BEFORE THE ILLINOIS POLLUTION CONTROL BOARD

IN THE MATTER OF:	)	
	)	
PROPOSED NEW 35 ILL. ADM. CODE	)	
217, SUBPART W, THE NOX TRADING	)	R 01-9
PROGRAM FOR ELECTRICAL	)	(Rulemaking-Air)
GENERATING UNITS, AND AMENDMENTS	)	
TO 35 ILL. ADM. CODE 211 AND 217	)	P.C. #1

NOTICE OF FILING

TO:

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(By Messenger)

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PERSONS ON THE ATTACHED SERVICE LIST

PLEASE TAKE NOTICE that I have today filed with the Clerk of the Illinois Pollution Control Board the Comments of Aric Diericx on Behalf of Dynegy Midwest Generation, Inc., a copy of which is hereby served upon you.

Respectfully submitted,

DYNEGY MIDWEST GENERATION, INC.

By: _____
One of its Attorneys

Dated: September 19, 2000

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BEFORE THE POLLUTION CONTROL BOARD

IN THE MATTER OF:	)	
	)	
PROPOSED NEW 35 ILL. ADM. CODE 217, SUBPART W, THE NOx TRADING PROGRAM FOR ELECTRICAL GENERATING UNITS, AND AMENDMENTS TO 35 ILL. ADM. CODE 211 AND 217	)	R01-9 (Rulemaking-Air)

COMMENTS OF ARIC DIERICX ON BEHALF OF DYNEGY MIDWEST GENERATION, INC.

My name is Aric Diericx. I am employed at Dynegy Midwest Generation, Inc. ("DMG"). I am the Manager of Environmental Resources for DMG. I have been with DMG and its predecessor, Illinois Power Company, for 21 years. My entire career has been involved with environmental issues, primarily air quality management. DMG's comments to the proposed rules focus on:

(1) The status of SIP Call-related litigation and the corresponding uncertainty it adds to this rulemaking;

(2) The effectiveness of the allocation method proposed by the Illinois EPA;

(3) The anticipated NOx reductions required by Appendix F Electrical Generating Units ("EGUs");

(4) The costs Appendix F EGUs will incur to comply with the proposed rules; and

(5) DMG's recommendations on the Early Reduction Credit portion of the Compliance Supplement Pool.

Uncertainties on the NOx Control Front

Considerable uncertainty surrounds the U.S. Environmental Protection Agency's ("U.S. EPA") initiatives concerning ozone transport and ambient ozone concentrations. This uncertainty will probably continue over the next three to twelve months. As the Board considers adopting these NOx rules, it needs to remain aware of ongoing national litigation and the possible rulemakings that could affect the final form of Illinois' rule.

First, in American Trucking Association v. EPA, 175 F.3d 1027 (D.C. Cir. 1999), the U.S. Court of Appeals for the District of Columbia remanded the U.S. EPA's 8-hour ozone standard. The court did not revoke the standard, but did state that if failure to do so would cause harm, it would consider revoking the standard. The U.S. Supreme Court granted certiorari to U.S. EPA and other petitioners. Oral argument is set for Fall 2000. In the meantime, the 8-hour ozone standard sits idle along with that portion of the NOx SIP Call Rule that was designed to address the 8-hour standard.

In Michigan v. EPA, 213 F.3d 663 (D.C. Cir. 2000), the U.S. Court of Appeals for the District of Columbia generally upheld the U.S. EPA's ozone transport rule. With regard to certain non-EGU units and internal combustion engines, the court directed the U.S. EPA to correct its rulemaking to allow for adequate public review, which the U.S. EPA has yet to do. On June 23, 2000, the court lifted its stay on the state-filing deadline, thus making October 30, 2000 the new target date for filing SIPs. On August 30, 2000, the court responded to the implementation concerns raised by state and industry/labor petitioners and ruled that the compliance deadline for the NOx SIP Call Rule should be delayed from May 1, 2003 to May 31, 2004. The decision's impact is not yet fully understood. The U.S. EPA's ozone season and the control season contemplated by the

Board's rulemaking begin annually on May 1. The NOx SIP Call Rule reductions, therefore, will not be effective until May 1, 2005. The U.S. EPA may still develop an alternative interpretation. It may, nevertheless, be several months until the ultimate compliance date is defined.

Next, in Appalachian Power Company v. EPA, Case No. 99-1268 (D.C. Cir.), the petitioner challenged the technical amendments the U.S. EPA made to the state-specific NOx budgets under the NOx SIP Call Rule. A briefing schedule is in place and the parties will likely explore the U.S. EPA's handling and revising of the state NOx budgets. The relative instability of the state NOx budgets created by this litigation, and the Michigan v. EPA decision concerning non-EGUs and ICEs, makes it difficult to implement the NOx SIP Call Rule. States must know what their NOx emission reduction budgets are so that a state can correctly implement the NOx emission reduction program ordered by the U.S. EPA. The Appalachian Power case should directly address Illinois' concerns over an inadequate growth factor, which produces an inaccurately stringent NOx allocation for the EGU sources.

In a related matter, Appalachian Power v. EPA, Case No. 99-1200 et al. (D.C. Cir.), in which the U.S. EPA's Section 126 determinations are being challenged, many of the same arguments presented to the court concerning the NOx SIP Call Rule have been and will be reiterated. One important issue that will need to be addressed with the court is delaying the NOx SIP Call Rule compliance date and revising the Section 126 determinations to mirror that compliance timeline. This could have some bearing on the language that triggers implementation in Illinois based on the development of these rules in other states.

Finally, the proposed Federal Implementation Plan for the NOx reduction program, referred to in this rulemaking as 40 C.F.R. Part 96, also includes a May 1, 2003 compliance date. If the currently proposed FIP is applied to a state with this earlier compliance date, a challenge will most certainly be brought. In order to correct Part 96 to reflect the new SIP compliance date, the U.S. EPA will need to re-propose Part 96, in effect beginning the rulemaking process anew. It could take the U.S. EPA several months to complete these steps and impose a FIP with the revised compliance date. The fact that Part 96 is now flawed may also alleviate some of the pressure on the Board to adopt this NOx rule by October 30th because the U.S. EPA may not be as willing to impose the FIP.

The NOx Trading Budget and Allowance Allocations

The Illinois EPA proposes to implement the NOx trading program allowing for the allocation and trading of NOx allowances among EGUs. The Illinois EPA's allocation methodology, while based on the U.S. EPA's model, deviates from it in two significant respects. First, the proposal does not use the same emission rate in allocating allowances to Appendix F EGUs and non-Appendix F EGUs. For Appendix F EGUs, it purports to use the 0.15 lbs./mmbtu rate. For non-Appendix F EGUs, allocations are based on the more stringent of the 0.15 lbs./mmbtu rate and the unit's permitted rate. The proposal also deviates from the federal model in that it phases in the rule's full impact on Appendix F EGUs through the use of the so-called "fixed/flex" approach.

The Illinois EPA's proposed allocation methodology is appropriate and justified inasmuch as the NOx SIP Call Rule places the greatest burden on Appendix F EGUs. Indeed, the impact on Appendix F EGUs will be even greater than the Illinois EPA has

predicted. In several significant respects, the Illinois EPA has materially underestimated the impact of the rule on the Illinois EGU sector.

The Illinois EPA Underestimated the Amount of NOx Reductions Required by EGUs

According to the Illinois EPA, the budget for EGUs is derived from reductions based on control measures determined by the U.S. EPA to be "highly cost-effective." (Ex.25: Prepared Testimony of K. Bassi at 3). The U.S. EPA, however, grossly underestimated the level of reductions that will be necessary for the sector, as well as the cost to achieve compliance.

To determine the budget allowances for Illinois EGUs, the U.S. EPA used projected increases in heat input values from 1996 to 2007. According to the U.S. EPA, it then applied this growth rate to the projected 2003 heat inputs before determining the state EGU budget allocations. The budget NOx emission rate of 0.15 lbs./mmbtu was applied to the predicted 2007 heat input values to determine the budget allowance for the existing EGUs. Using its Integrated Planning Model ("IPM"), the U.S. EPA used a growth factor of 1.08 or eight percent to predict the 2007 heat input values. The U.S. EPA's model, however, badly underestimated growth in the Illinois EGU sector. In fact, the 1998 ozone season heat input of the EGU sector had already exceeded the U.S. EPA-forecasted amount for 2007. *See,* Attachment 1 hereto (submitted to the U.S. EPA as an exhibit to Illinois Power Company's February 22, 1999 comments to Docket Nos. A-96-56, A-97-43 and A-98-12). Illinois' actual heat input data for the 1998 ozone season clearly demonstrates that the 1.08 growth factor was insufficient to accurately predict growth through that year. It also implies that Illinois' actual heat input for the years between 1998 and 2007 ozone season have been grossly under-predicted by the IPM.

Because the growth factor under-predicts Illinois' heat input growth, the NOx emissions reductions required by Appendix F EGUs has also been underestimated. The Illinois EPA estimates that Appendix F EGUs will need to reduce NOx emissions by 74% under the proposed NOx budget. *See, Technical Support Document for Control of Nitrogen Oxide Emissions from Electrical Generating Units ("TSD")*, pp. 27-29, AQPSTR 00-1, Illinois EPA (July 2000). Even if the 74% reduction figure were accurate, system-wide reductions of that magnitude would be virtually impossible to accomplish even over a short period of time. But because the budget is based on an insufficient growth factor, the true level of reductions that will be necessary will clearly exceed 74%. Accordingly, the impact on the Appendix F EGUs will be larger than the Illinois EPA predicts. If, however, the Illinois EPA were to introduce an alternative rulemaking to reduce NOx emissions to 0.25 lbs./mmbtu, not only would the impact on Appendix F EGUs be reduced, but early reduction incentives in 2001 and 2002, as discussed below, could complement that program and produce air quality benefits in a shorter timeframe.

The Illinois EPA Underestimated the Cost of Compliance

By underestimating the emissions reductions required by Appendix F EGUs, the Illinois EPA has significantly underestimated the costs to be incurred by the Appendix F EGUs in achieving compliance with the NOx SIP Call Rule. The cost of NOx controls increases greatly for an emission rate more stringent than 0.25 lbs./mmbtu, and even more when the limit drops below 0.15 lbs./mmbtu. The Illinois EPA estimates that the average annual cost to reduce NOx emissions will be approximately $1,486/ton of NOx reduced. *TSD* at 38. DMG calculated the incremental cost for it to go from a 0.25

lbs./mmbtu rate rule to the NOx SIP Call Rule levels. On a dollar-per-ton-removed basis, the incremental cost to go to the SIP Call Rule level (i.e., below 0.15 lbs./mmbtu) is $7,339 over a five-year period and $4,582 over a ten-year period. This estimate is similar to that identified by the U.S. EPA when it admitted that the incremental cost-effectiveness of going below 0.15 lbs./mmbtu is $4,200 per ton. 63 Fed. Reg. 57,356, 57,413 (October 27, 1998). While DMG recognizes that the Board and the Illinois EPA must work within the NOx control parameters set by the U.S. EPA, the Board should be aware of these more representative control costs so they can be interpreted correctly with the other ozone control measures implemented in Illinois.

Accordingly, the impact of the NOx SIP Call Rule on Appendix F EGUs is even more severe than the Illinois EPA has stated. The allocation methodology recognizes that the NOx SIP Call Rule will impact Appendix F EGUs much more severely than newer units. Phasing in the rule's impact on Appendix F EGUs simply acknowledges the reality that additional time is needed for these units to achieve an equal footing with newer units. The allocation method recognizes the long lead-time to design, procure, and install controls on large coal-fired units. Without these fixed allocations, the multi-million dollar NOx control systems would become obsolete before they were put into service.

The phased approach also will enable the Appendix F EGUs to continue providing service to customers without significant interruptions. As the Illinois EPA recognized, Illinois depends heavily on coal-fired electricity generation. (Ex. 25: Prepared Testimony of K. Bassi at 12). By phasing in NOx reductions, the regulations provide the Appendix F EGUs -- consisting largely of coal-fired units -- with adequate time to make adjustments in operations so that service is not interrupted as a result of

complying with the proposed regulations. The approach advocated by the Illinois EPA and the Appendix F EGUs provides both a firm planning/design target and a gradual system of allocation adjustments. While such a system cannot preclude the need for more costly NOx systems in the future, it has the potential to spread the need for the next round of NOx retrofits over time, thereby, somewhat mitigating the economic impact.

DMG also believes that the Illinois EPA's allocation approach is well founded because it relies on the use of heat input, a performance tool consistent with the initial allocation scheme and one with which the Illinois EPA and sources are familiar. By retaining the heat input basis, these rules will remain on par with the Acid Rain rules that also utilize heat input.

Early Reduction Credits

The Compliance Supplement Pool ("CSP") provides for additional allowances that may be allocated to budget EGUs, but only for use in the 2003 and 2004 control periods. The total number of allowances available to budget EGUs through the CSP is 15,261 tons. The Illinois EPA proposes to allocate these allowances as credits to budget EGUs that achieve early reductions in NOx emissions. (Ex.25: Prepared Testimony of K. Bassi at 16).

Section 217.770 of the Illinois EPA's proposal provides for the creation and administration of the Early Reduction Credits ("ERCs") for budget EGUs. Budget EGUs may request ERCs for NOx emission rate reductions achieved in either the 2001 or the 2002 control periods. The reduction is measured by subtracting the EGU's actual NOx emission rate for the applicable control period from the NOx emission rate required for the unit in the 2000 control period (or its actual emission rate in the 2000 control period if

none was legally required). The amount of the credit is determined by multiplying the unit's heat input value for the applicable control period by the rate reduction achieved for that period. Requests for ERCs must be submitted by November 1, 2001, for reductions made in the 2001 control period and by November 1, 2002 for reductions made in the 2002 control period. Section 217.770(e) provides that, in the event the NOx SIP Call Rule's May 1, 2003 implementation date is delayed, then the early reduction request must be submitted by November 1 of the year two years before the implementation date for the reductions made in the control period two years before the implementation date, and by November 1 of the year preceding the implementation date for the reductions made in the control period preceding the implementation date. It further provides that "[s]hould this occur, the other dates in this Section shall be adjusted accordingly." Id.

The Board should not adopt Section 217.770(e) because it is inconsistent with the purpose of the ERCs. The rationale for establishing the ERCs is to encourage and reward early reductions. Section 217.770(e)'s "slide-back" feature, which sets back the control periods in which credits can be requested so as to coincide with the two years immediately preceding the program's implementation date, could actually work to discourage efforts aimed at achieving the earliest reductions in NOx emissions. Because the program has a finite number of allowances to award, allowances will be distributed pro rata if more credits are earned than are available for distribution. Accordingly, the credit allowances to be received for NOx reductions achieved by a budget EGU in the 2001 control period will devalue if the credits are not determined and issued based on the reductions made during the 2001 control period. Indeed, as each year passes, the reductions achieved in the 2001 control period will continue to depreciate in value, as an

increasing number of budget EGUs install controls in advance of the sliding implementation date.

What is worse, the implementation date will slide even if the Board adopts the NOx Trading Program on an expedited basis as the Illinois EPA has urged. This is true because the program's implementation date would slide if any other Region V state or other state bordering Illinois does not promulgate its own SIP revision to comply with the NOx SIP Call Rule by the implementation date. Under the Illinois EPA's proposal, then, delaying capital spending projects would be the economically prudent course. Indeed, it may be the only justifiable course from a financial standpoint, inasmuch as one would not be able to assess the economic value of implementing the capital expenditure in 2001 or 2002.

In addition, constructing a program that awards credits for reductions achieved after 2002 might run afoul of federal law. The NOx SIP Call Rule's CSP provisions state that ERCs may be awarded from the CSP for emissions reductions "in years prior to the year 2003." 40 C.F.R. § 51.121(e)(3)(iv)(A). The SIP Call Rule requires a state to "complete the [ERC] issuance process by no later than May 1, 2003." Id. at § 51.121(e)(3)(iv)(A)(1). The U.S. EPA may interpret these provisions as preventing states from awarding ERCs for reductions that occur in the 2003 ozone season or that occur before May 31, 2004.

Finally, whether or not Section 217.770(e) is retained in its entirety, the last sentence of the section needs to be amended. This sentence indicates that if the implementation date is delayed, "the other dates in this Section should be adjusted accordingly." The Illinois EPA testified that this provision was intended simply to

"slide" the dates back to accommodate the delayed implementation. The sentence needs to be amended to clarify that the reference to the "2000" control period in Section 217.770(c)(3) is an exception. This provision sets the base year for early emission rate reduction comparisons. If it were not excepted from the slide-back feature of Section 217.770(e), the EGU that reduces emissions in 2001 would not be able to realize the benefit of the reductions as ERCs. The result is not intended by the Illinois EPA. The Illinois EPA's witness clarified that even if the control periods in which ERCs can be earned were pushed back, an EGU that achieves reductions in 2001 will not be penalized because those reductions will be evident in subsequent years. (Tr. of 8/28/00 at 129-130). This can only be true, of course, if the base year remains the same. Accordingly, the last sentence in Section 217.770(e) must be revised to exclude the reference to the 2000 control period in Section 217.770(c)(3).

Conclusion

DMG believes that the Illinois EPA has addressed many of the concerns of the various stakeholders. But DMG also believes that by addressing the relatively minor issues raised in these comments, this rulemaking can be improved and implemented as a viable approach to satisfying the Illinois' requirements regarding the EGU portion of the NOx SIP Call Rule.

COMPARISON OF ACTUAL 1998 OZONE SEASON HEAT INPUT vs IPM PROJECTION FOR 2007
STATE OF ILLINOIS

Kincaid	26,169,980
CILCO	29,021,620
Soyland	863,079
CWLP	13,777,986
So.Ill. Power	9,864,000
AmerenCIPS	68,721,572
Illinois Power	84,984,319
Electric Energy Inc.	39,741,147
Commonwealth Edison	177,352,160
Total	450,495,863
IPM Projected 2007	411,298,433

PROOF OF SERVICE

I, Gabriel M. Rodriguez, on oath state that I have served the attached Comments of Aric Diericx on Behalf of Dynegy Midwest Generation, Inc. by first class U.S. Mail, postage prepaid, upon the persons on the attached service list.

Gabriel M. Rodriguez
One of the Attorneys for Dynegy Midwest Generation, Inc.

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