance, the continuous demonstration of compliance, as well as the requirements for notification, recordkeeping and reporting requirements. The following table cross references these requirements by source category.

TNRCC has submitted a revision to the MECT rule which is being parallel processed with this notice that is the

submission of emission quantification protocols. The protocols in 30 TAC Chapter 117 specify initial and continuous monitoring methodologies. These requirements in Chapter 117 have met the public notice provisions for protocols. EPA concluded that the TNRCC MECT EIP SIP submittal will meet the Clean Air Act requirements and EPA EIP guidance expectations for emission quantification protocols, monitoring, recordkeeping and reporting in the integrity element of enforceable, if, as was discussed above, any use of protocols other than those specified in Chapter 117 will be approved by EPA.

Cross Reference of MECT Source Category by Compliance, Notification, Recordkeeping, and Reporting Requirements

30 TAC Chapter 117 Source Categories	Initial Demonstration of Compliance	Continuous Demonstration of Compliance	Notification, Recordkeeping and Reporting Requirements
Utility Boilers, Auxiliary Steam Boilers & Stationary Gas Turbines .....	§ 117.111 .....	§ 117.113 .....	§ 117.119
Industrial, Commercial and Institutional Boilers, Process Heaters, Stationary Gas Turbines, I.C. Engines, FCCs, BIFs, Duct Burners, Recovery Furnaces, Lime Kilns, Lightweight Aggregate Kilns, Heat Transfer Furnaces, Magnesium Chloride Fluidized Bed Dryers & Incinerators.	§ 117.209 .....	§ 117.213 .....	§ 117.219
Acid Manufacturing—Adipic Acid Manufacturing .....	§ 117.311 .....	§ 117.113 .....	§ 117.319
Acid Manufacturing—Nitric Acid Manufacturing .....	§ 117.411 .....	§ 117.413 .....	§ 117.419
Small Combustion Sources—Water Heaters, Small Boilers and Process Heaters.	Emission Specifications § 117.465.	Certification Requirements § 117.467.	117.469
Small Combustion Sources—Boilers, Process Heaters, and stationary Engines at Minor Sources.	Emission Specifications § 117.475.	Operating Requirements § 117.478.	§ 117.479

4. Enforceable Element—Evaluation

The EIP evaluation procedure is the process of retrospectively assessing the performance of the EIP. The primary purpose of program evaluation is to determine the overall effects of the MECT EIP on emissions and measure other aspects of program performance, such as increased flexibility or reduced costs.

The EIP performance procedures may include tracking and evaluating program performance measures that were raised by the stakeholders during the rule development process. The EIP Guidance includes program evaluation procedures. A program that conforms to the EIP Guidance will include procedures that make the public aware that the program is being evaluated, and give the public ample opportunity to help evaluate the program. The EIP Guidance specifies that a program evaluation will be conducted at least every 3 years. The schedule coincides with other periodic reporting provisions such as those applicable to emission inventory revisions required by the

CAA. The EIP Guidance expectation is that the state will submit the results of the EIP program evaluation to EPA.

The evaluation program should include inspections to allow assessment of the implementation of the program and to confirm assumptions. Annual evaluation of the program is appropriate for at least 2 years, until the projected emissions have been adequately confirmed.

The MECT EIP SIP submittal at § 101.363 requires program audits every three years. The audit will evaluate the impact of the program on the state's attainment demonstration, the availability and cost of allowances, compliance by the participants, and any other elements the TNRCC executive director may choose to include. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for evaluation in the integrity element of enforceable.

5. Enforceable Element—Reconciliation

The expectation for EIP evaluation procedures is a commitment to develop

and implement reconciliation procedures if the EIP evaluation determines that source emissions exceed the allowances for a control period. The primary purpose of conducting a program reconciliation is to correct any differences between allowances versus actual emissions. This allows for the opportunity to make mid-course corrections to the program.

A program that conforms to the EIP Guidance will include an enforceable commitment that if the program evaluation shows a problem with the EIP such as emissions exceeding allowances, the problem will be corrected as expeditiously as possible. The commitment to correct the problem should be based on what may be achieved using reasonable, sustained efforts within the context of the TNRCC's rule making process. Corrections should include any revisions to the program to ensure that subsequent problems do not occur. The EIP Guidance specifies that any problem will be corrected as soon as practicable,

but no later than the next triennial program evaluation.

The MECT EIP SIP submittal at section 101.363 requires program audits every three years. The audit will evaluate the impact of the program on the state's attainment demonstration, the availability and cost of allowances, compliance by the participants, and any other elements the TNRCC executive director may choose to include. The revised attainment demonstration submittal which is being parallel processed includes a TNRCC study to be completed in 2002 which will evaluate and potentially adjust Chapter 117 emission limitations. In addition, the 2004 mid-course correction by TNRCC will evaluate control measures and enforceable commitments necessary to reach attainment in 2007. There will be an opportunity at both of these occasions to adjust allowances to reach attainment if the audit results indicate that all issued allocations are higher than assumed in the attainment demonstration. The proposed revisions to the MECT rule have a different percent reduction if section 117.106(c)(5) and section 117.206(c)(18) apply. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for reconciliation procedures in the integrity element of enforceable.

#### 6. Enforceable Element—Public Disclosure

The public disclosure provisions of an EIP were developed pursuant to the CAA (section 114(c)) and implementing regulations (40 CFR 2.301) which specify procedures and criteria for determining what information is available to the public and what information may be withheld from the public as confidential business information. These procedures and criteria apply to information in EIPs, just as they apply to information in other CAA programs.

Congress has recognized that regulatory failures can and do occur. To provide another avenue of protection, Congress ensured that the public has the right to access information and file suit in a Federal court. Because citizens have the right to bring legal actions under the CAA, a program that conforms to the EIP Guidance will ensure that the public has access to emission information. The public needs to be able to see the data in order to adequately judge the effectiveness of the EIP and exercise the right to file suit.

A program that conforms to the EIP Guidance will ensure that—

- Information will be disclosed in a manner that is transparent, allowing the public to easily and accurately calculate the emissions of each participating source,

- Facilities participating in the EIP will disclose violations to the state in an annual certification of compliance or non-compliance,

- Sources that violate permits will notify the affected community of the violation and of potential health and environmental impacts,

- The state will compile these disclosures into an annual comprehensive report on emissions and violations,

- The state will submit the report to EPA and make it available to the public, and

- The state will obtain from the participating sources and disclose to the public all information necessary to calculate every source's or source category's emissions.

The MECT EIP SIP submittal stipulates at section 101.352(i) that TNRCC will maintain a registry of allowances in each compliance account. Section 101.359 requires facilities with a compliance account to submit an ECT-1 form annually for each control period to TNRCC with account emissions and transfers. TNRCC rules at 30 TAC section 1.5 require public disclosure of information held by the agency, presumably including the annual report. There are, however, exemptions for information relating to trade secrets and "economics of operation." If these provisions are interpreted to cover activity levels, it could impede the public from obtaining information necessary to determine emissions from some units. Activity levels are necessary to determine mass emissions from sources without monitoring devices such as continuous emission monitoring systems (CEMS). This issue regarding confidentiality of records has been transmitted to TNRCC as a comment on the proposed MECT rule revisions which are being parallel processed.

The proposed revision to the MECT rule that is being parallel processed contains a new section 101.363, Program Audits and Reports. The rule at section 101.363(b) requires TNRCC to annually develop and make available to EPA and the public a report that includes the number of allowances allocated to each compliance account, the number of actual NO<sub>x</sub> allowances subtracted from each compliance account based on the actual NO<sub>x</sub> emissions from the site and a summary of all trades completed. If the State demonstrates to EPA's satisfaction that

the confidentiality provisions will not prevent public disclosure of activity level data necessary to determine emissions under the cap program, the TNRCC MECT EIP SIP submittal will meet the Clean Air Act requirements and EPA EIP guidance expectations for public disclosure procedures in the integrity element of enforceable.

#### 7. Enforceable Element—Sources With Title V Permits

The EPA EIP expectation for sources with Title V permits is that the facility's operating permit will be modified to include the detailed compliance provisions necessary to assure compliance with the EIP. Thus, the permit becomes a valuable tool to ensure the source meets the requirements of the CAA. Also, Title V program requirements, such as permit modification requirements, may not be subsumed, overridden, or otherwise affected by requirements of a discretionary EIP approved into a SIP.

Once the Title V permit includes terms and conditions necessary to implement the EIP, the source may typically make individual trades under the EIP without the need for future formal permit revisions. This is true because most trading activity under such a permit would already be addressed and allowed by the specific terms and conditions of the permit and such trading would not normally conflict with the permit. This is the principle expressed by 40 CFR 70.6(a)(8), which states that permit revisions are not required for trading program changes that are "provided for" in the permit.

Concerning permit content, the MECT EIP program would—in order to conform to the EIP Guidance—provide that sources subject to title V place a copy of any notices specified by the EIP in the operating permit file, and make these notices available to the public. These notices should be designed to provide meaningful information in the permitting context, and should help the public to determine the lawful emissions credits generated by or available to the source at any given time.

This expectation centers upon the requirement that a facility's Title V operating permit list all of the CAA requirements that apply to that facility, including monitoring and other provisions necessary to assure compliance with the MECT EIP. By identifying MECT EIP requirements as alternate operating scenarios, for instance, the modifications of the permit can be held to a minimum.

Requirements of the MECT EIP to be included in the Title V permit include the compliance, monitoring, record keeping, reporting and public notice provisions. The TNRCC MECT EIP SIP submittal did not include a showing that the TNRCC title V operating permit regulations do not interfere with the incorporation of MECT EIP provisions into title V permits as specified by section 16.8 of the EIP guidance. Since the Title V program is outside the SIP process, the expectations of this section, if not met by the facility, do not serve as grounds for not approving the MECT EIP SIP submittal and/or the attainment demonstration SIP.

#### 8. Enforceable Element—Tracking Mechanisms

The expectations for setting up tracking mechanisms in a multi-source emission cap-and-trade EIP are to facilitate a full and open trading of allowances. The EIP Guidance expectation is that the MECT EIP will have an efficient, effective method to track and record allowance transfers. The TNRCC MECT SIP submittal at section 101.353 established the allocation of allowances procedure in the MECT EIP. The allowance and authorized account representative will initially be identified by TNRCC by January 1, 2002. A secure data management system, enforceable procedure for data reporting, and time frame establishment are required by section 101.359. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for tracking mechanisms in the integrity element of enforceable.

#### Integrity Element Three—Quantifiable

The EPA EIP guidance at section 4.1(a) defines the EIP expectations for the integrity element of quantifiable for all EIPs on a programmatic basis. The EIP states that the creation and use of emission reductions are quantifiable if the source can reliably calculate the amount of emissions and/or emission reductions occurring during implementation of the program, and replicate the calculations. It further states that when quantifying results, sources will use same methodology used to measure baseline emissions, unless there are good technical reasons why this is not appropriate. The only source specific expectation for quantifiable in MECT EIPs found at section 4.1(b) is that sources will quantify total emissions per unit of time.

The EIP quantification procedures should ensure that these fundamental

elements are applied throughout the life of the EIP. For the MECT EIP, the source of the data used in quantification of allowances includes using data already reported or available. The expectation is that quantification will be performed continuously throughout the compliance period to demonstrate compliance with the allowances. A program conforming to the EIP Guidance will also include quantification protocols—the technical plans and procedures used to quantify emissions during the control period.

#### 1. Quantifiable Element—Predicting Results

The expectation for predicting EIP results is that the program include projections of the emission reductions associated with program implementation. These projected results would be based on technical assumptions related to and consistent with the assumptions used to develop the area's attainment demonstration, and provide sufficient supporting information showing what the impact would be on the applicable inventory. The MECT EIP may not interfere or be inconsistent with SIP or SIP-related requirements including the attainment plan or maintenance plan, reasonable further progress, and rate of progress. Reliable and replicable forecasts of HGA's pre- and post-EIP emission levels are part of EPA's evaluation of the SIP submittal.

The TNRCC SIP narrative for the attainment demonstration contains the emission reduction projections associated with MECT EIP implementation. The EIP SIP submittal at section 101.353(a)(3) demonstrates that the MECT has increasing reductions of NO<sub>x</sub> emissions over time in order to reach attainment. The MECT implements an approximate reduction in NO<sub>x</sub> emissions of over 80%. The reductions are achieved by implementation of the emission factors required for applicable stationary sources as found at 30 TAC sections 117.106, 117.206 and 117.475. These reduction levels were developed to support, and are consistent with, the attainment demonstration. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for predicting results in the integrity element of quantifiable.

#### 2. Quantifiable Element—Uncertainty

The expectation for addressing uncertainty is to provide greater rule effectiveness, elimination of alternative emission limits, and other environmental benefits. However,

implementing any type of EIP may result in higher or lower emissions than projected, due to geographic or timing uncertainties in emission distributions. A program that conforms to the EIP Guidance will provide a range of estimates of the emission reductions attributable to the EIP, judge the likelihood that the EIP will interfere with state air quality planning requirements and demonstrations, demonstrate that emission projections in the air quality management plan have been adjusted and determine whether that level of uncertainty is acceptable and document the decision.

The regulation for the MECT EIP was submitted with other control measure implementing regulations to be approved as part of the SIP. These implementing SIP approved rules have been determined to be necessary for the implementation of the attainment demonstration SIP. The SIP narrative for the attainment demonstration contains the degree of uncertainty associated with reaching attainment. Enforceable commitments and other measures have been incorporated in the attainment demonstration SIP. Thus the MECT EIP is an integral part of the air quality planning procedure and the measures necessary to reach attainment of the NAAQS. The MECT rules therefore will not interfere with attainment of the NAAQS, they are part of the strategy to attain those standards. Although not submitted with the MECT EIP SIP submittal, the EPA EIP guidance expectations for addressing uncertainty have been incorporated into other attainment demonstration SIP submittals.

Uncertainty is addressed in the EIP guidance at section 6.4(c). With respect to uncertainty in emissions measurement, the Chapter 117 monitoring provisions are adequate to reduce uncertainty to a reasonable level. In particular, the larger sources are required to have monitoring with the least uncertainty—CEMS and parametric emission monitoring systems (PEMS). This section of the EIP focuses on the different levels of uncertainty associated with using reductions from one type of source at another type of source, which is very relevant to using MDERCS and DERCS in the MECT. The MECT rules authorize the use of DERCS and MDERCS generated pursuant to 30 TAC Chapter 101, Subchapter H, Division 4 to comply with the annual cap. The DERC and MDERC rules are being reviewed for conformance with the EIP Guidance section 6.4(c) as part of EPA's evaluation of Subchapter H, Division 4. EPA will shortly propose action on the rules in Subchapter H,

Division 4. MDERCS and DERCS may not be utilized for compliance with MECT program annual caps until the DERCS and MDERC rules are approved by EPA. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for uncertainty in the integrity element of quantifiable.

### 3. Quantifiable Element—Approving Quantification Protocols

EIPs rely on emission quantification protocols to determine source compliance and overall program performance. An EIP quantification protocol is the technical procedure a source uses to calculate the amount of emissions associated with that source's activities under an EIP.

TNRCC has submitted a revision to the MECT rule which is being parallel processed with this notice that is the submission of emission quantification protocols. The protocols which are contained in 30 TAC Chapter 117 specify initial and continuous monitoring methodologies. These requirements in Chapter 117 have met the public notice provisions for protocols. The Chapter 117 rules do not, however, contain missing data provisions establishing how to determine emissions when required NO<sub>x</sub> monitoring equipment is not functioning properly. EIP section 5.2(c) states that protocols should contain such provisions.

EPA concluded that the TNRCC MECT EIP SIP submittal will meet the CAA requirements and EPA EIP guidance expectations for approving emission quantification protocols, if the rules are revised to specify missing data provisions as described in EIP guidance section 5.2(c).

### 4. Quantifiable Element—Selecting Emission Measurement Protocols

The expectation for the hierarchy for selecting emission measurement protocols is based upon site-specific information almost always being more reliable as an indicator of emissions than emission factors. Sources should use site-specific data whenever available or feasible. The EPA EIP guidance document recommends the following emission quantification approaches in the priority order described in the hierarchy below:

- a. CEMS data on the unit generating the emissions during the generation.
- b. CEMS data on the unit generating the emissions at a time other than the generation, but at representative conditions.

- c. Multiple emission tests at the affected unit(s) at representative conditions.

- d. Emission test at the affected unit(s) at representative conditions.

- e. Emission test at maximum load or stack tests at identical unit.

- f. Emission factors (where allowed) or material balance.

The proposed approval of this notice is based upon the review that the hierarchy for selecting emission measurement protocols has been consistent with the EPA EIP guideline document. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for selecting emission measurement protocols in the integrity element of quantifiable.

### Integrity Element Four—Permanent

The EPA EIP guidance defines the expectations for the integrity element of permanent for all EIPs on a programmatic basis. The EIP states that emission reductions are permanent if a source commits to actions or achieves reductions for a future period of time as defined in the EIP.

For compliance flexibility EIPs, the results of an EIP are permanent if you are able to ensure that no emission increases (compared to emissions if there was no EIP) occur over the time defined in the SIP. For programmatic reduction EIPs, the results of an EIP are permanent if the EIP is able to ensure that the programmatic reductions occur over the duration of the EIP rule, and for as long as they are relied on in the SIP or SIP-related requirements. The only source specific provision for permanent in MECT EIPs found at section 4.1(b) is that the integrity element of permanent does not apply to emission reductions made by sources.

The TNRCC MECT EIP SIP submittal at section 101.352(b) requires for every control period, each site to hold allowances equal to or greater than the total NO<sub>x</sub> emissions. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for the integrity element of permanent.

### Fundamental EIP Principle Two—Equity

Equity issues can be caused by an uneven distribution of emissions, or other non-emission effects. Some communities are considered communities of concern, because they have historically experienced higher emission levels than other communities in the same locale. These higher emissions often result in less healthy air quality. Equity issues may need

resolution if the EIP continues or exacerbates existing pollutant concentrations in existing communities of concern, or causes new communities to experience higher emission levels than other communities in the same locale. There are two elements that comprise the fundamental principle of equity in EIPs. They are general equity and environmental justice.

### Equity Element One—General Equity

General equity means that an EIP ensures that all segments of the population are protected from public health problems, and no segment of the population receives a disproportionate share of a program's disbenefits. The MECT EIP SIP submittal consists of an overall reduction of NO<sub>x</sub> emissions of 80%. Although allowances can be traded annually to meet compliance requirements, the overall trend at all sources will be a reduction of NO<sub>x</sub> levels. In addition, the TNRCC submittal at section 101.353(c) requires for a source, exceeding the allowances in the compliance account, allowances for the next control period to be reduced by a like amount plus an additional 10%. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for general equity in the fundamental principle of equity.

### Equity Element Two—Environmental Justice

The environmental justice element applies if the MECT EIP covers VOCs, and could disproportionately impact communities populated by racial minorities, people with low incomes, and/or Tribes. The localized hazardous air pollutant (HAP) provisions of an EIP could occur if the EIP allowed VOC HAPs to be shifted from one facility to another. Although the TNRCC MECT EIP SIP submittal is a mass cap and trade program for NO<sub>x</sub> stationary sources only, section 101.356(f) provides for sites to use VOC DERCS and MDERCs in place of allowances for compliance provided a demonstration has been made and approved by TNRCC and EPA. The use of VOC reductions in place of NO<sub>x</sub> allowances will only drive the VOC emissions lower. The MECT EIP rule does not allow VOC HAPs to be shifted from one facility to another. There is no likelihood under the MECT EIP for disproportionate impact on communities of concern. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for environmental justice in the fundamental principle of equity.

### Fundamental Principle Three— Environmental Benefit

EPA EIP expectations for the fundamental principle of environmental benefit are that a MECT EIP ensures a declining budget or emission caps that set an absolute limit on mass emissions which would otherwise have increased or would have increased at a greater rate. The TNRCC MECT EIP SIP submittal at section 101.353(a)(3) provides for increasing reductions of NO<sub>x</sub> emissions over time in order to reach attainment. In addition the MECT EIP will ensure lower NO<sub>x</sub> emissions than the implementation of 30 TAC Chapter 117 emission standards for the HGA attainment demonstration will ensure, since the MECT program limits mass emissions based on historical activity levels, and reduces the mass cap over time based on the emission rate specifications in section 117. The Chapter 117 ESAD limitations are rate based and do not limit mass emissions. Thus, the environmental benefit expectation for the MECT EIP cap on all emissions to be below the level that would have otherwise been set for the affected sources has been met. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for the fundamental principle of environmental benefit.

### Other Elements of All Trading EIPs

The other provisions of a trading EIP are discussed at § 6.5 of the EPA EIP guidance document. These include provisions for geographic trading across boundaries, provisions for notifying the relevant Federal Land Manager (FLM) in a Class I area, accounting for emission reductions that occur prior to the approval of the EIP, and restricting use of Alternative Emission Limits (AELs).

#### 1. Other Trading EIP Elements—New Source Review and Trading

The expectation is for trading EIPs to contain provisions that include new source review and trading since the NSR program may affect implementation of a trading EIP and, in turn, the EIP may affect implementation of some portions of the NSR program. To meet this expectation, sources allowed to comply with offset or netting requirements with EIP emission reductions may only use those emission reductions which independently meet relevant NSR requirements in the CAA, EPA NSR regulations and guidance, and provisions of the EPA EIP guidance document. The EIP expectation is that TNRCC will ensure that major sources and major modifications are not

exempted from any NSR or Prevention of Significant Deterioration of Air Quality (PSD) requirement because of the implementation of the MECT EIP. Another expectation is that a major source or major modification may not avoid NSR review by using an EIP except for the use of emission reductions that meet the NSR/PSD requirements for netting when the EIP emission reductions occur contemporaneously with their use and occur at the same source as the emission increase.

The TNRCC MECT SIP submittal at section 101.352(d) states that allowances cannot be used for netting requirements under 30 TAC Chapter 116, Subchapter B, Divisions 5 and 6 which relate to Nonattainment Review and Prevention of Significant Deterioration Review. However, section 101.352(e) does permit allowances to occur simultaneously to satisfy the correlating one to one portion of the offset requirements for new or modified facilities subject to federal nonattainment NSR requirements as provided at 30 TAC Chapter 116, Subchapter B, Division 7 relating to Emission Reductions Offsets. It is understood that the use of allowances for the offset requirements will be accomplished by a permanent transfer of the allowances to the source undergoing permitting. The proposed MECT revision which is being parallel processed by EPA in this notice contains the new section 101.356(c) which provides for the permanent selling of the annual allowances. The permanent transfer of the allowances would meet the requirements of section 116.115(b)(2)(C)(iii) for the life of the source. EPA concluded that if the State clarifies that the new source will have to obtain offsets for the life of the source the TNRCC MECT EIP SIP submittal will meet the Clean Air Act requirements and EPA EIP guidance expectations for new source review and trading for the category of other trading EIP elements.

#### 2. Other Trading EIP Elements— Limitations on Emission Reduction Use

The expectations are for trading EIPs to provide limitations on emission reduction use to be consistent with provisions of the CAA and other existing EPA policies. A program that conforms to this expectation will not allow the use of NO<sub>x</sub> emission reductions generated outside the modeling domain, emission reductions to meet NSPS, BACT, LAER, NSR offset requirements, title IV Acid Rain requirements, and any air toxic requirement under section 112 of the

CAA. Nor would emission reductions be used to meet various statutorily-mandated mobile source requirements, including exhaust and evaporative emission standards for both highway and non-road vehicles and engines; Federal Reid Vapor Pressure (RVP), reformulated gasoline (RFG), anti-dumping and detergent additive requirements, emission reductions to meet the municipal waste combustion rules and federally-mandated inspection/maintenance (I/M) program requirements.

The TNRCC MECT SIP submittal at section 101.351 limits the MECT EIP to only stationary sources within the eight county Houston Galveston ozone nonattainment area. The MECT EIP rule at section 101.356 does not allow the use of NO<sub>x</sub> emission reduction credits (ERCs) from 30 TAC Chapter 101, Subchapter H, Division 1 ERC EIP program for MECT banking and trading. Likewise, section 101.352(c) allows unused allowances to be used as ERCs but the use of ERCs as allowances is not permitted. DERCs or MDERCs allowed for use as allowances would by definition be surplus to the statutory mobile source, NSPS, BACT, LAER, NSR, sulfur in fuel Tier II, and municipal waste combustor (MWC) requirements. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for limitations on emission reduction use for the category of other trading EIP elements.

#### 3. Other Trading EIP Elements— Banking Emission Reductions

The expectations for trading EIPs for banking emission reductions center on emission spiking. The expectation is that, if the banking of emission reductions is allowed in the EIP, an evaluation would be performed to examine how likely it is that emission spiking will occur, and that safeguards would be included in the EIP to prevent emission spiking commensurate with the probability that spiking will occur.

The TNRCC MECT SIP submittal at section 101.356(a) allows a source participating in the EIP to bank the allowances not used in one control period to be used in the following control period. The MECT EIP also requires that the oldest allowances must be used first. This also tends to prevent carryover for more than one year and thus prevent emission spiking. The MECT rules so restrict "banking" that any potential for emissions "spiking" would be minimal. Banking is limited to just one year, and the chance of carryover to subsequent years is

minimized by section 101.354(b) (requiring Executive Director to debit most recently allocated allowances before banked allowances—thus increasing likelihood that banked allowances will expire). Use of the banking provision will be random, and with the significantly declining cap, chances of spiking should be minimal. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for banking emission reductions for the category of other trading EIP elements.

#### 4. Other Trading EIP Elements—General Conformity

The expectations for trading EIPs for general conformity are to ensure that a federal entity can not use emission reductions generated by an EIP to meet the offset or mitigation options of the general conformity requirements. The general conformity requirements will be contained in the revised general conformity rules that EPA will propose shortly. The EIP guidance will be revised as appropriate following promulgation of the general conformity rules. The EIP guidance does not specify that the MECT rules contain any provision on general conformity, so the MECT meets this EIP expectation on general conformity.

#### 5. Other Trading EIP Elements—Specific Pollutant Effects

The expectation for provisions to address specific pollutant effects may need to be included in the EIP SIP submittal. If  $\text{NO}_x$  is in the MECT EIP, provisions for localized increases in emissions of criteria pollutants in section 16.11 of the EPA EIP guidance may apply. If VOCs are in the MECT EIP, provisions for localized increases in HAPs in section 16.2 may apply. If inter-precursor trading is included in the MECT EIP, provisions for ozone inter-precursor trading in section 16.9 may apply.

With respect to localized increases on  $\text{NO}_x$ , the expectation applies to trading EIPs which can potentially exceed the annual significant emissions increase threshold of 40 tons per year (tpy). This increase applies only to emission increases above what the source was emitting before the implementation of the EIP. Since the MECT EIP will result in a substantial overall emissions decrease it is highly unlikely that this provision will be triggered.

With respect to VOCs, if the MECT EIP could cause localized increases in HAPs, the provisions of section 16.2 of the EPA EIP guidance would be applicable. Since the only potential

VOC participation in the EIP is the use of DERCs and MDERCs, there could be no increase in VOCs above the baseline. For this reason the Hazardous Air Pollutant (HAP) framework is not applicable to the MECT EIP. For the same reasons the expectations of section 16.9 of the EIP guidance for provisions for ozone inter-precursor trading are not applicable to the MECT EIP submittal. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for specific pollutant effects for the category of other trading EIP elements.

#### 6. Other Trading EIP Elements—Transportation Conformity

The expectations for trading EIPs to ensure consistency with transportation conformity are that the MECT EIP rule contain requirements that mobile sources generating mobile discrete emission reductions credits certify the reductions are not used to meet transportation conformity requirements. To meet the expectation, the EIP rule would require notification to TNRCC, the HGA Metropolitan Planning Organization (MPO), and the Texas Department of Transportation of the generator's intention to generate MDERCs. Once notified, the MPO may not use these MDERCs to satisfy the requirement for transportation conformity. The expectation is that the generator will provide enough information to the MPO about the likely emission reductions from the activity to allow the MPO to adjust its regional conformity analyses appropriately. TNRCC must also include provisions for assessing penalties against sources that use EIP MDERCs that are not surplus to transportation conformity requirements.

The MECT rules do not require notification to the MPO as stated in the EIP guidance. It is understood that any MDERC to be traded must be surplus to any state or federal law, regulation or agreed order. This would mean that the MDERC has to be surplus to the conformity analysis relied upon in the SIP attainment demonstration which is required by a federal rule. The TNRCC MECT SIP submittal at section 101.356(f) requires any MDERCs traded must be surplus in accordance with the emission quantification protocols established in 30 TAC Chapter 101, Subchapter H, Division 4. If the State commits to EPA's satisfaction to provide for notification of MDERC generation to the MPO, EPA will conclude that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for

transportation conformity for the category of other trading EIP elements.

#### 7. Other Trading EIP Elements—Inter-Credit Trading

The expectations for trading EIPs to contain provisions for inter-credit trading center on the acquisition and use of an emission reduction generated under one EIP to meet the requirements of another EIP. The expectation is that if the EIP includes inter-credit trading, the provisions of section 16.12 will be met. The TNRCC MECT SIP submittal at section 101.356(f) requires any DERCs or MDERCs traded must be generated in accordance with the emission quantification protocols established in 30 TAC Chapter 101, Subchapter H, Division 4. The DERC and MDERC rules are being reviewed for conformance with the EIP section 16.12 as part of EPA's evaluation of 30 TAC Chapter 101, Subchapter H, Division 4. EPA will shortly propose action on the rules in Subchapter H, Division 4. MDERCs and DERCs may not be utilized for compliance with MECT program annual caps until the DERC and MDERC rules are approved by EPA.

EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for inter-credit trading for the category of other trading EIP elements.

#### 8. Other Trading EIP Elements—EIPs That Include Reasonably Available Control Technology (RACT) Sources

The expectations for trading EIPs that include RACT sources are that if the EIP covers RACT sources, the provisions of the EIP guidance document section 16.13 be met. Sources with an alternative RACT limit usually are allowed to emit at a higher rate than sources covered under the presumptive RACT limit. Sources subject to presumptive and alternative RACT limits may generate reductions for use in a trading EIP. However, in a program that conforms to the EIP Guidance, the amount of the reduction would be based on application of the presumptive RACT limit rather than the alternative RACT limit. Sometimes alternative RACT determinations are considered a type of Alternative Emission Limitation. Once the MECT EIP is adopted TNRCC may not issue any new AELs.

The RACT and ESAD for the HGA area in Chapter 117 are as stringent if not more stringent than the presumptive limits contained in the Control Technology Guideline (CTG) documents. Therefore these presumptive national limits will be above the rates used to establish MECT

allowances. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for EIPs that include RACT sources for the category of other trading EIP elements.

#### 9. Other Trading EIP Elements— Geographic Trading Across Jurisdictional Boundaries

The expectations for trading EIPs for geographic trading across jurisdictional boundaries does not provide additional geographic restrictions to trading if the MECT EIP only covers areas that are not needing and lacking an attainment demonstration. In this case the geographic restrictions contained in the approved SIP will apply to the MECT EIP. The TNRCC MECT SIP submittal at section 101.351 limits the MECT EIP only to stationary sources within the eight county Houston Galveston ozone nonattainment area. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for geographical trading across jurisdictional boundaries for the category of other trading EIP elements.

#### 10. Other Trading EIP Elements— Federal Land Manager (FLM) Notification

The expectations for trading EIPs for Federal Land Manager notification in PSD Class I areas is found at section 16.6 for trading EIPs located in or within 100 km of a PSD Class I area. The nearest PSD Class I area to the HGA area is Breton Island National Wildlife preserve off the coast of Louisiana. It is more than 300 kilometers from the HGA area. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for FLM notification for the category of other trading EIP elements.

#### 11. Other Trading EIP Elements— Tracking Systems and Market Clearinghouses

The expectations for trading EIPs for tracking systems and market clearinghouses is that both TNRCC and the sources participating in trading EIPs will obtain accurate information about market activities related to trading emission reductions. Specifically, the State will obtain information that would allow the tracking of generation/use of emission reductions, ensure compliance, target enforcement resources and conduct periodic EIP performance audits. A tracking system is needed to meet these provisions. The information would be made readily available to the public.

The TNRCC MECT SIP submittal at section 101.356(e) requires all trades to be completed by the TNRCC executive director following the submittal of a completed TNRCC ECT-2 form, Application for Transfer of Allowances. The completed ECT-2 shall include the price paid per allowance. The ECT-2 shall be submitted to TNRCC at least 30 days prior to the allowances being deposited into the transferee's broker or compliance account. The TNRCC executive director will issue a letter to the purchaser and seller reflecting the trade. The trade will be considered finalized upon issuance of the letter. The MECT SIP submittal at section 101.363 requires each source to report trades annually in the compliance report using TNRCC form ECT-1. Performance audits of allowance trading is required by section 101.363. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for tracking systems and market clearinghouses for the category of other trading EIP elements.

#### 12. Other Trading EIP Elements—Multi- Claimants

The expectations for trading EIPs concerning multi-claimants focuses on certain situations where ownership of an EIP emission reduction strategy could be claimed by more than one party. When these situations occur, it is important that the MECT EIP ensure that ownership is successfully claimed by only one party to avoid double counting of reductions. From the MECT EIP SIP submittal, all sources in the cap must participate by receiving allocations of allowances as per section 101.353. The banking and trading of allowances are specified by section 101.356. The allocation, banking and trading of allowances is controlled by TNRCC at each phase by the submission and approval of forms such that there should be no practical question of ownership of allowances. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for multi-claimants for the category of other trading EIP elements.

#### 13. Other Trading EIP Elements— Emission Reductions Prior to EIP Approval

The expectations for trading EIPs address the condition that there may be sources that reduce emissions before the development of an EIP. Some generators may want these old emission reductions to participate in the trading EIP. Any emission reductions that result from emission reduction strategies that were

started before November 30, 1990 may not be allowed to participate in a trading EIP. In the MECT EIP SIP submittal at section 101.353, all sources in the cap must participate by receiving allocations of allowances. The allocations are based upon the level of activity and emission rates of all sources for the annual periods of 1997, 1998 and 1999. There is no provision for ERCs to occur prior to the approval of the EIP or outside the process of initial allocation of allowances. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for emission reductions prior to EIP approval for the category of other trading EIP elements.

#### 14. Other Trading EIP Elements— Compliance Margins

The expectation for trading EIPs for provisions for compliance margins is that the MECT trading EIP will include provisions to account for compliance margins when sources participating in an EIP are initially complying with an emission limit. The provision for compliance margins is for sources participating in an EIP to comply with an emission limit. Since the MECT EIP is based upon allowances consisting of mass emissions determined from historical actual emissions, the provision does not apply. The eighty percent reduction of emissions from historical levels will leave little if any room for compliance margins. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for compliance margins for the category of other trading EIP elements.

#### 15. Other Trading EIP Elements— Alternative Emission Limits

The trading EIPs expectation is for provisions restricting the use of alternative emission limits. Under traditional air quality management approaches, sources are required by regulation to meet emission limitations. In some cases, sources may find it difficult to meet these requirements by the required deadline. In such events, States have granted sources some form of relief (e.g., waivers, exemptions, compliance deadline extensions, and temporary relaxations to the regulatory requirements). These forms of relief are known as alternative emission limits, or AELs. While AELs may be necessary in limited cases, widespread use of AELs ultimately means that expected emission reductions will be delayed. A benefit of trading EIPs is that they provide sources an alternative means for obtaining required emission reductions

on time. This means that in many cases, sources will not need AELs as a means of regulatory relief.

The TNRCC MECT EIP SIP submittal at section 101.353 specifies that all allowances are based upon the level of activity and emission rates of all sources in the cap for the annual periods of 1997, 1998 and 1999. Once the MECT EIP is operational, if a source cannot meet the allowance limitation additional allowances must be purchased. The EIP Guidance expectation is that the MECT program will prohibit the issuance of AELs which would raise the annual cap unless the source demonstrates that it can not purchase allowances. The MECT program contains no explicit prohibition against issuance of AELs. EPA concluded that the TNRCC MECT EIP SIP submittal will meet the Clean Air Act requirements and EPA EIP guidance expectations for alternative emission limits for the category of other trading EIP elements, if the state demonstrates how existing provisions will prevent issuance of an AEL that increases an annual allocation, or the state commits not to issue such an AEL, unless the source demonstrates that it cannot acquire allowances.

#### Provisions for a Multi-Source Emission Cap-and-Trade EIP

The expectations for additional provisions needed for a multi-source emission cap-and-trade EIP are found in the EPA EIP guidance document. A multi-source emission cap-and-trade EIP is an emission trading EIP that limits the total emissions from a group of sources to a level needed for an area to attain a NAAQS, and allows sources flexibility in complying with their emission limits.

The following list presents several conditions that an EIP that conforms to the Guidance would meet to ensure the integrity of the emission cap. It also includes references to the TNRCC MECT SIP submittal which ensure the integrity of the emission cap.

- Sources have the ability to measure and report all capped emissions. TNRCC has revised the MECT rule by submitting emission quantification protocols that meet the EPA EIP guidance.

- Each affected source must designate an authorized account representative as per section 101.356(d) who is responsible for the source's emissions, trading and allowances.

- The SIP submittal demonstrated that sources cannot shift a significant amount of production, and therefore emissions, to non-affected sources outside the EIP since all regulated

stationary sources of NO<sub>x</sub> in the HGA area must participate in the MECT.

- Penalties for non-compliance are known in advance, are automatic when a unit's emissions in the control period exceed its allowances, and are equivalent to traditional CAA penalties as per TNRCC's enforcement statutes, regulations and policies.

- All the emissions, allowance, and transaction information are to be publicly available on the TNRCC world wide web site.

- The MECT EIP covers sources with RACT requirements. Rather than allow RACT sources to comply using the EIP, the MECT EIP has incorporated the RACT and limitations to reach attainment into the allowances of the EIP.

- The MECT EIP rule can not increase localized emissions of HAPs since the only use of VOCs allowed to be traded are reductions below the baseline for the attainment demonstration.

EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for additional provisions needed for a multi-source emission cap and trade EIP.

#### 1. Other Multi-Source Cap & Trade Provisions—Setting the Budget

The expectations for setting the budget for a multi-source emission cap-and-trade EIP are that the program baseline for the cap-and-trade program will be no greater than the sum of the historical average emissions of the participating sources.

The MECT program baseline is based almost entirely on the sum of historical emissions from sources in the program. For some newer sources, allocations are based on allowable emissions for two years, but this is only until an actual emissions baseline is established as required by 30 TAC 101.353(a)(2)(B) and (4)(B).

EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for setting the budget needed for a multi-source emission cap and trade EIP.

#### 2. Other Multi-Source Cap & Trade Provisions—Defining the Affected Sources

The expectations for defining the affected sources for a multi-source emission cap-and-trade EIP are found at section 7.4(c) of the EPA EIP guidance document. A multi-source emission cap-and-trade EIP contains a certain set of sources. The aggregate emissions from these sources are capped. The emission cap aspect of a multi-source emission

cap-and-trade EIP will be compromised, however, if TNRCC defines the population of sources in a way that allows production from sources covered under the EIP to shift to those that are not covered. The TNRCC MECT SIP submittal at section 101.351 establishes the MECT EIP cap for stationary sources with emissions greater than 10 tpy. Significant emission shifts are unlikely since any sources with emissions less than 10 tpy whose sources increase above 10 tpy are required to obtain allowances from other sources and become part of the cap. Section 101.353(b) requires new or modified sources not in the cap to obtain allowances for each control period from sources participating in the MECT EIP. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for defining the affected sources for a multi-source emission cap and trade EIP.

#### 3. Other Multi-Source Cap & Trade Provisions—Opt-in Sources

The expectations for provisions for opt-in sources in a multi-source emission cap-and-trade EIP are found at section 7.4(d) of the EPA EIP guidance document. Additional sources may want to "opt-in" to the multi-source cap-and-trade EIP. These additional sources could be smaller, located in a different geographic area, or represent another sector than the originally defined affected sources. All trading units are within the HGA area. There is no provision for opt-ins. Section 101.353(b) requires new or modified sources not in the cap to obtain allowances for each control period from sources participating in the MECT EIP. The TNRCC MECT SIP submittal at section 101.353(b) requires new or modified sources not in the cap to obtain allowances for each control period from sources participating in the MECT EIP. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for opt-in sources for a multi-source emission cap and trade EIP.

#### 4. Other Multi-Source Cap & Trade Provisions—Distributing Allowances

The expectations for provisions for distributing allowances in a multi-source emission cap-and-trade EIP are found at section 7.4(e) of the EPA EIP guidance document. The expectation is that after the emission budget is set, the population of covered sources would receive a share of the emission budget. Factors that may be used to assign a share of the budget include historical,

current or projected emission levels and existing control technology requirements. The TNRCC MECT SIP submittal at section 101.351 applies to all stationary NO<sub>x</sub> facilities subject to TNRCC Rule 117 emission specifications at sites with emissions design capacity above 10 tpy in the HGA ozone nonattainment area. The emission budget in the MECT EIP was established based on historical emission levels. From section 101.351(a), the initial allowances in the MECT EIP will be based on the actual historical emissions for each source from 1997, 1998 and 1999. Section 101.351(a)(3) requires three steps from January 1, 2002 through April 1, 2007 where the allowances are reduced to reach the final goal of approximately 80% overall reduction from the historical levels. The program will be audited every three years to evaluate its impact on the attainment demonstration. The TNRCC Executive Director will recommend any measures necessary to remedy problems.

The revised attainment demonstration submittal which is being parallel processed includes a TNRCC study to be completed in 2002 which will evaluate and potentially adjust Chapter 117 emission limitations. In addition to the 2004 mid-course correction by TNRCC will evaluate control measures and enforceable commitments necessary to reach attainment in 2007. There will be an opportunity at both of these occasions to readjust allowances to reach attainment if the audit results indicate that all issued allocations are higher than assumed in the attainment demonstration.

Section 101.353(g) of the MECT Rules states that in "extenuating circumstances" the TNRCC executive director may deviate from the requirements for determining the amount of allowances to be issued to a facility. TNRCC explained the purpose of this provision as being to "prevent significantly low allocations" in "extraordinary circumstances, for example a catastrophe which required a facility to shut down during the historic period upon which allocations would normally be based." TNRCC Chapter 101 Rule Log No. 1998-089-101-AI, at 74. Existing sources that wish to utilize section 101.353(g) were required by paragraph (1) of the rule to file applications by June 30, 2001. We are informed that approximately 15 sources filed applications by the deadline, and that their NO<sub>x</sub> emissions represent approximately one half of one percent of total emissions regulated by the MECT program.

Section 101.353(g) allows executive director discretion. It is expected, however, that prior to the time that EPA takes final action on the MECT rules, the state will have made decisions on all applications that were submitted by June 30, 2001. In order for EPA to approve the MECT rules, the state must demonstrate prior to final EPA action that any allocations issued pursuant to section 101.353(g)(1) are not inconsistent with the attainment demonstration, and comply with the CAA.

Paragraph (2) of section 101.353(g) allows a finite group of relatively new sources to submit applications after June 30, 2001. In order for EPA to approve the MECT rules, the state must either (1) demonstrate that the allocations that could be issued pursuant to section 101.353(g)(2) would not be inconsistent with the attainment demonstration and would comply with the CAA, or (2) modify the rule to eliminate executive director discretion or require EPA approval of any allocation issued pursuant to paragraph (g)(2).

EPA concluded that the TNRCC MECT EIP SIP submittal will meet the Clean Air Act requirements and EPA EIP guidance expectations for distributing allowances for a multi-source emission cap and trade EIP, if the above-described demonstrations or modifications are made.

#### 5. Other Multi-Source Cap & Trade Provisions—Emissions Banking

The TNRCC MECT SIP submittal at section 101.356(a) allows a source participating in the EIP to bank the allowances not used in one control period to be used in the following control period. The EIP Guidance expectation at section 16.15 is that a banking EIP would safeguard against emissions spiking. The MECT rules so restrict "banking" that any potential for emissions "spiking" would be minimal. Banking is limited to just one year, and the chance of carryover to subsequent years is minimized by section 101.354(b)(requiring Executive Director to debit most recently allocated allowances before banked allowances—thus increasing likelihood that banked allowances will expire). Use of the banking provision will be random, and with the significantly declining cap, chances of spiking should be minimal. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for emissions banking for a multi-source emission cap and trade EIP.

#### 6. Other Cap & Trade Provisions—Allowing Shutdowns to Generate Reductions

Shutdowns may be allowed to generate emission reductions within the context of a multi-source cap-and-trade program if the emissions reductions resulting from the shutdown are still in the applicable emissions inventory and the EIP has provisions to address shifting demand. The MECT EIP at section 101.353(h) states that if allowances are being allocated based on allowable emissions and the facility does not achieve two complete consecutive calendar years of actual level of activity data, then allowances will not continue to be allocated if the facility ceases operation or is not built. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for allowing shutdowns to generate reductions for a multi-source emission cap and trade EIP.

#### 7. Other Cap & Trade Provisions—Shifting Demand

Shifting of activity levels is a potentially serious problem for all multi-source cap-and-trade EIPs. A source in a cap could decide to shift production to a source outside the cap within the same non-attainment area. Shifting demand from sources within the cap to sources outside the cap is unlikely to occur due to the fact that the regulated industries (refineries, petrochemical, chemical, etc.) are made up of relatively large sources. In other words, all significant sources that could do the work performed by capped sources are also within the cap. The under 10 ton sources just are not capable of assuming any significant portion of the activity. If emissions at a non-capped source increase to over ten tons per year, it will become regulated under the cap. It was concluded that significant shifting of demand is unlikely to occur, due to the nature of the EIP. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for shifting demand for a multi-source emission cap and trade EIP.

#### 8. Other Cap & Trade Provisions—True-up Period

Within the context of a multi-source emission cap-and-trade EIP a source may be allowed to obtain emission allocations after the end of the compliance period. The time between the end of the compliance period and when the source would demonstrate compliance is called the true-up period.

The length of a true-up period should be based on the length of the compliance period. In general, for a compliance period of several months up to a year the true-up period should not be more than 60 days. For shorter compliance periods the true-up period should be shorter than 60 days. The MECT EIP at section 101.352(b) and at section 101.354(d) requires each site no later than March 1 of each year to hold a quantity of allowances in its compliance account that equals or exceeds the total emissions of NO<sub>x</sub> emitted during the control period just ended. This requirement will begin March 1, 2003. This "true up" period is 60 days. EPA concluded that the TNRCC MECT EIP SIP submittal meets the Clean Air Act requirements and EPA EIP guidance expectations for a true-up period for a multi-source emission cap and trade EIP.

#### D. Conclusion

EPA reviewed the TNRCC MECT SIP submittal with respect to the expectations of the EPA EIP Guidance document and the requirements of the Clean Air Act. Overall EPA has concluded, after review and analysis, that the TNRCC MECT EIP regulation can provide a positive contribution toward the attainment of the one-hour ozone standard in the HGA area. EPA proposes to conclude that the program will satisfy all requirements of the Clean Air Act, if certain modifications and/or demonstrations described above are made.

## II. Background

### A. Date of State's SIP Submission

What Was the Date of the State's SIP Submission?

EPA received the proposed MECT SIP revision submitted by the TNRCC on December 22, 2000. The MECT SIP revision consisted of new sections to 30 TAC Chapter 101, Subchapter H, Division 3 which had been promulgated by TNRCC in December 2000. The MECT regulation is found at new sections 101.350 through 101.363. The Governor submitted revisions to the MECT submittal by letter dated June 15, 2001 and requested parallel processing of the revisions.

Was the TNRCC MECT Rule Subject to Public Notice?

The TNRCC held public hearings on the proposed MECT rules at the following locations: September 18, 2000, in Conroe and Lake Jackson; September 19, 2000 in Houston (2 hearings); September 20, 2000, in Katy and Pasadena; September 21, 2000, in

Beaumont, Amarillo, and Texas City; September 22, 2000, in Dayton, El Paso, and Arlington; and September 25, 2000, in Austin and Corpus Christi. The comment period closed at 5 p.m. on September 25, 2000. Fifteen individuals opposed the cap and trade concept. Eight individuals expressed general support for the cap and trade concept. The public input was incorporated into the final TNRCC regulation.

What Are the Sections of the MECT Rule?

New section 101.350 contains definitions of terms used in the rule. Other sections are: section 101.351 Applicability, section 101.352 General Provisions, section 101.353 Allowances, section 101.354, Allowance Deductions, section 101.356 Allowance Banking and Trading, section 101.358 Emission Monitoring and Compliance Demonstration, section 101.359 Reporting and section 101.360 Level of Activity Certification. The revised MECT rule contains section 101.363, Program Audits and Reports.

### B. General Criteria for an EIP

What Are the General Criteria for an EIP?

The document, Improving Air Quality with Economic Incentive Programs, (EPA-452/R-01-001) January 2001 is the EPA guideline for discretionary EIP submittals for SIP credit. As previously stated, the guidance document does not represent the EPA's final action for any discretionary EIP. Final action occurs when the EPA has approved or disapproved the discretionary EIP submitted as a SIP revision.

What Is the Applicability of Previous EPA EIP Regulations and Guidance?

The EPA EIP Guidance will take precedence over the discretionary EIP guidance provided in prior documents such as the 1994 EIP (published at 59 FR 16690) and the guidance in the emission trading policy statement (ETPS) (published on December 4, 1986 at 51 FR 43813). In addition, the guidance represents the EPA's final action on the Open-Market Trading Rule (OMTR) (proposed in August 3, 1995 at 60 FR 39668, and on August 25, 1995 at 60 FR 44290). While the proposed OMTR rule was never made final, the EPA EIP Guidance addresses the public comments received for that proposal, and provides guidance on other types of EIPs as well. These previously published documents provide supplementary information and useful background for designing an EIP. The requirements for mandatory EIPs remain

in the Code of Federal Regulations (CFR), title 40, part 51, subpart U (59 FR 16690).

How Does the EPA EIP Guidance Affect the EPA's 1994 EIP Rule?

The EPA's 1994 EIP rule established requirements for mandatory EIPs, and guidance for discretionary EIPs. The rule still remains in effect for mandatory EIPs. The new EPA EIP document updates the guidance the EPA's 1994 EIP rule provides for developing discretionary EIPs. The EPA removed § 51.490(b) of the EPA's 1994 EIP rule when the final version of the EIP guidance was published.

Why Was the EPA EIP Guidance Developed?

The EPA intended for the EPA EIP to be the primary guidance for use in EIP development. The EPA intended for the EIP guidance to achieve the following:

- Update the existing guidance using a new plain language format.
- Tie together, for reference purposes, all of the existing related guidance in one document.
- Provide additional information on issues not discussed in previously existing guidance.

The EPA EIP guidance document provides strategic advice on choosing a program and determining which sources to include in the program. It provides information on using emission reductions attributable to a discretionary EIP to meet the air quality-related programs such as SIP or SIP-related requirements. It also discusses the important tasks in program implementation such as tracking and evaluation.

What Are the Goals of the EPA EIP Guidance?

The goals of the EPA EIP guidance are as follows:

- Define economic incentive programs.
- Select the best type of EIP for a given situation.
- Provide help in understanding the process for getting an EIP rule approved as part of the SIP.
- Provide the information needed to implement an approved EIP.
- Provide information regarding evaluation and updating an approved EIP.
- Describe other guidance that might be applicable.

Is the EPA EIP Guidance Information on the Program-Level or the Source-Level?

Both, the guidance provides information at two levels, a program-level and a source-level. Program-level

guidance applies to the EIP as a whole. States are primarily responsible for implementing these provisions. Source-level guidance applies to specific sources participating in the EIP. While the State is responsible for establishing the appropriate requirements for sources in the rule, the sources themselves are responsible for implementing these other provisions. Program-level and source-level guidance will apply to the majority of EIPs, but there are some exceptions where source-level guidance is not applicable. The EPA intended the guidance to be a "living document," and plans to update the guidance periodically as the EPA establishes new policies and standards.

#### How Will EPA Act on an EIP SIP Submittal?

Once an EIP SIP revision is submitted, EPA will take action through notice-and-comment rule making to determine if the statutory requirements have been met. Only action taken after the conclusion of that rulemaking would constitute final Agency action. The EPA would take steps to expedite its proposed approval in the case of SIP revisions containing programs that contain the elements of the EPA EIP guidance.

If a program that does not contain the elements of the EPA EIP guidance for that type of program is submitted, EPA would still seek to determine whether the applicable CAA requirements were met, and, if so, EPA would approve the submission. The EPA would make the determination through notice-and-comment rule making.

### III. Administrative Requirements

Under Executive Order 12866 (58 FR 51735, October 4, 1993), this proposed action is not a "significant regulatory action" and therefore is not subject to review by the Office of Management and Budget. For this reason, this action is also not subject to Executive Order 13211, "Actions Concerning Regulations That Significantly Affect Energy Supply, Distribution, or Use" (66 FR 28355, May 22, 2001). This proposed action merely proposes to approve state law as meeting federal requirements and imposes no additional requirements beyond those imposed by state law. Accordingly, the Administrator certifies that this proposed rule will not have a significant economic impact on a substantial number of small entities under the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*). Because this rule proposes to approve pre-existing requirements under state law and does not impose any additional enforceable duty beyond that required by state law,

it does not contain any unfunded mandate or significantly or uniquely affect small governments, as described in the Unfunded Mandates Reform Act of 1995 (Public Law 104-4). This proposed rule also does not have a substantial direct effect on one or more Indian tribes, on the relationship between the Federal Government and Indian tribes, or on the distribution of power and responsibilities between the Federal Government and Indian tribes, as specified by Executive Order 13175 (65 FR 67249, November 9, 2000), nor will it have substantial direct effects on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government, as specified in Executive Order 13132 (64 FR 43255, August 10, 1999), because it merely proposes to approve a state rule implementing a federal standard, and does not alter the relationship or the distribution of power and responsibilities established in the Clean Air Act. This proposed rule also is not subject to Executive Order 13045 (62 FR 19885, April 23, 1997), because it is not economically significant.

In reviewing SIP submissions, EPA's role is to approve state choices, provided that they meet the criteria of the Clean Air Act. In this context, in the absence of a prior existing requirement for the State to use voluntary consensus standards (VCS), EPA has no authority to disapprove a SIP submission for failure to use VCS. It would thus be inconsistent with applicable law for EPA, when it reviews a SIP submission, to use VCS in place of a SIP submission that otherwise satisfies the provisions of the Clean Air Act. Thus, the requirements of section 12(d) of the National Technology Transfer and Advancement Act of 1995 (15 U.S.C. 272 note) do not apply. As required by section 3 of Executive Order 12988 (61 FR 4729, February 7, 1996), in issuing this proposed rule, EPA has taken the necessary steps to eliminate drafting errors and ambiguity, minimize potential litigation, and provide a clear legal standard for affected conduct. EPA has complied with Executive Order 12630 (53 FR 8859, March 15, 1988) by examining the takings implications of the rule in accordance with the "Attorney General's Supplemental Guidelines for the Evaluation of Risk and Avoidance of Unanticipated Takings" issued under the executive order. This proposed rule does not impose an information collection burden under the provisions of the

Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*).

#### List of Subjects in 40 CFR Part 52

Environmental protection, Air pollution control, Intergovernmental relations, Nitrogen dioxide, Nonattainment, Ozone, Reporting and recordkeeping requirements, Volatile organic compounds.

Dated: July 16, 2001.

Gregg A. Cooke,

Regional Administrator, Region 6.

[FR Doc. 01-18318 Filed 7-20-01; 8:45 am]

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## DEPARTMENT OF TRANSPORTATION

### National Highway Traffic Safety Administration

#### 49 CFR Part 573

[Docket No. NHTSA-2001-9599]

RIN 2127-A130

#### Motor Vehicle Safety; Limitations on Sale and Lease of Noncompliant and Defective Motor Vehicles and Items of Motor Vehicle Equipment

**AGENCY:** National Highway Traffic Safety Administration (NHTSA), DOT.

**ACTION:** Notice of proposed rulemaking (NPRM).

**SUMMARY:** NHTSA proposes to add regulations limiting the sale or lease of noncompliant and defective motor vehicles and items of motor vehicle equipment. The Intermodal Surface Transportation Efficiency Act (ISTEA) and the Transportation Recall Enhancement, Accountability, and Documentation (TREAD) Act amended federal motor vehicle safety laws by limiting the sale or lease of defective and noncompliant vehicles and equipment. The proposed rules would codify the limitations set forth in ISTEA and the TREAD Act and reduce questions relating to the meaning of those limitations.

**DATES:** *Comment Closing:* Comments must be received by September 21, 2001. The effective date of a final rule based on this proposal would be 30 days after publication of the final rule.

**ADDRESSES:** You should mention the docket number of this document in your comments, and submit your comments in writing to: Docket Management, Room PL-401, 400 Seventh Street, SW., Washington, D.C. 20590. Comments may also be submitted to the docket electronically by logging onto the Dockets Management System website at