

SOUTH COAST AIR QUALITY MANAGEMENT DISTRICT

Draft Staff Report Proposed Amendments to Regulation XX – Regional Clean Air Incentives Market (RECLAIM)

Proposed Amended Rules 2001 – Applicability and 2002 – Allocations for Oxides of Nitrogen (NO_x) and Oxides of Sulfur (SO_x)

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Background

The South Coast Air Quality Management District (SCAQMD) Governing Board adopted the Regional Clean Air Incentives Market (RECLAIM) program in October 1993. The purpose of RECLAIM is to reduce NOx and SOx emissions through a market-based approach. The program replaced a series of existing and future command-and-control rules and was designed to provide facilities with the flexibility to seek the most cost-effective solution to reduce their emissions. It also was designed to provide equivalent emission reductions, in the aggregate, for the facilities in the program compared to what would occur under a command-and-control approach. Regulation XX includes a series of rules that specify the applicability and procedures for determining NOx and SOx facility emissions allocations, program requirements, as well as monitoring, reporting, and recordkeeping requirements for sources located at RECLAIM facilities. Regulation XX – RECLAIM was most recently amended on December 4, 2015 and October 7, 2016. The December 2015 amendment was designed to achieve programmatic NOx RECLAIM trading credit (RTC) reductions of 12 tons per day from compliance years 2016 through 2022 and the October 2016 amendment was to address RTCs from facility shutdowns.

In response to concerns regarding actual emission reductions in the RECLAIM program under a market-based approach, Control Measure CMB-05 of the 2016 Air Quality Management Plan (AQMP) committed to an assessment of the RECLAIM program in order to achieve further NOx reductions of five tons per day, including actions to sunset the program and ensure future equivalency to command-and-control regulations. During the adoption of the 2016 AQMP, the Resolution directed staff to modify Control Measure CMB-05 to achieve the five tons per day NOx emission reduction as soon as feasible but no later than 2025, and to transition the RECLAIM program to a command-and-control regulatory structure requiring Best Available Retrofit Control Technology (BARCT) level controls as soon as practicable. Staff provided a report on transitioning the NOx RECLAIM program to a command-and-control regulatory structure at the May 5, 2017 Governing Board meeting and provides quarterly updates to the Stationary Source Committee with the first quarterly report provided on October 20, 2017.

On July 26, 2017 California State Assembly Bill 617 was approved by the Governor, which addresses non-vehicular air pollution (criteria pollutants and toxic air contaminants). It is a companion legislation to Assembly Bill 398, which was also approved, and extends California's cap-and-trade program for reducing greenhouse gas emissions from stationary sources. RECLAIM facilities that are in the cap and trade program are subject to the requirements of AB 617. Among the requirements of this bill is an expedited schedule for implementing BARCT for cap and trade facilities. Air Districts are to develop by January 1, 2019 an expedited schedule for the implementation of BARCT no later than December 31, 2023. The highest priority would be given to older, higher polluting units that will need to install retrofit controls.

Staff conducted a programmatic analysis of the RECLAIM equipment at each facility to determine if there are appropriate and up to date BARCT NOx limits within existing SCAQMD command-and-control rules for all RECLAIM equipment. It was determined

that command-and-control rules would need to be adopted and/or amended to provide implementation timeframes for achieving BARCT compliance limits for certain RECLAIM equipment and to also update some of these rules if the emission limits do not reflect current BARCT. Staff also determined that there are some RECLAIM facilities that either do not have any NO_x emissions, report only NO_x emissions from equipment that is exempt from permitting (e.g., Rule 219 equipment), or operate RECLAIM equipment that is already meeting BARCT. The RECLAIM transition will first address those facilities that can operate under a command-and-control regulatory structure without undergoing any equipment modifications to meet BARCT. Subsequent transitioning of facilities will involve command-and-control rule amendments that will address RECLAIM equipment which will require the installation of BARCT.

Proposed Amended Rules 2001 and 2002 will initiate the transition of the NO_x and SO_x RECLAIM program to a command-and-control regulatory structure by precluding any new, non-RECLAIM facilities from entering into RECLAIM. Staff is not proposing future rulemaking to transition SO_x RECLAIM at this time to allow staff to focus resources on the transition of NO_x RECLAIM to a command and control regulatory structure. In preparation for facilities in the RECLAIM program to transition to command and control, the proposed amendments will address the RTC holdings for the initial wave of facilities that will be exited from RECLAIM or that elect to exit RECLAIM, as well as establishing notification procedures for RECLAIM facilities for their transition out of the program.

Public Process

Staff has held monthly working group meetings to discuss the transition of the NO_x RECLAIM program and to discuss numerous key issues and challenges. Staff has also met individually with numerous facility operators and industry groups regarding the transition. A public consultation meeting was held on November 8, 2017, with the comment period closing on November 22, 2017. Responses to comments received are provided in Appendix A of this staff report.

Affected Facilities

There are currently 266 facilities in the NO_x RECLAIM program and 31 facilities in the SO_x RECLAIM program. These 31 facilities in the SO_x program are also in NO_x RECLAIM. These facilities either had NO_x emissions greater than or equal to four tons per year in 1990 or any subsequent year or elected to enter the program. The proposed amendments would apply to any facility in the NO_x RECLAIM program that will be transitioned. Any facility outside of RECLAIM that exceeds four tons per year of NO_x or SO_x emissions would no longer be allowed into RECLAIM.

Summary of Proposal

The proposed amendments to Regulation XX will affect Rule 2001 – Applicability and Rule 2002 – Allocations for Oxides of Nitrogen (NO_x) and Oxides of Sulfur (SO_x).

Proposed Amended Rule (PAR) 2001

Rule 2001 specifies inclusion criteria into the RECLAIM program for new and existing facilities, as well as for facilities that elect to enter into the program. The proposed change to the applicability would also establish a final date for any new facility inclusions into RECLAIM.

The Executive Officer maintains a listing of all RECLAIM facilities. The proposed amendments would include new or existing facilities into the NO_x and SO_x RECLAIM programs only up until the date of amendment. Subdivision (b) would state:

“The Executive Officer will maintain a listing of facilities which are subject to RECLAIM. The Executive Officer will include facilities up until (date of amendment)...”

Subdivision (c) addresses amendments to the RECLAIM facility listing. Subparagraphs (c)(1)(C), (c)(1)(D), and (c)(1)(E) specify actions for inclusion of any new facility that would be subject to RECLAIM, any existing facility that would be subject to RECLAIM, and for any existing non-RECLAIM facility that elects to enter the program. Since no more inclusions will be allowed under the proposed amendments, these subparagraphs will be removed. Additionally, since the inclusion of outer continent shelf (OCS) facilities into RECLAIM as a result of EPA delegation of authority occurred during the program’s implementation and no additional OCS facilities will be included, subparagraph (c)(1)(F) will be removed. Proposed subparagraph (c)(1)(C) would require the Executive Officer to amend the RECLAIM facility listing:

“Upon the transition of a facility out of RECLAIM, pursuant to Rule 2002.”

Subdivision (f), Entry Election, contains provisions for non-RECLAIM facilities that may elect to enter RECLAIM. Since no more inclusions will be allowed under the proposed amendments, these provisions will be removed and replaced with:

“On and after (date of amendment), a non-RECLAIM facility may not elect to enter the RECLAIM program.”

The proposed amendments to Rule 2001 would prevent any further inclusions of non-RECLAIM facilities into both the NO_x and SO_x RECLAIM programs.

Proposed Amended Rule (PAR) 2002

Rule 2002 establishes the methodology for calculating RECLAIM facility allocations and adjustments to RECLAIM Trading Credit (RTC) holdings for NO_x and SO_x. The proposed amendments will contain the notification procedures for facilities that will be transitioned out of RECLAIM and will address the RTC holdings for these facilities that will be transitioned out of RECLAIM or that elect to exit RECLAIM. These provisions will be contained in new proposed paragraphs (f)(6) through (f)(9), which will detail how a facility will be notified regarding the transition.

As a facility is identified to transition out of RECLAIM, the Executive Officer will provide a written letter to notify a RECLAIM facility that it is under review for transition by way of an initial determination notification. This initial notification will also include an existing list of NO_x emitting equipment and a request for the owner or operator of the RECLAIM facility to confirm the RECLAIM source equipment at the facility, as well as to identify any NO_x emitting equipment that is not subject to permitting requirements (e.g., Rule 219 permit exempt equipment). The RECLAIM facility would be required to provide an identification of all NO_x emission equipment (including equipment that is exempt from permitting) within 45 days of the date of the initial determination notification. The facility can also respond and provide information to the Executive Officer to confirm that it is ready for the transition to command-and-control. A facility is ready to transition into command-and-control if:

- a) All equipment is at BARCT; or
- b) The applicable equipment command-and-control rules have been adopted and/or amended to reflect current BARCT.

Proposed paragraph (f)(6) states:

“If the Executive Officer provides the owner or operator of a NO_x RECLAIM facility with an initial determination notification that their facility is under review for being transitioned out of NO_x RECLAIM, the owner or operator shall submit to the Executive Officer within 45 days of the initial determination notification date the identification of all NO_x RECLAIM emission equipment, including Rule 219 exempt equipment. The Executive Officer will review the information submitted and, if complete, determine if the facility will be transitioned out of the NO_x RECLAIM program.”

Proposed subparagraphs (f)(6)(A) and (f)(6)(B) address facilities that fail to respond to the initial notification determination and facility submissions that are incomplete. In proposed subparagraph (f)(6)(A), the Executive Officer will notify a facility if its submission of information is not complete and will provide a timeline for the submission of the complete information. If a facility fails to submit the requested information within 45 days of the initial determination notification date or fails to revise an incomplete submission by the timeline provided by the Executive Officer, proposed subparagraph (f)(6)(B) states that this would result in:

“...the prohibition on all RTC uses, sales, or transfers by the facility until all requested information is submitted.”

If the notified facility, after responding, is deemed as ready to transition into command-and-control after review by the Executive Officer, it will receive a final determination notification that it will be removed from RECLAIM and be subject to command-and-control regulations [proposed paragraph (f)(7)]. Staff has initially identified 38 RECLAIM facilities that can be removed from the program. These facilities either have no NO_x emissions or have emissions solely from the combination of the following:

- (A) *Rule 219 equipment, unless it would be subject to a command-and-control rule that it cannot reasonably comply with, various location permits, or unpermitted equipment; and/or*
- (B) *RECLAIM source equipment that meets current command-and-control BARCT rules*

These criteria are listed in proposed subparagraphs (f)(7)(A) and (f)(7)(B). Some facilities have NO_x emissions only coming from the equipment types listed in (f)(7)(A) and not from RECLAIM source equipment, which consists of process units, large sources, and major sources. Other facilities may operate RECLAIM source equipment (e.g., process units, large source, and major sources), but this equipment meets the emission requirements in current command-and-control regulations.

Certain Rule 219 equipment (e.g., small boilers and heaters) would be subject to SCAQMD Rule 1146.2 upon exit from RECLAIM. Some existing Rule 219 equipment or other unpermitted equipment, if exited from RECLAIM and subject to command-and-control rules, would not comply with the current requirements. To prevent this situation of exiting RECLAIM facilities with equipment that would be subject to command-and-control rules that it cannot reasonably comply with, proposed paragraph (f)(8) would withhold these facilities from exiting the RECLAIM program:

“In the event that the Executive Officer, upon review of the information pursuant to paragraphs (f)(6) and (f)(7), nonetheless determines that a facility should not yet be transitioned out of the NO_x RECLAIM program, the owner or operator will be notified.

If it is determined that a facility is deemed as not ready to exit from RECLAIM and is notified, it will remain in RECLAIM until a subsequent notification and determination is made to exit.

Proposed paragraph (f)(9) outlines requirements pertaining to RTCs for facilities that are notified for exiting RECLAIM. It states that:

“Any RECLAIM facility that receives a final determination notification from the Executive Officer pursuant to paragraph (f)(7) shall not sell or transfer any future compliance year RTCs as of the date specified in the final determination notification and may only sell or transfer current compliance year RTCs until the facility is transitioned out of the RECLAIM program.”

If, after review, a RECLAIM facility receives a final determination notification, then the facility would not be able to sell any future compliance year RTCs by a date certain as specified in the notification, but only the current compliance year RTCs until the facility exits RECLAIM. Some stakeholders have expressed concern regarding the ability to transfer RTCs from exiting facilities to other facilities in RECLAIM that are under common ownership. RECLAIM facilities can transfer or sell RTCs until the date specified in the final determination notification. The basis for establishing an RTC

“freeze” is to minimize sell-offs of credits to facilities that will remain in RECLAIM after this first wave of exiting facilities. In addition, it will provide staff time for analysis and preserve future options for the use of RTCs.

The proposed amendments will establish the procedures for the initial wave of facilities that will exit the RECLAIM program and transition from a programmatic to a command-and-control regulatory structure. Future amendments to the notification procedures will be proposed as needed to accommodate other groups of facilities transitioning out of RECLAIM.

Emission Reductions and Cost Effectiveness

The proposed amendments do not result in any significant effect on air quality and do not result in any emissions limitation. As a result, a cost effectiveness analysis is not required.

AQMP and Legal Mandates

The California Health and Safety Code requires the SCAQMD to adopt an Air Quality Management Plan to meet state and federal ambient air quality standards and adopt rules and regulations that carry out the objectives of the AQMP. This proposed amendment of Regulation XX (Proposed Amended Rules 2001 and 2002) initiates the transition of the RECLAIM program to a command-and-control regulatory structure in order to achieve the commitments of Control Measure CMB-05 of the Final 2016 AQMP.

California Environmental Quality Act (CEQA)

SCAQMD staff has reviewed the proposed amendments to Rule 2001 and Rule 2002 pursuant to: 1) CEQA Guidelines Section 15002(k) – General Concepts, the three-step process for deciding which document to prepare for a project subject to CEQA; and 2) CEQA Guidelines Section 15061 – Review for Exemption, procedures for determining if a project is exempt from CEQA. The effect of preventing any new or existing non-RECLAIM facility that emits four or more tons per year of NO_x or SO_x from entering the RECLAIM program would result in no change to these facilities in continuing to be subject to their current permits and/or all applicable non-RECLAIM, SCAQMD Rules and Regulations. Further, the action of identifying facilities that will be transitioning out of the RECLAIM program will not alter the applicability of SCAQMD Rules and Regulations on the identified facilities. Thus, the proposed amendments to Rule 2001 would not be expected to cause any physical changes that would affect emissions or any other environmental topic area. Similarly, the proposed amendments to Rule 2002 establishing procedures for notifying facilities to be transitioned out of the NO_x RECLAIM program, and addressing the use of RTCs during the transition period for the set of facilities are also not be expected to cause any physical changes that would affect emissions or any other environmental topic area. Therefore, SCAQMD staff has determined that it can be seen with certainty that there is no possibility that the proposed

amendments to Rule 2001 and Rule 2002 may have a significant adverse effect on the environment. Thus, the proposed amendments to Rule 2001 and Rule 2002 are considered to be exempt from CEQA pursuant to CEQA Guidelines Section 15061(b)(3) – Activities Covered by General Rule. A Notice of Exemption has been prepared pursuant to CEQA Guidelines Section 15062 - Notice of Exemption. If the proposed project is approved, the Notice of Exemption will be filed with the county clerks of Los Angeles, Orange, Riverside and San Bernardino counties.

Socioeconomic Analysis

PAR XX includes proposed amendments to Rule 2001 – Applicability and Rule 2002 – Allocations for Oxides of Nitrogen (NO_x) and Oxides of Sulfur (SO_x). PAR 2001 would prevent any further inclusions of non-RECLAIM facilities into both the NO_x and SO_x RECLAIM programs and would not affect the existing facilities constituting either the NO_x or SO_x RECLAIM universes. In comparison, PAR 2002 contains the notification procedures for existing facilities that would be transitioned out of the NO_x RECLAIM program into command-and-control. It also establishes the criteria for the first set of facilities to exit the NO_x RECLAIM program. Once that NO_x RECLAIM facility receives a final determination notification that it is ready to exit the NO_x RECLAIM program, then PAR 2002 would prohibit that facility from selling any future compliance year RTCs. However, the facility would be able to sell the current compliance year's RTCs until the facility exits the NO_x RECLAIM program.

Affected Industries

Among the 266 facilities currently in the NO_x RECLAIM program as of November 2017, an estimated total of 38 facilities would be directly affected by PAR 2002 as they are potentially ready to exit out of the NO_x RECLAIM program.¹ 25 of these facilities are located in Los Angeles County, eight in Orange County, two in Riverside County, and three in San Bernardino County. Based on the North American Industry Classification System (NAICS), the majority of the directly affected facilities belong to the industry sectors of Manufacturing (NAICS 31-33) and Mining, Quarrying, and Oil and Gas Extraction (NAICS 21). Table 1 lists all affected industries, and the aggregate NO_x emissions and NO_x RTC holdings by industry, as measured in tons-per-day (TPD). The amount of NO_x emitted by the 38 directly affected facilities and their overall NO_x RTC holdings account for approximately 0.9 and 1.0 percent of the NO_x RECLAIM universe total, respectively.

¹ Staff's presentation at the November 8, 2017 Public Consultation Meeting identified 39 facilities that were ready to exit out of the NO_x RECLAIM program. However, one of them is a shutdown facility and therefore not included in the socioeconomic impact assessment.

Table 1: NOx Emissions and RTC Holdings by Affected Industry

NAICS	Industry Sector	Number of Facilities	Audited NOx Emissions in 2015 (TPD)*	NOx RTC Holdings for Compliance Year 2019+ (TPD)**
21	Mining, Quarrying, and Oil and Gas Extraction	8	0.006	0.009
31-33	Manufacturing	18	0.090	0.077
44-45	Retail Trade	1	0.001	0.000
48-49	Transportation and Warehousing	2	0.033	0.013
51	Information	1	0.002	0.000
53	Real Estate and Rental and Leasing	2	0.005	0.003
54	Professional, Scientific, and Technical Services	1	0.001	0.052
56	Administrative and Support and Waste Management and Remediation Services	2	0.014	0.003
72	Accommodation and Food Services	1	0.003	0.002
92	Public Administration	2	0.028	0.060
Total of Affected Industries		38	0.182	0.219
NOx RECLAIM Universe		266	19.851	21.449

* 2015 is the most recent year for which audited emissions are available.

** NOx RTC holdings as of November 16, 2017. The holdings remain unchanged from 2019 onwards for the 38 directly affected facilities.

Potential Cost Impacts for Directly Affected Facilities

PAR 2002 would prohibit a directly affected facility from selling any future compliance year RTCs upon receipt of a final determination notification that it is ready to exit the NOx RECLAIM program. It is expected that all final determination notifications would be received in 2018, which would then mean that the 38 directly affected facilities would not be able to sell their NOx RTCs for compliance year 2019 onwards.

Among the 38 facilities, 36 were allocated NOx RTCs free of charge at the outset of the NOx RECLAIM program. The remaining two facilities joined the NOx RECLAIM program after its inception in 1994 and therefore have no initial allocations. Taking into account past credit shaves and other adjustments, the adjusted initial allocations for the 38 directly affected facilities would amount to a total of 3.746 TPD in year 2019. However, during past two decades, over 96 percent of these initial allocations have been sold as IYBs to other NOx RECLAIM facilities and brokers/investors. According to the NOx RTC holdings data as of November 16, 2017, if no further transaction occurs after this date, the 38 facilities are estimated to have a total NOx RTC holding of 0.219 TPD for compliance years 2019 and later (see Table 1), which the facilities would not be able to sell upon receiving final determination notifications. However, it is foreseeable that at least some of these NOx RTC holdings may be sold or transferred before they are frozen due to receipt of final determination notifications.

Since there were no costs associated with the initially allocated RTCs for a RECLAIM facility, the affected facilities would not incur financial losses when the frozen future

compliance year RTC holdings are at or below their adjusted initial allocations. However, it was estimated that 0.042 TPD out of the total 0.219 TPD of future compliance year NO_x RTCs, currently held by the 38 directly affected facilities, were acquired by some of the affected facilities in addition to their initial allocations, either through purchases with positive prices or transfers at no cost. If these facilities continue to stay in the NO_x RECLAIM program and their NO_x emissions remain near their 2015 levels, then over one third of these additionally acquired RTCs (0.015 TPD) were estimated to be used for compliance purposes, with the remaining (0.027 TPD) being potential surplus RTCs available for sale or transfer. These potential surplus NO_x RTCs are currently held by three of the directly affected facilities. Applying the most recent 12-month rolling average NO_x RTC price of \$6,323 per ton,² the value of these potential surplus RTCs would be approximately \$62,000 per compliance year. However, as they pertain to the SCAQMD, RTCs are not property rights. It is known to all market participants that purchasing RTCs beyond the current compliance year is accompanied by known investment risks that are embedded within the RECLAIM programs. The risk factors include, but may not be limited to, programmatic allocation shaves, potential RTC trade freezes, and the eventual sunset of either RECLAIM programs.

At the same time, a total of 19 directly affected facilities are expected to have insufficient NO_x RTC holdings if they were to continue to stay in the NO_x RECLAIM program and their NO_x emissions remain at about their 2015 levels. By exiting the NO_x RECLAIM program, these facilities would avoid the need to acquire about 0.110 TPD of NO_x RTCs which, if valued at \$6,323 per ton, would imply potential cost-savings approximately worth \$254,000 per compliance year.

To staff's knowledge, the applicable pieces of NO_x emitting equipment (i.e., RECLAIM source equipment) at the 38 directly affected facilities are all currently at BARCT. Therefore, no additional control equipment is expected to be needed and no associated costs would be incurred for the RECLAIM source equipment consisting of process units, large sources, or major sources. However, it should be noted that any RECLAIM combustion equipment at these 38 facilities that operates without a permit (e.g., small boilers and heaters) could become subject to Rule 1146.2 upon a facility's exit out of the NO_x RECLAIM program. Therefore, they may be affected by the upcoming proposed amendments to Rule 1146.2. Any associated cost impacts will be analyzed as part of that particular rule amendment process.

Among the directly affected facilities that are currently in operation and not operated by public agencies, only four were classified as small businesses based on the 2016 Dun and

² 12-month rolling average of Compliance Year 2017 NO_x RTCs, as calculated from October 2016 to September 2017. See Table II of "Twelve-Month and Three-Month Rolling Average Price of Compliance Years 2016 and 2017 NO_x and SO_x RTCs," available at: <http://www.aqmd.gov/docs/default-source/reclaim/nox-rolling-average-reports/rtc-price-cy-2016-17---oct-2017.pdf>.

Bradstreet data.³ For these four facilities, none of their estimated future compliance year NO_x RTC holdings exceed their corresponding adjusted initial allocations. Moreover, three of these facilities may accrue potential cost-savings approximately worth \$21,000 per compliance year by exiting the NO_x RECLAIM program, due to the lack of need to purchase additional NO_x RTCs beyond their estimated holdings for compliance purposes. The fourth facility no longer has applicable NO_x emitting equipment; therefore, it would not incur any cost or cost-savings associated with PAR 2002.

Potential NO_x RTC Market Impacts

With the anticipated sunset of the NO_x RECLAIM program, the number of NO_x IYB trades have plummeted to merely three trades over the 12-month period of October 2016 to September 2017, from 44 trades over the 12-month period of May 2015 to April 2016.⁴ The IYB price has also declined rapidly, largely reflecting the remaining years of the NO_x RECLAIM program life that is expected by the market participants. However, the short-term price impact of facility exit on the discrete-year RTC market may not go hand-in-hand with the overall impact of sunsetting the NO_x RECLAIM program on the IYB market, as evidenced by the recent surge in discrete-year NO_x RTC prices.

The analysis below will focus on the potential impacts on the discrete-year NO_x RTC market that are associated with PAR 2002 only. The potential exit of the 38 facilities from the NO_x RECLAIM program could possibly affect the demand and supply in the NO_x RTC market for compliance year 2019 and beyond, and the future prevailing NO_x RTC prices, too. The remaining NO_x RECLAIM facilities may be indirectly impacted as a result.

The overall NO_x emissions from the RECLAIM universe had a maximum year-over-year difference of approximately five percent during the period of 2011-2015. Table 2 reports the potentially foregone market demand and supply for three different NO_x emission scenarios: the first scenario assumes future NO_x emissions of the 38 directly affected facilities would be five percent below their respective 2015 levels; the second scenario assumes the same emission levels as in 2015; and the third scenario assumes their future NO_x emissions would be five percent above their respective 2015 levels.

³ The SCAQMD defines a "small business" in Rule 102 as, among other things, one which employs 10 or fewer persons and which earns \$500,000 or less in gross annual receipts. For the purpose of qualifying for access to services from the SCAQMD's Small Business Assistance Office (SBAO), Rule 102 further defines a small business as a business with total gross annual receipts of \$5 million or less, or with 100 or fewer employees. The federal Clean Air Act Amendments (CAAA) of 1990 and the federal Small Business Administration (SBA) also provide definitions of a small business. The CAAA classifies a business as a "small business stationary source" if it: (1) employs 100 or fewer employees, (2) does not emit more than 10 tons per year of either VOC or NO_x, and (3) is a small business as defined by SBA. The federal SBA definitions of small businesses vary by six-digit NAICS codes. In general terms, it defines a small business as having no more than 500 employees for most manufacturing and mining industries, and no more than \$7 million in average annual receipts for most nonmanufacturing industries.

⁴ Table V: Twelve-Month Rolling Average Price Data for Infinite-Year Block NO_x RTCs in "Twelve-Month and Three-Month Rolling Average Price of Compliance Years 2016 and 2017 NO_x and SO_x RTCs," available at: <http://www.aqmd.gov/docs/default-source/reclaim/nox-rolling-average-reports/rctx-price-cy-2016-17---oct-2017.pdf>.

The foregone market demand, as estimated by the shortage of a facility's future compliance year NO_x RTC holdings for NO_x emissions reconciliation, ranges from 0.073 TPD to 0.086 TPD. At the same time, the potential foregone market supply from *all* directly affected facilities with potential surplus RTC holdings was estimated to range between 0.114 TPD and 0.119 TPD, or about 30 to 60 percent higher than the estimated foregone market demand, depending on the emission scenario. However, when compared to the volume of discrete-year NO_x RTCs traded in calendar year 2016, the range of 0.114-0.119 TPD of potential surplus NO_x RTCs is merely two percent of that total traded volume.⁵ Moreover, it was observed that some of these facilities with potential surplus NO_x RTCs have never sold or transferred NO_x RTCs to another NO_x RECLAIM facility since the NO_x RECLAIM program began in 1994. Therefore, it is reasonable to assume that they will not participate in the market even if they continue to stay in the NO_x RECLAIM program. When estimated by the potential surplus NO_x RTC holdings from only the facilities with a historical record of NO_x RTC sales and/or transfers, the foregone market supply would range from 0.082 TPD to 0.085 TPD. This range is consistent with the estimated foregone market demand, particularly under the scenarios where future NO_x emissions are assumed to be at or above the 2015 levels.

Table 2: Potential Impacts on NO_x RTC Market Demand and Supply

	NO _x Emission Scenarios for Future Compliance Years		
	<i>5% Below 2015 NO_x Emissions</i>	<i>Same as 2015 NO_x Emissions</i>	<i>5% Above 2015 NO_x Emissions</i>
Foregone Market Demand	0.073	0.080	0.086
Foregone Market Supply <i>– From All Facilities with Surplus RTC Holdings</i>	0.119	0.116	0.114
Percent Difference: <i>(Supply – Demand)/Demand</i>	62%	46%	32%
Foregone Market Supply <i>– From Facilities with Surplus RTC Holdings & Historical Record of RTC Sales/Transfers</i>	0.085	0.084	0.082
Percent Difference: <i>(Supply – Demand)/Demand</i>	16%	5%	-5%

Note: Percent differences are rounded to the nearest integer.

Given the analysis above and the fact that the 38 facilities—which are potentially ready to exit out of the NO_x RECLAIM program into command-and-control—account for about one percent of NO_x emissions and NO_x RTC holdings in the NO_x RECLAIM universe, staff concludes that the potential impact of PAR 2002 on the demand and

⁵ In calendar year 2016, a total of 2,173 tons of discrete year NO_x RTCs were traded (2173 tons/365 days = 5.953 TPD). See page ES-2 of “Annual RECLAIM Audit Report for 2015 Compliance Year,” available at <http://www.aqmd.gov/docs/default-source/reclaim/reclaim-annual-report/2015-reclaim-report.pdf>. Notice, however, that some of the RTCs might have been traded more than once in the same year.

supply of NO_x RTC market is expected to be minimal and large price fluctuations in the NO_x RTC market are unlikely to result directly from the potential exit of the 38 directly affected facilities out of the NO_x RECLAIM program. Therefore, PAR 2002 would have minimal impacts on the existing facilities that are not yet ready to exit the NO_x RECLAIM program.

Job Impacts

It has been a standard practice for SCAQMD's socioeconomic impact assessments that, when the annual compliance cost is less than one million current U.S. dollars, the Regional Economic Impact Model Inc. (REMI)'s Policy Insight Plus Model is not used to simulate jobs and macroeconomic impacts, as is the case here. This is because the resultant impacts would be diminutive relative to the baseline regional economy. Since the overall cost impacts of PAR XX are expected to be minimal, a REMI analysis was not conducted.

References

Dun & Bradstreet Enterprise Database. 2016.

South Coast Air Quality Management District. Draft Staff Report for Proposed Amendments to Regulation XX – Regional Clean Air Incentives Market, Diamond Bar, CA. December 2017.

South Coast Air Quality Management District. Twelve-Month and Three-Month Rolling Average Price of Compliance Years 2016 and 2017 NO_x and SO_x RTCs: October 2017 Quarterly Report to Stationary Source Committee, Diamond Bar, CA. October 2017.

Draft Findings Under California Health & Safety Code Section 40727

California Health & Safety Code §40727 requires that the Board make findings of necessity, authority, clarity, consistency, non-duplication, and reference based on relevant information presented at the public hearing and in the staff report. In order to determine compliance with Sections 40727 and 40727.2, a written analysis is required comparing the proposed rule with existing regulations.

The draft findings are as follows:

Necessity: PARs 2001 and 2002 are necessary to facilitate the transitioning of RECLAIM to command-and-control by not allowing any facilities from entering the program and to establish the mechanism for notifying and exiting RECLAIM facilities from the program.

Authority: The SCAQMD obtains its authority to adopt, amend, or repeal rules and regulations from California Health and Safety Code Sections 39002, 39616, 40000, 40001, 40440, 40702, 40725 through 40728, and 41508.

Clarity: PARs 2001 and 2002 have been written or displayed so that their meaning can be easily understood by the persons affected by the rules.

Consistency: PARs 2001 and 2002 are in harmony with, and not in conflict with or contradictory to, existing federal or state statutes, court decisions or federal regulations.

Non-Duplication: PARs 2001 and 2002 do not impose the same requirement as any existing state or federal regulation, and are necessary and proper to execute the powers and duties granted to, and imposed upon the SCAQMD.

Reference: In amending these rules, the following statutes which the SCAQMD hereby implements, interprets or makes specific are referenced: Health and Safety Code sections 39002, 40001, 40702, 40440(a), and 40725 through 40728.5.

Comparative Analysis

H&S Code §40727.2 (g) is applicable because the proposed amended rules or regulations do not impose a new or more stringent emissions limit or standard, or other air pollution control monitoring, reporting or recordkeeping requirements. As a result, a comparative analysis is not required.

Incremental Cost Effectiveness

California H&S Code § 40920.6 requires an incremental cost effectiveness analysis for BARCT rules or emission reduction strategies when there is more than one control option which would achieve the emission reduction objective of the proposed amendments, relative to ozone, CO, SO_x, NO_x, and their precursors. The proposed amendment does not include new BARCT requirements; therefore this provision does not apply to the proposed amendment.

Conclusions and Recommendations

The proposed amendments are needed to facilitate the transitioning of RECLAIM to command-and-control by not allowing any facilities from entering the program and to establish the mechanism for notifying and exiting RECLAIM facilities from the program.

ATTACHMENT A

PAR 2001 AND PAR 2002 PUBLIC COMMENTS AND RESPONSES

The Public Consultation Meeting for Proposed Amended Rules 2001 and 2002 was held on November 8, 2017. Comment letters received on and after that date are responded to below.

Agency/Company	Date	Comment Letter Number
Southern California Air Quality Alliance	11/20/17	1
NRG Energy, Inc.	11/22/17	2
California Council for Environmental and Economic Balance	11/22/17	3

Comment Letter #1 (Southern California Air Quality Alliance):



November 20, 2017

SENT VIA E-MAIL

Kevin Orellana
Program Supervisor
South Coast Air Quality Management District
21865 Copley Drive
Diamond Bar, CA 91765

Re: SCAQMD Proposed Amended Rule 2002

Dear Mr. Orellana:

On behalf of the Southern California Air Quality Alliance I have been actively participating in the rule development process for the sunseting of the RECLAIM program. We appreciate the willingness of SCAQMD staff to consider and address our concerns.

1-1

After reviewing the proposed amendments to Rules 2001 and 2002, we have a serious concern regarding subparagraph (f)(6)(A). That paragraph provides:

“The owner or operator of a NOx RECLAIM facility that has received a final determination notification from the Executive Officer that it will be transitioned out of the RECLAIM program shall not sell any future compliance year RTCs and may only sell current compliance year RTCs until the facility is transitioned out of the RECLAIM program.”

While the language in this subparagraph prohibits the “sale” of future compliance year RTCs, we are concerned that this may be interpreted to prohibit the “transfer” of future compliance year RTCs to other facilities under common ownership with the facility which has received the final determination notification.

1-2

As I noted during my testimony at the SCAQMD Stationary Source Committee meeting on November 17, a number of facilities keep the bulk of company RTCs in a central account at one facility and transfer RTCs as needed to the other facilities. If the facility with the central account gets the determination notification it could be required to “forfeit” all the RTCs being held by it, including RTCs needed by the company’s other facilities. Without RTCs to transfer to the other facilities to satisfy their RTC obligations, multiple violations could occur.

We request that the proposed rule amendments include clarification that intra-company transfers of RTCs between facilities under common ownership do not qualify as prohibited “sales” of RTCs.

6601 Center Drive West
Suite 500
Los Angeles, CA 90045
Attn: Curtis L. Coleman
(310) 348-8186 Ph
(310) 670-1229 Fax
colemanlaw@earthlink.net

This situation will only be exacerbated if District staff determines that the prohibition on sale is effective upon the initial notification, as is currently being considered per the staff presentation at the Stationary Source Committee meeting.

1-3

Mr. Kevin Orellana
November 20, 2017
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If you have any questions, or wish to discuss this further please feel free to contact me at your convenience.

Thank you for your consideration of this request.

Very truly yours



Curtis L. Coleman, Esq.
Executive Director
Southern California Air Quality Alliance

cc: Philip M. Fine, Ph.D.
Tracy Goss
Gary Quinn, P.E.

Responses to Comment Letter #1 (Southern California Air Quality Alliance):**Response to Comment 1-1:**

SCAQMD staff appreciates your ongoing participation throughout the rulemaking process.

Response to Comment 1-2:

The draft rule language has been updated to prohibit the sale or transfer of future compliance year RTCs as of the date specified in the final determination notification. A RECLAIM facility would still have the opportunity to transfer its RTCs to another RECLAIM facility under common ownership during the time interval between the date of the initial and final notification determination notification.

Response to Comment 1-3:

The staff proposal is to prohibit the sale or transfer of future year RTCs upon the date in the final determination notification.

Comment Letter #2 (NRG Energy, Inc.):



NRG Energy, Inc.
West Region
5790 Fleet Street, Suite 200
Carlsbad, CA 92008

November 22, 2017

via email to korellana@aqmd.gov

Mr. Kevin Orellana
Planning, Rule Development and Area Sources
South Coast Air Quality Management District
21865 Copley Drive
Diamond Bar, CA 91765

RE: Proposed Amended Rule 2001 – Applicability and Rule 2002 – Allocations for Oxides of Nitrogen and Oxides of Sulfur

Dear Mr. Orellana,

On behalf of our Los Angeles Basin electrical generating facilities, NRG Energy, Inc. (NRG) appreciates the opportunity to comment on Proposed Amended Rule (PAR) 2001 – Applicability and PAR 2002 – Allocations for Oxides of Nitrogen (NO_x) and Oxides of Sulfur (SO_x) within South Coast Air Quality Management District’s (SCAQMD) Regulation XX - Regional Clean Air Incentives Market (RECLAIM).

2-1

NRG has been a stakeholder in the RECLAIM amendments since 1998. We appreciate the availability and openness of SCAQMD staff to our comments and suggestions, and to that of California Council for Environmental and Economic Balance’s (CCEEB) of which we are a member, during this rulemaking. Our comments follow.

Timing of Freezing Sale or Transfer of RTCs and Common Ownership Considerations as Facilities Exit RECLAIM – both in the Preliminary Draft Staff Report and at the November 8, 2017 RECLAIM working group and public consultation meeting, SCAQMD staff expressed uncertainty about when future compliance year RECLAIM Trading Credits (RTCs) would be frozen as a facility transitions out of RECLAIM. NRG believes greater clarity in PAR 2002(f)(6)(A) is needed, and specifically sufficient time is needed, to allow a facility to manage its RTCs up to the point that it exits from RECLAIM. For example, as currently drafted, PAR 2002(f)(6)(A) would prevent a facility such as an electricity generating facility under common ownership or operation, which may exit RECLAIM at the same or at a different time as a commonly owned or operated facility, from moving its respective future year RTCs to one another of its facilities at the point in which final determination notification from the Executive Officer that it will be transitioned out of the RECLAIM program is received. A proper transition time from the initial notification to the final notification and then the exit date is needed during which the facility and SCAQMD can develop the appropriate transition/compliance plans, in particular where movement of RTCs between facilities with common ownership or operation may be needed to ensure the respective facility’s permitted NOx Potential To Emit is maintained as the respective facility moves to command and control. Each facility will likely have unique circumstances that will need to be managed at the subsidiary level as well as at the parent ownership level. Also, SCAQMD will be in rulemaking throughout 2018. This rulemaking may affect facility compliance and influence compliance plans; so, the final notification/determination should account/align with the relevant amended rules. During this transition period, SCAQMD staff can continue to solicit stakeholder input through the RECLAIM Working Group and therefore consider potential impacts related to the timing of the proposed Regulation XX amendments.

2-2

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November 22, 2017
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We appreciate the open communication of SCAQMD staff during these important proposed RECLAIM amendments. If you have any questions, please contact me at george.piantka@nrg.com or 760-710-2156 at your convenience.

Best Regards,



George L. Piantka
Sr. Director, Regulatory Environmental Services
NRG Energy, West Region

cc: Dr. Phillip Fine, SCAQMD Deputy Executive Officer
Tracy Goss, SCAQMD Manager

Responses to Comment Letter #2 (NRG Energy, Inc.):**Response to Comment 2-1:**

SCAQMD staff appreciates your comments and ongoing participation throughout the RECLAIM rulemaking.

Response to Comment 2-2:

The draft rule language has been updated to prohibit the sale or transfer of future compliance year RTCs as of the date specified in the final determination notification. As also stated in Response to Comment 1-1, a RECLAIM facility would still have the opportunity to transfer its RTCs to another RECLAIM facility under common ownership during the time interval between the date of the initial and final notification determination notification. Staff believes that this time interval is sufficient for facilities under common ownership to be able to transfer RTCs. As has been discussed in previous working group meetings, however, Electricity Generating Facilities (EGFs) will be treated as a separate industry category, with amendments to Rule 1135 (Emissions of Oxides of Nitrogen from Electric Power Generating Systems) forecasted to be presented to the SCAQMD Governing Board in November 2018. The first working group meeting for this industry category will be held in January 2018. It is anticipated that any initial determination notifications pertaining to EGFs will be sent upon amendment of Rule 1135.

Comment Letter #3 (California Council for Environmental and Economic Balance):



California Council for Environmental and Economic Balance

101 Mission Street, Suite 1440, San Francisco, California 94105
415-512-7890 phone, 415-512-7897 fax, www.cceeb.org

November 22, 2017

Mr. Kevin Orellana
Planning, Rule Development and Area Sources
South Coast Air Quality Management District
21865 Copley Drive
Diamond Bar, CA 91765

RE: Proposed Amended Rule 2001 – Applicability and Rule 2002 – Allocations for Oxides of Nitrogen and Oxides of Sulfur

Dear Mr. Orellana,

On behalf of the members of the California Council for Environmental and Economic Balance (CCEEB), we submit the following comments on Proposed Amended Rule (PAR) 2001 – Applicability and PAR 2002 – Allocations for Oxides of Nitrogen (NO_x) and Oxides of Sulfur (SO_x). CCEEB is a coalition of business, labor, and public leaders that advances strategies for a sound economy and a healthy environment. CCEEB represents many facilities that operate in the air basin and participate in the Regional Clean Air Incentives Market (RECLAIM). As an active participant of the RECLAIM working group, CCEEB appreciates the difficult task of sunseting the RECLAIM Program, and offers these comments as a means to help support District efforts.

3-1

CCEEB’s comments here are focused on PAR 2002:

- **Common ownership of RTCs for multiple RECLAIM facilities** – as currently drafted, PAR 2002(f)(6)(A) prevents an owner/operator from transferring fungible future compliance year RECLAIM Trading Credits (RTCs) from a facility transitioning out of RECLAIM to a facility still regulated under RECLAIM and needing to satisfy permitted limits. CCEEB wishes to work with staff on a provision to address the common ownership of RTCs for owner/operators of multiple RECLAIM facilities.
- **Freeze RTCs upon Final Determination, Develop Plans for Transition** – both in the Preliminary Draft Staff Report and at the November 8, 2017 RECLAIM working group and public consultation meeting, staff expressed uncertainty about when future compliance year RTCs would be frozen. CCEEB favors the option of freezing RTCs at the final notification of facility’s RECLAIM transition. During this transition period, staff should continue to solicit stakeholder input

3-2

3-3

through the RECLAIM Working Group on proposed amendments to the remaining portions of the program and consider potential impacts related to timing. Additionally, CCEEB has concerns regarding the equity of having different implementation schedules for facilities before and after the date of the PAR 2002 amendment.

3-3 cont.

What follows is an expanded discussion of each point.

Common Ownership of Future Compliance Year RTCs

PAR 2002 establishes the methodology for calculating RECLAIM facility allocations and adjustments to RTC holdings for NO_x and SO_x. The proposed amendments contain District procedures for notifying facilities that they will be transitioned out of RECLAIM and addresses RTC holdings for these facilities and those that elect to exit the program.¹ Subparagraph (f)(6)(A) stipulates that when a RECLAIM facility receives a final determination notification from the Executive Officer it shall not sell any future compliance year RTCs and may only sell current compliance year RTCs until it has transitioned out of the program.²

The proposed language appears to preclude an owner/operator of multiple RECLAIM facilities from handling RTCs as common assets among its multiple facilities. RECLAIM, as a market based regulatory program, is intended to provide owner/operators flexibility in achieving the lowest cost NO_x and SO_x emission reductions while still achieving the required emission reductions. Central to this is allowing owner/operators of multiple RECLAIM facilities to trade and transfer RTCs among facilities for the most efficient and cost-effective emission reductions. CCEEB seeks clarification on subparagraph (f)(6)(A) in terms of whether PAR 2002 would preclude the transfer of RTCs among facilities with common ownership. If so, we wish to discuss with staff what is the rationale for this approach. If it is the intent of the proposal to allow the transfer of RTCs between facilities with common ownership, as we support, we ask that staff clarify the language to make this option clear.

3-4

Freeze RTCs upon Final Determination, Not Initial Notification

PAR 2002 (f)(6)(a) would suspend future compliance year RTCs upon a facility's receipt of a "final determination notification from the Executive Officer that it will be transitioned out of the RECLAIM program."³ However, in the draft staff report and at the November 8, 2017 working group meeting, staff indicated that it is also considering

3-5

¹ South Coast Air Quality Management District. Preliminary Draft Staff Report Proposed Amendments to Regulation XX – Regional Clean Air Incentives Market. November 2017.

² South Coast Air Quality Management District. Proposed Amended Rule 2002 – Allocations of Oxides of Nitrogen and Oxides of Sulfur. Amended November 6, 2017.

³ *Ibid.* Subsection (f)(6)(A).

“freezing future infinite year block RTCs trades at the time of the initial notification to prevent over-supply of RTCs.”⁴

The freezing of future compliance year RTCs at the time of initial determination, as opposed to final determination, is problematic for two primary reasons. The first is the resulting economic impacts on RECLAIM facilities. The second is what appears to be an uneven treatment among facilities transitioning out of RECLAIM. For these reasons, CCEEB favors the option of freezing of future compliance year RTCs upon the final determination that a facility will be transitioned from the RECLAIM program.

To illustrate these concerns, consider a scenario in which a facility receives its initial notification, but later is deemed not ready to transition out of NOx RECLAIM, at which point the freeze on its RTC holdings would be lifted. This scenario presents regulatory and business uncertainty during the period between notification and determination. Freezing and unfreezing RTCs based upon a back-and-forth discussion between a facility and the District on the status of a multiple sources would be overly burdensome, and we believe unnecessary given that the District can simply freeze RTCs upon final determination, as the rule currently proposes. At a minimum, we ask staff to analyze whether freezing RTCs at initial notification could create uncertainty and result in supply volatility. Given the potential to impact RTC prices by unexpected changes in RTC supply, CCEEB believes this should be considered as part of the rule’s analysis.

3-5 cont.

Additionally, we have concerns about equity between facilities slated for the first round of transition and those transitioning after adoption of PAR 2002. Staff has stated that the timing of PAR 2002 “would not apply to the first group of facilities that will receive the initial notifications, but to subsequent groups of facilities [...] after the amendments to Rules 2001 and 2002.”⁵ The difference in timing of the freeze of RTCs between facilities transitioned before and after the date of the PAR 2002 seems arbitrary. CCEEB wishes to better understand why staff is considering different alternatives to when RTCs would be frozen, and believes this and the equity issues are important considerations.

3-6

Given the significance of PAR 2002 for the future success of the RECLAIM transition, adequate time for stakeholder input must be provided. As such, we ask staff to delay the set hearing for PAR 2002 for a month, allowing stakeholders to raise the issues we present here at the next RECLAIM Working Group meeting on December 14, 2017. We do not believe a short delay to work through these concerns presents any challenges to the District’s efforts, and PAR 2001 could remain on track, with a set hearing on December 1.

3-7

⁴ South Coast Air Quality Management District. Preliminary Draft Staff Report Proposed Amendments to Regulation XX – Regional Clean Air Incentives Market. November 2017. p. 5.

⁵ *Ibid*

RE: PAR 2001 & 2002

November 22, 2017

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We appreciate the opportunity to provide these comments and look forward to continuing to engage staff in the rulemaking process and RECLAIM working group.

Sincerely,

A handwritten signature in black ink that reads "Bill Quinn". The signature is written in a cursive, flowing style.

Bill Quinn
CCEEB Vice President
South Coast Air Project Manager

cc: Mr. Jerry Secundy
Ms. Janet Whittick
Mr. Devin Richards
CCEEB South Coast Air Project Members

Responses to Comment Letter #3 (California Council for Environmental and Economic Balance):**Response to Comment 3-1:**

SCAQMD staff appreciates your comments and support during the sunseting of the RECLAIM program.

Response to Comment 3-2:

Staff acknowledges the comment and believes that the proposed draft rule language addresses the concerns for facilities under common ownership.

Response to Comment 3-3:

Staff agrees with not allowing for the sale or transfer of future compliance year RTCs upon the date specified in the final determination notification and not an earlier date. Staff will continue to solicit stakeholder input through the RECLAIM working group, as well as through individual stakeholder meetings. The implementation schedules for RECLAIM facilities will be addressed in Proposed Rule 1100 (Implementation Schedule for NO_x Facilities), which is forecasted to be presented to the SCAQMD Governing Board in April 2018. As command-and-control and industry-specific rules are amended, the respective compliance schedules will be reflected in subsequent amendments to Rule 1100. Stakeholder comments and concerns will be addressed through the various working group meetings throughout the rulemaking process.

Response to Comment 3-4:

Staff acknowledges the concern for facilities under common ownership. The proposed amended rule allows for this transfer of RTCs among facilities with common ownership and is further explained in the draft staff report. See Response to Comments 1-2 and 2-2.

Response to Comment 3-5:

The draft rule language has been updated to prohibit the sale or transfer of future compliance year RTCs as of the date specified in the final determination notification.

Response to Comment 3-6:

The proposed amendments to Rule 2002 for not allowing for the sale or transfer of future compliance year RTCs upon the date specified in the final determination notification will apply for all RECLAIM facilities.

Response to Comment 3-7:

Staff does not believe further time is necessary and will move forward to present the staff proposal at the January 5, 2018 SCAQMD Governing Board Meeting.