

BEFORE THE ILLINOIS POLLUTION CONTROL BOARD

DYNEGY MIDWEST GENERATION, LLC,)
)
Petitioner,)
)
v.)
)
ILLINOIS ENVIRONMENTAL)
PROTECTION AGENCY,)
)
Respondent.)

PCB 12-135
Variance – Air

NOTICE OF FILING

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PLEASE TAKE NOTICE that we have today filed with the Office of the Clerk of the Pollution Control Board **DMG'S RESPONSE TO THE BOARD'S QUESTIONS**, copies of which are herewith served upon you.



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Dated: August 9, 2012

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DMG’S RESPONSE TO THE BOARD’S QUESTIONS

NOW COMES Petitioner, DYNEGY MIDWEST GENERATION, LLC (“DMG”), and responds to questions posed by the Pollution Control Board (“Board”) in this matter on July 27, 2012. By way of background, on June 8, 2012, pursuant to Section 37(a) of the Environmental Protection Act, 415 ILCS 5/37(a), and the Board’s rules addressing variances at 35 Ill. Adm. Code Part 104, Subpart B, DMG filed a Petition for Variance from certain provisions of 35 Ill. Adm. Code § 225.233(f)(2) from the date of the Board’s order granting the variance until April 1, 2015. Specifically, DMG requested relief from the prohibition on sulfur dioxide (“SO₂”) allowance sales and the requirement to surrender excess SO₂ allowances to the Illinois Environmental Protection Agency (“Agency” or “Illinois EPA”). The Board accepted the Petition for Variance on June 21, 2012. The Agency published notice of DMG’s request for variance in newspapers located in the counties where each of DMG’s plants is located on June 19 or 20, 2012. (Agency Recommendation (“Rec.”), p. 2.) As of July 23, 2012, the Agency had received no written comments or requests for hearing. Rec., p. 3. On July 12, 2012, the Environmental Law and Policy Center and other environmental groups submitted comments

opposing granting of the variance but specifically did not request a hearing in this matter. PC #1.

The Agency submitted its Recommendation neither supporting nor opposing the request for variance on July 23, 2012. Rec., pp. 1, 14. In response to the questions posed by the Board, DMG states as follows:

1. (a) ***Please describe how CSAPR is structured to ensure upwind states are limited in their contribution of emissions in downwind states.***

1. There are two programmatic elements of the Cross-State Air Pollution Rule (“CSAPR”) that ensure that upwind states are limited in their contributions of emissions to downwind states with respect to SO₂ emissions¹: (i) the division of the states subject to the CSAPR into two groups and (ii) the implementation of variability limits. A third element of the CSAPR that ensures that upwind states are limited in their contributions to downwind receptors is the level at which the U.S. Environmental Protection Agency (“USEPA”) set the state allowance allocations, based on robust air quality analyses.

2. In developing the CSAPR, USEPA determined that some states had more impact on downwind SO₂ receptors than other states. The states with greater impact were grouped together and called Group 1 states, and the states with lesser impact were grouped together and called Group 2 states. Illinois is a Group 1 state.² Sources in Group 1 states are required to hold

¹ References to the CSAPR programs herein are only to its SO₂ programs. The CSAPR also includes programs restricting emissions of nitrogen oxides (“NO_x”) implemented through cap and trade. However, NO_x is not an issue with respect to this Petition for Variance.

² Sources in Group 1 states are also subject to an additional reduction in the number of allowances in the third year of the CSAPR, while sources in Group 2 states are not. Therefore, covered sources in Illinois are subject to this additional reduction.

sufficient “TR SO₂ Group 1”³ allowances in their compliance accounts at true-up to equal their emissions during the previous control period. 76 Fed. Reg. 48,208, 48,271, 48,452 (§ 97.624) (Aug. 8, 2011). “TR SO₂ Group 2” allowances cannot be converted into “TR SO₂ Group 1” allowances and vice versa. Therefore, sources in Group 1 are effectively allowed to trade with sources located only in other Group 1 states for compliance purposes; likewise, Group 2 sources may trade only with other Group 2 sources for compliance purposes.⁴ This separation of trading programs prevents Group 1 sources from using Group 2 allowances and potentially exacerbating the impact of Group 1 states on downwind receptors.

3. Variability limits are an upper bound on total SO₂ emissions that sources subject to the CSAPR in a state may emit during a calendar year. The variability limits are greater than the total number of allowances allocated to the sources in a state. Thus USEPA anticipated that there could be differences in electricity demand in portions of the CSAPR region that could vary from year to year. 76 Fed. Reg. at 48,265. USEPA believed that the variability limits, set at specific percentage levels⁵ greater than the total number of allowances allocated for a state,

³ “TR Group 1” and “TR Group 2” are the names USEPA uses to describe SO₂ allowances in the preamble to the CSAPR. Originally, the CSAPR was called the Transport Rule, but USEPA changed the name of the program when it finalized the rule. Some elements of the nomenclature held over in the preamble to the final rule. “TR Group 1 SO₂ allowances” are the same as “CSAPR Group 1 SO₂ allowances.”

⁴ 76 Fed. Reg. at 48,214 (“The two SO₂ trading programs are exclusive, *i.e.*, a covered source in a Group 1 state may use only a Group 1 allowance for compliance, and likewise a source in a Group 2 state may use only a Group 2 allowance for compliance.”) Note that any person may open a trading account in any of the four trading programs created under the CSAPR. However, the compliance requirements prevent Group 1 and Group 2 cross-trading for all practical purposes, *i.e.*, for purposes of compliance.

⁵ The variability limit for statewide SO₂ emissions across the CSAPR region is 18%. 76 Fed. Reg. at 48,267. That is, total emissions in a state may exceed the statewide total allowance allocations by 18% in any given control period. However, once total statewide mass emissions exceed 18% above the statewide total allocations (or emissions cap), the variability limit has

provide the necessary flexibility for generators to supply the demands for their electricity. 76 Fed. Reg. at 48,265. Beginning in the third year of the CSAPR (*i.e.*, presumably 2015),⁶ if the total amount of SO₂ emissions in a calendar year exceeds the number of allowances allocated for a state plus the state's variability limit, USEPA would determine which sources in the state contributed to the emissions in excess of the variability limit. Those sources must surrender additional allowances to cover their respective shares of emissions in excess of the variability limit. *See* 76 Fed. Reg. at 48,294-96. Given the deferred implementation of the variability limits,⁷ it appears that the variability limits would not apply during the term of the variance that DMG seeks. Nevertheless, according to USEPA:

Based on the current level of EGU emissions and EPA's short-term modeling results,^[8] EPA maintains that EGU emissions in 2012 and 2013 in each of the states subject to the Transport Rule – without the assurance provisions being applicable in those years

been exceeded and those sources whose emissions exceeded their proportionate share of the 18% must surrender additional allowances to cover the excess.

⁶ The third year of the final rule as adopted is 2014. However, several persons appealed the CSAPR, and the court granted a stay of the effectiveness of the program during the pendency of the appeal. *EME Homer City Generation, LP v. Environmental Protection Agency*, No. 11-1302, Order (D.C. Cir. Dec. 30, 2011). It is reasonable to assume at this time that the earliest implementation date for the rule is 2013, making 2015 the third year of the program.

⁷ In revisions to the CSAPR, USEPA determined that seamless transition from the Clean Air Interstate Rule to the CSAPR required a delay in implementation of the variability limits. 77 Fed. Reg. 10,324, 10,331 (Feb. 21, 2012). The revision changes the implementation date of the variability provisions from 2012, the first year of the program, to 2014, the third year of the program. It is reasonable to assume that if the 2012 and 2013 dates of the program slide to 2013 and 2014 (*supra*, note 6), the third year, when variability limits would first apply, would be 2015.

⁸ USEPA examined recent emissions and modeled projected 2012 and 2013 emissions without applying the variability limits (also called assurance provisions) and determined that the CSAPR “trading programs will still result in emission reductions that cause total emissions in *each state* to be below the level of the applicable state assurance level, even when sources are not subject to the assurance provisions in those years.” 77 Fed. Reg. at 10,330 (emphasis in original).

– have virtually no chance of exceeding the applicable state assurance level. Consequently, imposition of the assurance provisions during 2012-2013 is unnecessary and could actually be detrimental to smooth program implementation. . . .

77 Fed. Reg. at 10,331. USEPA concludes that the CSAPR, even without the variability limits in the first two years of the program, will adequately protect air quality at downwind receptors.⁹

The Board's granting this requested variance, which would result in allowance utilization as modeled by USEPA and would not impair the CSAPR air quality benefits, will not have an effect on air quality or downwind receptors beyond what USEPA expects and has modeled in the course of the CSAPR rulemaking.

4. A third element in the development of the CSAPR that protects downwind receptors lies in the air quality analysis that USEPA performed. USEPA determined that the prescribed allowance allocations are protective of downwind receptors. 76 Fed. Reg. at 48,237. As described in great detail in the preambles to the proposed and final rules, USEPA identified which receptors were either nonattainment of the fine particulate National Ambient Air Quality Standard ("PM_{2.5}" or "PM_{2.5} NAAQS") or in jeopardy of becoming nonattainment (*i.e.*, maintenance areas) because of upwind contributions of PM_{2.5} or its precursors. *See* 76 Fed. Reg. 48,222-71.¹⁰ Where a state contributed "significantly" to a downwind receptor, either one already in nonattainment or one where maintenance was threatened, the state became subject to the CSAPR for SO₂. USEPA examined each electric generating unit ("EGU") in subject states to determine its historic emissions, applied reductions that would result from "on-the-books" state

⁹ 77 Fed. Reg. at 10,331 ("In summary, EPA concludes that . . . the assurance provisions [are] not necessary in 2012-2013 to ensure elimination of significant contribution and interference with maintenance. . . .").

¹⁰ The CSAPR regulates SO₂ emissions as a precursor to the formation of PM_{2.5}.

and federal rules, and then set each EGU's allowance allocation based on those factors, but in no event greater than the EGU's maximum emissions. Finally, USEPA determined that emissions from states at those levels plus the variability limits described above would not significantly impact the downwind receptors linked to each state. 76 Fed. Reg. at 48,237. USEPA explained that in the CSAPR, state emission budgets were based on each state's contributions to downwind receptors, as compared to the Clean Air Interstate Rule ("CAIR"), where state budgets were based on a regional level of required emission reductions. 77 Fed. Reg. at 10,331. Therefore, USEPA concludes that even without implementation of the variability limits during the first two years of the program, current emission levels and controls that will be put in place during the period ensure protection of downwind air quality. 77 Fed. Reg. at 10,331-32. Further, USEPA determined that a cap and trade program provides effective protection of air quality in the most cost-effective manner. 76 Fed. Reg. at 48,210-11, 77 Fed. Reg. at 10,331.

5. USEPA's own analyses support the relief that DMG requests in its Petition for Variance. Illinois EPA agrees that granting this requested variance will not detrimentally impact air quality, as demonstrated by USEPA's air quality analyses during the development of the CSAPR, Rec., p. 10, and subsequent air quality modeling, 77 Fed. Reg. at 10,329-32.

1. (b) ***Please identify the potential areas where DMG's SO₂ allowances could be sold or traded and the potential downwind receptor areas. Please describe any limit that defines how many allowances can be traded out of state.***

6. The CSAPR Group 1 states are Illinois, Indiana, Iowa, Kentucky, Maryland, Michigan, Missouri, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia, and Wisconsin. 76 Fed. Reg. at 48,440-41. This list of states represents the entire compliance trading universe available to DMG and, thus, as determined by the

structure of the CSAPR, the universe of potential downwind receptor areas.¹¹ The CSAPR does not limit how many allowances a source may sell or trade. Theoretically, a company could sell all of the allowances allocated to it and buy back enough allowances to cover its emissions in a calendar year. All that the CSAPR requires is that every source hold enough allowances in its compliance account to match its actual emissions during the preceding calendar year by the reconciliation deadline. For purposes of CSAPR, the geographic orientation of the Group 1 allowance sellers to the Group 1 allowance buyers does not matter. In that sense, there is no restriction on the scope of trades that DMG could make if the variance is granted.

7. Although DMG does occasionally engage in direct trades of emissions allowances, most of the allowance trading that DMG undertakes is “blind.” That is, allowances are traded through an exchange, such as the one operated by Intercontinental Exchange, Inc., and DMG may never know who buys its allowances. This is a general practice in allowance trading. In that sense, it is impossible for DMG to identify what receptors might be affected by any one of its allowance sales. DMG has not identified any particular buyers and has no trades pre-determined. It desires to go into the open market for Group 1 states and sell allowances it does not need for its own compliance purposes.

1. (c) ***Does the Illinois Environmental Protection Agency intend to propose amendments to the rules if CSAPR is implemented?***

8. This question is better posed to the Illinois EPA. To our knowledge, the Illinois EPA has not expressed an intent to propose amendments to its rules if CSAPR is implemented, but DMG is not privy to the Agency’s thoughts on this point and could not speak on behalf of the Agency in any event.

¹¹ That is, anyone could buy DMG’s allowances, but sources in only these 16 states may use DMG’s allowances for purposes of compliance.

2. (a) ***Please provide the most up-to-date map for the Ozone Monitoring Sites available from the latest Illinois Annual Air Quality Report.***

9. Included herewith as Attachment 1 is a map of the ozone monitoring sites from the *2010 Annual Air Quality Report*, the latest available such report.¹² Although DMG has provided the information that the Board has requested, DMG is puzzled by the request, as SO₂ is not a precursor to ozone.

3. (a) ***Please estimate a range for the value of excess SO₂ CSAPR allowances allocated for 2014.***

10. As indicated in DMG's Petition for Variance, the monetary value of these excess CSAPR SO₂ allowances in the first two-year phase of CSAPR cannot be estimated with reasonable certainty at this time because the CSAPR is stayed and there currently is no active market for CSAPR SO₂ allowances. However, assuming 2014 is the second year of the CSAPR and 2013 is the first year of the program and based on the allowance price assumptions identified in DMG's Petition for Variance as modified by information in a recent *Argus Air Daily* article (cited below), then DMG estimates that the value of 2014 allowances could range from

¹² DMG effectively provided this requested information with its Petition for Variance in Exhibits 2 and 4. The map in Exhibit 2 shows the locations of DMG's power plants. It also shows the locations of the air monitoring stations located nearest to the DMG power plants. The "Summary of Nearest IEPA Air Monitoring Locations" in Exhibit 4 to the Petition identifies the ozone monitoring stations closest to each power plant except for the Havana Power Station. The ozone monitoring stations closest to Havana are those located in Peoria County at Fire Station # 8 at MacArthur & Hurlburt in Peoria and at the Peoria Heights High School, 508 East Glen Avenue in Peoria. Comparing the addresses of the monitoring stations listed in Exhibit 4 to the Petition, which information is from the *2010 Annual Air Quality Report*, it appears that the map in Exhibit 2 is accurate.

approximately \$139 per allowance¹³ to \$2,500 per allowance. Therefore, the range in value of approximately 23,000 allowances available for sale or trade is \$3.197-\$57.5 million in 2014.

3. (b) *Please estimate a range for the total economic value of the allowances for both 2013 and 2014.*

11. Subject to the limitations identified above in Paragraph 10 and again assuming that 2013 is the first year of the CSAPR and 2014 is the second year, the estimated range of value of excess CSAPR SO₂ allowances for both 2013 and 2014 would be double the range estimated above in DMG's response to question 3(a): \$6.394-\$115 million.¹⁴

3. (c) *Please comment on the economic impact of not being able to sell or trade the allowances on rate payers and the people of the State of Illinois.*

12. DMG is unable to predict with any certainty the impact of not being able to sell or trade these allowances on ratepayers and the people of the State of Illinois.

13. DMG is an independent power producer and, as such, does not have any ratepayers. In general, if DMG were unable to sell its excess CSAPR SO₂ allowances, its net production cost would be higher compared to its production costs minus the proceeds from the CSAPR SO₂ allowance sales. Higher net production costs would, in general, result in a higher

¹³ In its Petition for Variance, DMG assumed a price per allowance range of \$400 to \$2,500 based on USEPA estimates and initial allowance trades before CSAPR was stayed. Pet., p. 19. However, a recent article identifies current prices as low as \$139 per allowance. "SO₂, NO_x flatline as ruling awaited," *Argus Air Daily*, Vol. 19, 144 at 2 (July 27, 2012). DMG believes the drop in price identified by *Argus Air Daily* (relative to the initial price estimates as assumed in DMG's Petition for Variance) is likely due to factors such as the low price of natural gas, the shutdowns of a number of coal-fired EGUs (thus lessening the demand for allowances), and other economic factors, as well as the uncertainty inherent in waiting for the court's decision on the CSAPR.

¹⁴ Given that emission allowances generally have greater value at the beginning of a new trading program and the current allowance price identified by *Argus Air Daily* (*supra*, note 13), DMG anticipates that the value of the excess allowances in 2013 and 2014 would be nearer to the lower end of the estimated range than the higher end.

market price for DMG's energy sales. Because DMG is not a utility and cannot recover costs through Illinois Commerce Commission approved rates, DMG would be able to recover any such increased production costs only to the extent that wholesale energy market prices allowed for such recovery. However, because energy pricing is affected by many complex factors, because the proceeds from potential allowance sales are uncertain, and because DMG does not know exactly how the energy prices of its wholesale competitors will be affected by the CSAPR or how other companies will reflect the cost of CSAPR compliance in the rates they set for their customers, DMG is unable to predict with any certainty the impact of not being able to sell or trade these allowances on ratepayers.

14. If DMG is not allowed to sell its excess CSAPR SO₂ allowances, it will have an adverse economic impact on DMG. In a general sense, such an adverse economic impact, in combination with other adverse economic impacts, if sufficiently material, potentially could adversely affect the number of Illinois citizens employed by DMG. A reduction in DMG's Illinois workforce potentially could result in less consumer spending in Illinois, resulting in less sales tax collected by the State and could mean lower income tax revenues for the State. DMG employees approximately 430 persons at its coal-fired power plants in Illinois, many of which are well-paying union jobs, and approximately an additional 148 support personnel at its offices in Illinois. *See* Pet., par. 1. In many of the Illinois communities and counties where DMG's plants are located, DMG is one of the largest employers and economic engines for the local economies, contributing millions in economic impacts and property and sales tax revenues. A combination of negative economic factors, including the inability to sell or trade the excess SO₂ allowances, could impact the economic viability of certain DMG assets in Illinois, which would

then negatively impact DMG employees, the affected local communities, and ultimately the State.

4. *Would you please elaborate on how CSAPR represents a “fundamental change” as mentioned above [in the Board’s quotation from the Petition at page 15].*

15. The Multi-Pollutant Standard (“MPS”) was adopted in the rulemaking where the Agency and Board were responding to the requirement to address the federal Clean Air Mercury Rule (“CAMR”), PCB R06-25. The MPS was partially the result of both the Agency’s and DMG’s recognition that the companion federal CAIR and attainment of the PM_{2.5} NAAQS would, practically speaking, require reductions of emissions of NO_x and SO₂. The MPS represented a compromise to achieve at least some of those reductions. Additionally, DMG was engaged in business planning to comply with the provisions of the consent decree entered in *United States, et al., v. Illinois Power Co., et al.*, No. 99-CV-833-MJR (S.D. Ill.) (entered May 27, 2005), which included requirements addressing the same pollutants as the MPS. Therefore, it was important to DMG to ensure that the MPS conformed with the consent decree to the extent possible and to avoid potentially inconsistent or even competing compliance requirements. Reflecting the CAIR, Part 225 would require the surrender of a number of Clean Air Act Title IV Acid Rain Program SO₂ allowances in addition to those required to be surrendered under the Acid Rain Program itself. *See* 35 Ill. Adm. Code § 225.310(a); 40 CFR 96, Subparts AAA, BBB, FFF, GGG, and HHH. Likewise, the consent decree required the surrender of Title IV Acid Rain Program SO₂ allowances. Therefore, at the time that Section 225.233(f) was adopted, it applied to Title IV Acid Rain Program allowances and reflected DMG’s (and the Agency’s) understanding that Title IV Acid Rain Program allowances were the only SO₂ allowances to which it applied.

16. The court in *North Carolina v. EPA*,¹⁵ held that USEPA improperly relied on Acid Rain Program SO₂ allowances in the CAIR. The court remanded the entirety of the CAIR. USEPA then developed the CSAPR, including its Clean Air Act Title I SO₂ trading program wholly separate from and in addition to the Acid Rain Program. It is a fundamentally different program based on an entirely new trading currency (*i.e.*, Title I CSAPR SO₂ allowances as opposed to Title IV Acid Rain Program SO₂ allowances). Thus, USEPA has recognized that consent decrees, such as the DMG consent decree, that require the surrender of only Title IV Acid Rain Program SO₂ allowances do not require the surrender of CSAPR Title I SO₂ allowances. USEPA, *Assessment of Impact of Consent Decree Annual Tonnage Limits on CSAPR Allocations*, Technical Support Document, Docket I.D. No. EPA-HQ-OAR-2011-0491 (Oct. 4, 2011), finalized at 77 Fed. Reg. 10,324 (Feb. 21, 2012) (*See* Table 10; USEPA specifically concludes there is no potential impact from the surplus allocation to Illinois Power, now DMG). That is, while DMG is required to surrender Title IV Acid Rain Program SO₂ allowances under the terms of its consent decree, it is not required to surrender CSAPR Title I SO₂ allowances under its consent decree, and USEPA did not adjust DMG's allowance allocations to reflect such a surrender. *Assessment of Impact TSD*.

17. Meanwhile, in R09-10, the Board amended Section 225.233(f)(4) by changing the definition of NO_x and SO₂ allowances. This 2009 amendment of the definition of SO₂ allowances subject to the allowance trading restrictions of Section 225.233(f) fundamentally changed the rule from the understanding between DMG and the Agency when the MPS was proposed and initially adopted. The Board added the language "or any future federal NO_x or

¹⁵ 531 F.3d 896 (D.C. Cir. 2008), *modified in reh'g*, *North Carolina v. EPA*, 531 F.3d 1176 (D.C. Cir. 2008).

SO₂ emissions trading programs that modify or replace these programs.” *See* Attachment 2, p. 42 of the Board’s Opinion and Order Final Notice, R09-10 (June 18, 2009). With the development of the CSAPR, which does not rely on Acid Rain Program SO₂ allowances, but rather includes allocation of SO₂ allowances created solely and uniquely for the CSAPR, the scope of the restriction in the MPS was effectively changed. It was expanded to include an unanticipated and unforeseen program with economic consequences that could not have been predicted at the time that DMG agreed to the language of the MPS and opted-in to that program. Likewise, neither the Agency nor any affected persons could have envisioned the structure of this subsequent program and its arguably more stringent restrictions on downwind impacts while still providing the efficiencies of a cap and trade program.

18. The amendment to Section 225.233(f)(4) fundamentally changed the scope of the MPS. Now the MPS does not track DMG’s consent decree, a basic premise in DMG’s agreement to the MPS when it was developed and adopted.

5. *Will Dynegy be able to realize allowances per section 225.233(f)(3) as well as those sought in the variance?*

19. DMG does not know at this time whether it will be able to realize any SO₂ allowances as provided in Section 225.233(f)(3). Whether DMG will be able to realize any such allowances depends on several currently unpredictable factors, including the cost of lime and coal, unit capacity factors, energy prices, and performance of the last scrubbers to become operational (*i.e.*, Baldwin Unit 2 and Havana Unit 6).

6. *Assuming an April 1, 2015 compliance deadline, please include more detail in the compliance plan proposed on page 27 of the petition. Please include [a] the estimated time schedule for the Baldwin Unit 2 dry scrubber/fabric filter system and Havana Unit 6 dry scrubber to become operational, [b] the estimated costs for remaining work to be done at Baldwin Unit 2 and Havana Unit 6, [c] the amount of SO₂ CSAPR allocations to be sold or traded, [d] the estimated time schedule for allowances to be sold or traded, and [e] the time schedule when sale or trade of excess SO₂ CSAPR allowances will cease.*

20. DMG does not believe that the information the Board has requested in Question 6 is proper for inclusion in the compliance plan for this variance. DMG believes the conditions and compliance plan proposed by the Agency, Rec. p. 13, are appropriate and acceptable and sufficient. Nevertheless, DMG provides answers to the Board's questions below for the purpose of further informing the Board in the areas the Board has identified.

[a] The consent decree prohibits DMG from operating Baldwin Unit 2 and Havana Unit 6 after December 31, 2012, unless DMG has installed and has commenced operation of dry scrubbers and fabric filter systems on those units. DMG did not intend that installation and operation of these consent decree-mandated control systems should be prerequisites or conditions to the Board's granting the requested variance. DMG provided information regarding the outages that will be necessary and the corresponding reductions in SO₂ emissions both from the outages and from operation of the dry scrubber as indications to the Board that DMG is proceeding with compliance with the MPS and that SO₂ emissions are, actually, being reduced.

[b] DMG estimates that the total cost for the remaining work at Baldwin Unit 2 and Havana Unit 6 is approximately \$34 million. This estimate includes a number of assumptions about uncertainties beyond DMG's control, such as costs associated with labor and materials. Again, expenditure of that sum of money should not be a condition of the variance.

DMG should not be required to expend a certain amount of money or be prohibited from spending more if it becomes necessary.

[c] The amount of DMG's CSAPR SO₂ allocation that may be sold or traded depends on DMG's actual emissions. Theoretically, DMG could sell the entirety of its allocation and buy back enough allowances to cover its own actual emissions. As indicated in DMG's Petition for Variance, DMG estimates an excess of approximately 23,000 CSAPR SO₂ allowances in each of 2013 and 2014 (*i.e.*, the presumed first two years of the CSAPR). The number of excess allowances that might be sold or traded depends upon demand and the market.

[d] The timeframe for trading CSAPR allowances has already begun.¹⁶ However, the more practical or realistic timeframe for trading CSAPR allowances, *i.e.*, when the allowances will be usable for purposes of compliance and, thus, in greater demand and thereby realize greater value, depends upon the court's decision in the appeal and USEPA's response to that decision. If the court upholds the CSAPR as adopted, then DMG expects that the value of the allowances could increase the day that the decision is handed down. If the court remands some or all of the CSAPR, USEPA may have to take some action that would implement the CSAPR before trading at any value would commence. It is generally expected that allowances will have their greatest value at the beginning of a new trading program.

[e] There is no regulatory time limit on when CSAPR allowances may be sold or traded. Nor does DMG have a time schedule for sale or trade of excess CSAPR SO₂ allowances. The timing of when any such allowances might be sold or traded depends largely upon demand and the market.

¹⁶ In late 2011, USEPA populated CSAPR allowance accounts for 2012 and 2013.

7. (a) ***Given that the first phase of CSAPR has been stayed, please clarify how many CSAPR SO₂ allowances would be allocated to DMG for 2013 and 2014, respectively.***

21. The CSAPR includes a system of allocations with a reduction in the SO₂ allowance allocation in the third year of the program for Group 1 states. DMG has been allocated a total of 49,012 SO₂ allowances per year for each of 2012 and 2013, the first two years of the CSAPR as finally adopted. Under the CSAPR as finally adopted, DMG will be allocated a total of 26,256 allowances for each year thereafter, including 2014, the third year of the CSAPR. Assuming that the CSAPR survives appeal and that USEPA will allow the CSAPR to slide a year, *i.e.*, the first two years are 2013 and 2014 and the third year is 2015, then DMG's allocation for 2014 should also be 49,012 SO₂ allowances. If USEPA persists with the rule as adopted, assuming that the court upholds the rule, then DMG would be allocated only 26,256 SO₂ allowances in 2014 and would have very few, if any, excess allowances.

7. (b) ***Please clarify how many of the 2013 and 2014 SO₂ CSAPR allowances DMG projects will be excess.***

22. DMG estimates that approximately 23,000 of the 49,012 allowances allocated to the DMG system in Illinois will be in excess of the MPS SO₂ compliance requirements in each of 2013 and 2014, assuming 2014 is the second (rather than third) year of the CSAPR. DMG cannot be any more precise than that. DMG's reference in the Petition to "approximately 20,000 allowances," Pet., p. 26, was merely shorthand; we regret causing confusion.

7. (c) ***Please state the amount of SO₂ emissions that would be allowed from any facility if the requested variance is granted, compared to that which would result if immediate compliance is required. In particular, please provide a specific estimate of the net difference between SO₂ emissions under the MPS requirement of 225.233(f)(2) (considering allowances surrendered to IEPA) and under the variance for 2013 and 2014 (considering allowances to be sold or traded).***

23. DMG is not certain what the Board means by “any facility.” If the Board is referring to DMG’s power plants, the granting of the variance will not affect emissions at all. Each of DMG’s coal-fired EGUs is subject to SO₂ emissions rate limitations pursuant to the consent decree. Additionally, the consent decree established a mass cap on DMG’s system-wide SO₂ emissions. The MPS also imposes a system-wide SO₂ emission rate. None of these limitations would be changed by the requested relief.¹⁷ The CSAPR allocates allowances and requires that DMG surrender an allowance for each ton of SO₂ emitted in a year plus additional allowances if the State of Illinois exceeds its variability limit and DMG also exceeds its share of the statewide variability limit. Otherwise, the CSAPR imposes no SO₂ limitations.

24. If the Board means by “any facility” any source subject to the CSAPR, DMG has no way of knowing how many tons of SO₂ might be emitted either with or without the variance being granted to DMG. Even though DMG may sell an allowance, DMG cannot predict when the allowance may be used, if ever. The buyer may use it immediately, never, or sometime in the future.

¹⁷ DMG also operates several gas- and oil-fired peaking EGUs that are subject to the CSAPR but are not subject to the MPS or the consent decree. The granting of this variance will not affect SO₂ emissions from these units. These EGUs operate infrequently in response to market demand, generally have minimal mass SO₂ emissions, and are subject to SO₂ emission rate limitations established in their air permits.

8. ***Dynegy proposed wording for the variance on pages 26-27 of the petition, but the wording does not appear to be contingent upon CSAPR being reinstated. Would you please propose such wording?***

25. USEPA has already allocated CSAPR allowances for 2012 and 2013 and populated source allowance accounts. Therefore, as relevant to the Petition, there could be some market for 2013 SO₂ allowances today.¹⁸ According to *Argus Air Daily*, the market is currently flat; nevertheless, there is a market. That being the case, making the variance contingent upon the reinstatement of CSAPR is not necessary. DMG believes the wording of the variance on pages 26-27 of the Petition is consistent with the Agency's Recommendation and reflects the scope of the relief that DMG seeks.

26. If the Board, however, determines that granting the variance should be contingent upon the CSAPR being reinstated, DMG suggests the following revised language for the variance (revisions are double underscored):

Subject to reinstatement of the CSAPR, the term of the variance shall commence upon the date of the Board's order granting the variance and shall terminate April 1, 2015. The variance is applicable to vintage 2013 and 2014 CSAPR SO₂ allowances. The following conditions shall apply to the variance:

- A. During the term of the variance, DMG shall not be subject to the requirements of Section 225.233(f)(2) relative to vintage 2013 and 2014 CSAPR SO₂ allowances.
- B. During the term of the variance, DMG shall comply with all other applicable MPS requirements, as otherwise required.
- C. Upon termination of the variance, DMG shall comply with all applicable MPS requirements, including Section 225.233(f)(2).

DMG shall be subject to the following compliance plan:

Within 60 days after termination of the variance, DMG shall prepare and submit to the Agency a report identifying the amount of SO₂ emissions


¹⁸ The MPS SO₂ allowance restriction does not apply in 2012.

from its coal-fired power plants during the term of this variance and the tons of SO₂ removed by DMG's spray dry absorbers during the term of the variance.

Respectfully submitted,

DYNEGY MIDWEST GENERATION, LLC

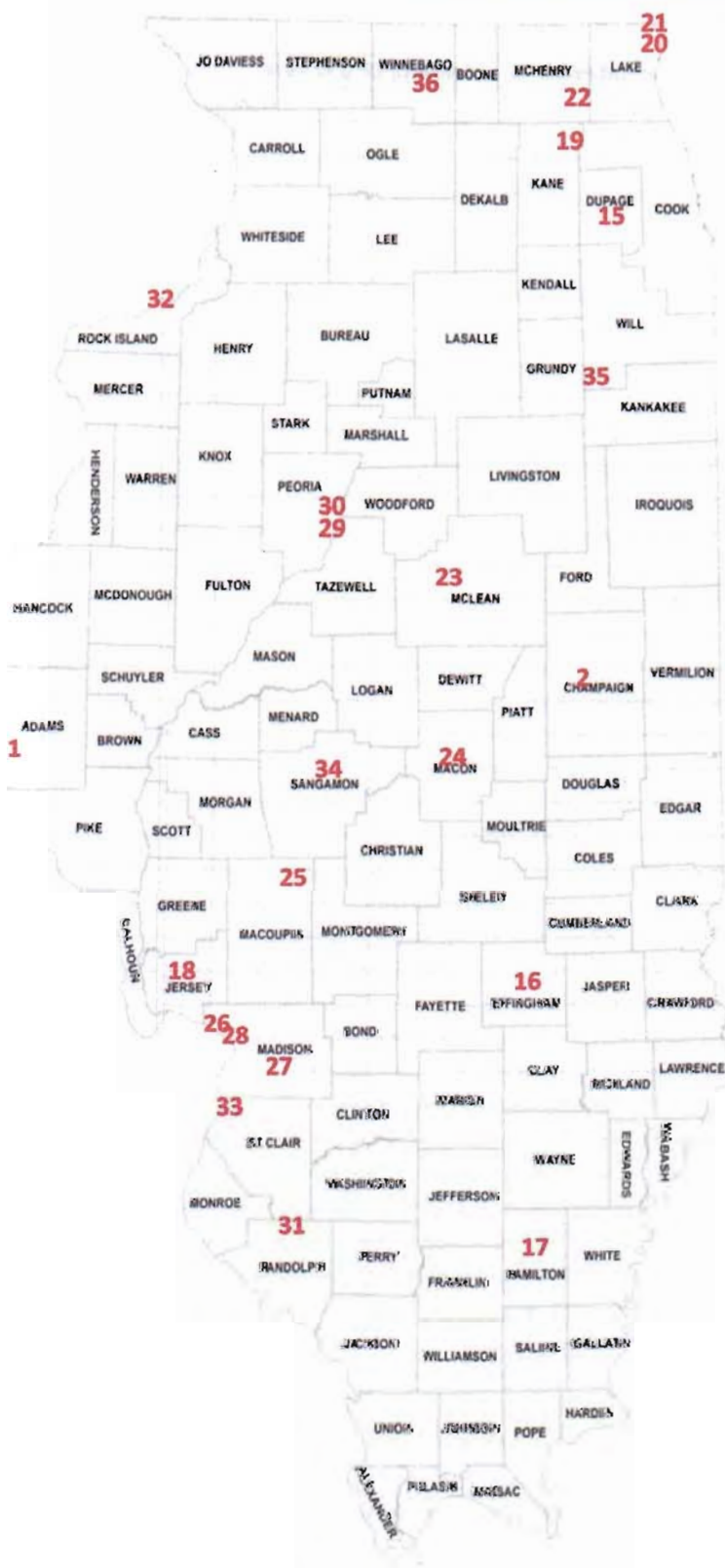
by:



One of its Attorneys

Dated: August 9, 2012

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Site ID	Site Name
1.	170010007 Quincy
2.	170190004 Champaign
3.	170310001 Alsip
4.	170310032 Chicago - South Water Filtration Plant
5.	170310042 Chicago - Willis Tower
6.	170310064 Chicago - University of Chicago
7.	170310072 Chicago - Jardine Water Plant
8.	170310076 Chicago - Com Ed Maintenance Bldg.
9.	170311003 Chicago - Taft High School
10.	170311601 Lemont
11.	170314002 Cicero
12.	170314007 Des Plaines
13.	170314201 Northbrook
14.	170317002 Evanston
15.	170436001 Lisle
16.	170491001 Effingham
17.	170650002 Knight Prairie
18.	170831001 Jerseyville
19.	170890005 Elgin
20.	170971002 Waukegan
21.	170971007 Zion
22.	171110001 Cary
23.	171132003 Normal
24.	171150013 Decatur
25.	171170002 Nilwood
26.	171190008 Alton
27.	171191009 Maryville
28.	171193007 Wood River
29.	171430024 Peoria
30.	171431001 Peoria Heights
31.	171570001 Houston
32.	171613002 Rock Island
33.	171630010 East St. Louis
34.	171670010 Springfield
35.	171971011 Braidwood
36.	172012001 Loves Park

- 2) The owners or operators of EGUs in an MPS Group must not sell or trade to any person or otherwise exchange with or give to any person SO₂ allowances allocated to the EGUs in the MPS Group for vintage years 2013 and beyond that would otherwise be available for sale or trade as a result of actions taken to comply with the standards in subsection (e) of this Section. Such allowances that are not retired for compliance, or otherwise surrendered pursuant to a consent decree to which the State of Illinois is a party, must be surrendered to the Agency on an annual basis, beginning in calendar year 2014. This provision does not apply to the use, sale, exchange, gift, or trade of allowances among the EGUs in an MPS Group.
- 3) The provisions of this subsection (f) do not restrict or inhibit the sale or trading of allowances that become available from one or more EGUs in a MPS Group as a result of holding allowances that represent over-compliance with the NO_x or SO₂ standard in subsection (e) of this Section, once such a standard becomes effective, whether such over-compliance results from control equipment, fuel changes, changes in the method of operation, unit shut downs, or other reasons.
- 4) For purposes of this subsection (f), NO_x and SO₂ allowances mean allowances necessary for compliance with Sections 225.310, 225.410, or 225.510, 40 CFR 72, or ~~subparts~~ Subparts AA and AAAA of 40 CFR 96, or any future federal NO_x or SO₂ emissions trading programs that modify or replace these programs. This Section does not prohibit the owner or operator of EGUs in an MPS Group from purchasing or otherwise obtaining allowances from other sources as allowed by law for purposes of complying with federal or state requirements, except as specifically set forth in this Section.
- 5) ~~By~~ Before March 1, 2010, and continuing each year thereafter, the owner or operator of EGUs in an MPS Group must submit a report to the Agency that demonstrates compliance with the requirements of this subsection (f) for the previous calendar year, and which includes identification of any allowances that have been surrendered to the USEPA or to the Agency and any allowances that were sold, gifted, used, exchanged, or traded because they became available due to over-compliance. All allowances that are required to be surrendered must be surrendered by August 31, unless USEPA has not yet deducted the allowances from the previous year. A final report must be submitted to the Agency by August 31 of each year, verifying that the actions described in the initial report have taken place or, if such actions have not taken place, an explanation of all changes that have occurred and the reasons for such changes. If USEPA has not deducted the allowances from the previous year by August 31, the final report ~~will~~ must be due, and all

CERTIFICATE OF SERVICE

I, the undersigned, certify that on this 9th day of August, 2012, I have served electronically the attached **DMG'S RESPONSE TO THE BOARD'S QUESTIONS**, upon the following persons:

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