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Exhibit 5 Air Quality

Memo from John Seitz EPA to Dave Howekamp Pre 1990 ERCs, dated August 24, 1994. Docketed August 29, 2003

August 26, 1994

MEMORANDUM

SUBJECT: Response to Request for Guidance on Use of Pre-1990 ERC's and Adjusting for RACT at Time of Use

FROM: John S. Seitz, Director
Office of Air Quality Planning and Standards (MD-10)

TO: David Howekamp, Director
Region IX, Air and Toxics Division

This is in response to the ERC questions raised in your May 31, 1994 memorandum. These issues were discussed and resolved in the ERC banking and trading work group. This memo addresses the issues raised for ozone precursors (VOC and NOx).

Question 1: What options exist for a District to allow sources to use pre-1990 ERC's?

Consistent with the "General Preamble for the Implementation of the Clean Air Act Amendments of 1990" (General Preamble), published on April 16, 1994 (57 FR 13497), States[1] may allow pre-1990 credits to be used only if they: (1) are explicitly included and quantified as growth in projection year inventories required in ROP plans or attainment demonstrations that were based on 1990 actual inventories, and (2) are otherwise creditable.

This growth could be included either at the time the inventory was submitted or in updates submitted after the original submittal, but before the ERC's are used. To do this, the ERC's being used must be contained in: (1) the current applicable federally-approved RFP and ROP plans as growth, and (2) all federally-required attainment demonstrations as emissions in the air. A State may choose to show that the magnitude of pre-1990 ERC's (in absolute tonnage) was included in the growth factor, or the State may choose to show that it was not included in the growth factor, but in addition to anticipated general growth. In either event, the segregation of pre-1990 ERC's from the projection-year growth factor will probably require a revision to the RFP, ROP, or attainment demonstration if the amount of projected growth is increased because of the explicit addition of pre-1990 ERC's.

To determine creditability, for a State to allow the use of ERC's that were banked before 1990, the State must collect and maintain information on these ERC's, including, at a minimum,

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1 In this document "State" means any governmental agency that has authority to develop and implement an implementation plan to comply with the Clean Air Act (Act). This includes, but is not limited to, air pollution control districts in California.

the name of the source that generated the ERC's, the source category that applies to this source, the quantity of ERC's generated by this source, the specific action that created the ERC's (e.g., a shutdown of a unit, process change, add-on control), the date that the ERC's were generated and enough other information to determine the creditability of all ERC's. Without this level of information, there is no way to prevent the introduction of inaccurate data to the air quality management process, which may ultimately jeopardize the State's ability to meet the other requirements of the Act.

Question 2. What guidance exists on adjusting existing and future ERC's for RACT?

At a minimum, States must ensure a RACT level of reductions on an area basis for all applicable RACT requirements at time of ERC use[2] (e.g., at the time of NSR permit issuance). A RACT level of reductions must consider the reductions that would occur from the application of: (1) RACT regulations that a State has proposed or adopted for the ERC-creating source category on or before the date that the ERC's are used, (2) all EPA-issued draft or final guidance[3] on the application of RACT for the applicable source category as of the date the ERC is used, and (3) a source-specific RACT determination for source categories that are required to apply RACT but for which the State has not proposed

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2 The application of RACT is required, independent of any RFP, ROP or attainment demonstrations, in section 172(c)(1) of the Act.

3 When EPA has issued a final guidance document, the State does not need to consider the draft document when determining the RACT level of emissions.

RACT regulations and EPA has not issued guidance.[4] This means that States must ensure that all applicable RACT requirements are accounted for when particular ERC's are used as described below:

(1) For ERC's that were created at source categories with RACT requirements that have a statutory/Federal or State implementation date on or before the date the ERC's are used, the State must ensure that a RACT level of emission reductions occurs on the date that the ERC's are used (e.g., by discounting ERC's).

(2) For ERC's that were created at source categories with RACT requirements that have an implementation date after the date the ERC's are used, the State must ensure that a RACT level of reductions will occur on or before the implementation date of the RACT regulations (e.g., by discounting ERC's). This allows the use of "limited-life ERC's" that are created and used until the implementation date of RACT requirements.[5]

For ozone nonattainment areas and any Ozone Transport Region, States must ensure a RACT level of reductions. For ERC's that were created by: (1) major sources of VOC or NOx (where required) that are not covered by CTG documents, but are required to implement RACT under section 182(b)(2)(C) of the Act, and (2) all sources included in the source categories listed under section 182(b)(2)(A) and (B) of the Act that are covered by CTG documents, the ERC's must be adjusted for RACT at time of use, except as follows: ERC's used prior to the date a State's RACT rule is proposed or May 31, 1995, whichever is earlier, do not require a RACT discounting since the State is not required to demonstrate such a RACT level of emission

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4 The State process for determining RACT in this document is intended to result in an equivalent RACT determination as required in the Act for all major sources. For example, for source categories that do not have CTG's and do have ACT's, the State would make a RACT determination by evaluating the range of controls in the applicable ACT and determining what is reasonable on a source-by-source basis or on a source-category basis considering local conditions.

5 Where ERC's are used, their use must be conditioned upon a permit requirement specifying that continued compliance (e.g., continued operation of a new source) beyond the RACT implementation date is contingent upon the State/source obtaining other emission reductions that are enforceable by the time the RACT rules require implementation.

Although this memorandum does not address emission reductions required to meet MACT regulations, the Act provisions covering NSR require all offsets to be surplus of all other requirements of the Act. Therefore, it is important to develop a similar policy for MACT discounting. The term "all other requirements of the Act" will be addressed in future ERC banking and trading guidance.

reductions until that date. However, such non-RACT adjusted ERC's have a limited life and may not be used past this date.

The adjustment of ERC's for RACT at time of use could cause some uncertainty for sources that have banked ERC's, especially for source categories that are undergoing significant change in their RACT requirements (e.g., major sources of NOx). Therefore, if a State wishes to guarantee banked ERC's for future use, several options exist, including:

(1) If ERC's are discounted at the time of State evaluation of the ERC, for all applicable RACT requirements at that time, EPA would only require a reevaluation of RACT when State or Federal actions have resulted in, or could result in, a different presumptive RACT for the applicable source category. Such an evaluation may result in the need for a State to retire a portion of the banked ERC's.

(2) States may provide other reductions to cover all or some portion of the emission reductions required for ensuring individual ERC's reflect current RACT levels.[6] This approach would allow States to discount ERC's at the time of deposit and cover subsequent discounting requirements through other creditable reductions. However, to make use of this approach, States would need to provide sufficient accounting procedures to track ERC's subject to the discounting requirement and to ensure that the proper discount is applied when each ERC is used (e.g, ERC's generated by non-RACT sources that are used for meeting RACT are generally subject to discounting equal to the offset ratio for the applicable nonattainment area).[7] A State could supply the compensating reductions by applying an across-the-board discount factor to all ERC's in the nonattainment area, or by requiring controls on small sources in the nonattainment area not subject to any federally-mandated RACT requirement, or by providing other creditable reductions. For example, a State may choose to demonstrate in the aggregate that the required reductions in ERC's due to the new RACT standards have been met through use of the alternative creditable reductions, thus eliminating the need to discount ERC's subject to the new RACT requirement. To do so, the State would track each ERC generated and determine, at the time of use, whether RACT for the generating source category has been met in the aggregate. This would entail the development of a "per ERC use" tracking system by the applicable regulatory agency, subject to EPA approval.

As discussed earlier, this policy only addresses the issues raised by Region IX for ozone precursors. My Office will continue to develop a consistent policy which addresses these issues for PM-10 and its precursors.

I appreciate the tremendous effort Region IX has put forth in working with the California Districts to develop flexible approaches to meeting the requirements of the Act. I look forward to

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6 See the EIP rule, promulgated on April 7, 1994, 59 FR 16703.

7 See the EIP rule, 59 FR 16714, section 51.493 (e)(1)(ii).

continuing to work with you on this mandate.

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