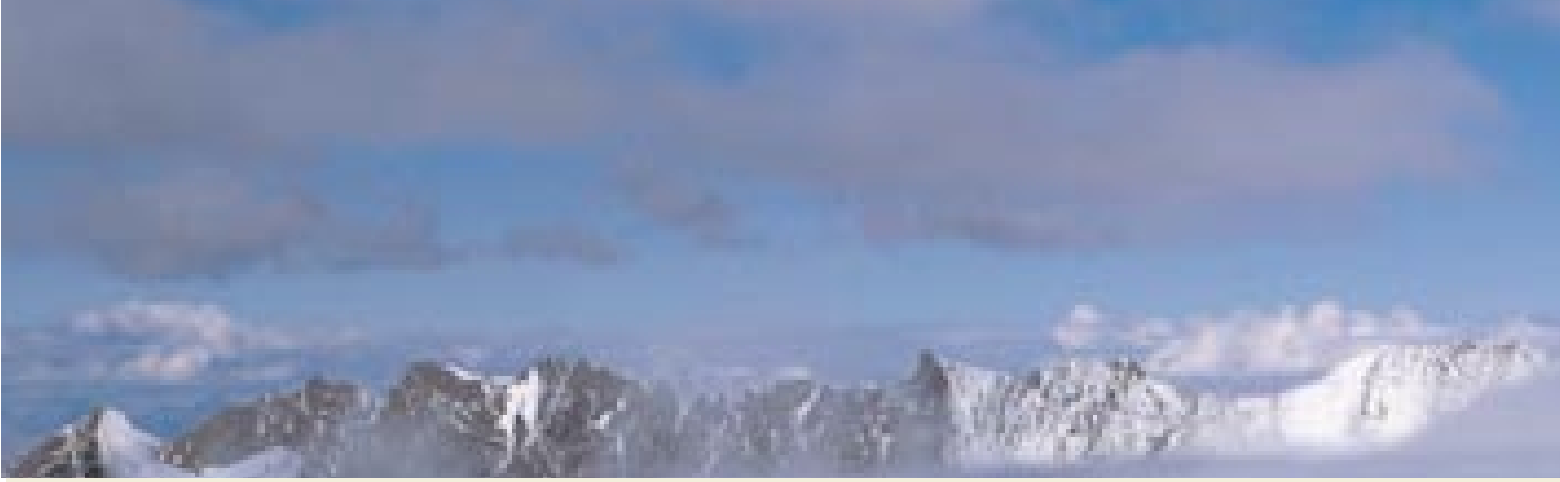

Clear Skies & New Source Reform:

The Politics Of

Politicians spent a lot of time in 2002 playing Clean Air Act ball, but they failed to advance it much. The Bush administration's Clear Skies Initiative legislation finally emerged as legislation late last summer; only to languish while more pressing public issues involving terrorism and the economy took center stage in Congress. Threatened appropriations riders to ban expenditure of authorized monies to implement new source review reform also were stalled in the tortuous continuing resolution process in Congress last fall. These Washington shenanigans raise questions about what Clean Air Act reforms public power utilities need over the long-run, especially from legislation such as the Clear Skies Initiative.

The Clear Skies Initiative and reform of New Source Review (NSR) dominate the clean air policy agenda right now. Both are highly charged political issues, underpinning President Bush's public persona and providing a vehicle for certain state attorneys general who aspire to higher public office. Both pivot ultimately on the need for new electric generating capacity.

The White House sent its Clear Skies legislation to Congress last July. The legislation would require dramatic cuts in power plant emissions to protect public health and precious ecosystems. Congressmen Billy Tauzin, R-La., and Joe Barton, R-Texas, and Sen. Bob Smith, R-N.H., (defeated in the New Hampshire Republican Party and recently replaced by Republican challenger John Sununu Jr. in the Nov. 5 election) who introduced the legislation in 2002. The Clear Skies bill sets mandatory caps on emissions of sulfur dioxide, nitrogen oxide and mercury emissions from the nation's power plants. It would require an overall 70 percent cut in emissions by eliminating 35 million tons of these pollutants over the next decade. President Bush contends that because Clear Skies is modeled on EPA's "most effective" Clean Air Act program—the market-based acid rain program enacted as part of the 1990 Clean Air Act Amendments—Clear Skies will ultimately be better for the environment and for utilities than existing command-and-control Clean Air Act rules that the legislation would replace. The Bush administration also argues that Clear Skies will enhance U.S. energy security by enabling the continued use of diverse fuels in generating electric power.

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Other features of Clear Skies include:

- Allowances and "cap and trade" programs for sulfur dioxide, nitrogen oxide and mercury.
- New clean coal technology initiatives.
- New "Phase III" reductions of sulfur dioxide (to a 4.5 million ton cap) by 2010, based on the existing acid rain allowance program.
- Auctions of allowances under a cap and trade program;
- A cap and trade program for nitrogen oxides based on the existing nitrogen oxide program in Title IV of the act with 1.562 million-ton cap in 2008 and a 1.162 million-ton cap in 2018.
- Mercury reductions based on caps and allocation procedures starting at 26 million tons in 2010 and 15 million tons in 2018.
- Performance standards for new boilers, combustion turbines and integrated gasification combined-cycle plants covered under the act. These new federal performance standards will include limits for sulfur dioxide, nitrogen oxide, particulate matter and mercury.
- Research, monitoring and assessment programs;
- A utility exemption from NSR and best available retrofit technology (BART) for existing utilities under EPA's regional haze rule (required about 2008), (but no

Clean Air

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exemption for past NSR violations involving modifications to existing sources and no changes to current preconstruction requirements in the prevention of significant deterioration (PSD) requirements for the protection of Class I areas for modifications of facilities within 50 kilometers of a national forest, park or wilderness area.

- Nonattainment areas under the revised eight-hour ozone and new particulate matter-fine ambient air quality standards will be treated as transitional areas if states can take into account emission caps from the legislation in lieu of other emissions data;
- Exemption of utilities from Section 112 National Emission Standard for Hazardous Air Pollutants mandates to install maximum achievable control technology (MACT) for mercury and other hazardous air pollutants.
- Limits on state use of transboundary Section 126 petitions and the "good neighbor" provisions of Section 110(a)(2)(D).
- Maintenance of current Section 821(a) (i.e., no "new") carbon dioxide reporting requirements in of the Clean Air Act.

Public acceptance of the Clear Skies legislation is uncertain and it seems generally like the legislation has few strong advocates outside the Bush White House. Many electric generators have offered guarded support, questioning particulars of the legislation while lauding its general direction. Environmental advocacy groups appear united in their opposition, largely because they feel that overall emission caps and limits are not tough enough and that mercury emissions should not be traded. Environmentalists simply do not buy the administration's theory that mercury emissions reductions will occur when controls are placed on nitrogen and sulfur oxides. Their arguments carry some weight with legislators since they cite the fact that approximately 80 percent of the water bodies that do not meet the Clean Water Act quality standards are also listed due to mercury air deposition to lakes, rivers and ponds. Air pollution control authorities are skeptical of the benefits and the costs of the multi-pollutant bill questioning the local impacts when marketable emissions reductions can be purchased by industries located far away from their local air pollution problems.

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The Bush administration argues that electric utilities should want the Clear Skies bill, because the legislation would alleviate future NSR uncertainty. In fact, no new enforcement cases have been filed in the courts over alleged violation of the NSR preconstruction permit requirements since spring 2002. In part, this is because everyone is awaiting the 11th Circuit U.S. Court of Appeals' ruling on EPA's administrative order finding that the Tennessee Valley Authority violated NSR and other Clean Air Act requirements over 20 years by illegally expanding its generating capacity without permits and pollution controls. In part, the downshift in EPA NSR enforcement reflects the administration's commitment to industry to reform the NSR rules this year to better reflect what the industry understood their applicability to be in the first place.

Backlash on NSR reforms, however, has been brewing in Congress and the environmental groups since EPA announced its intent to issue final NSR rules (the rulemaking, itself, now a 12-year undertaking). In its report to the president on NSR, EPA said it would revise the rules to clear up confusion regarding the applicability of NSR to routine changes (such as boiler tube replacements during unexpected outages)and the rules regarding the types of emission increases that trigger NSR review. Certain congressmen and senators have vowed to take action on EPA's long-awaited revisions to the NSR

rules when they are announced. Environmentalists have labeled the NSR reform rules "the greatest environmental rollback in Clean Air Act history." Congressional opponents of the NSR rule have vowed to effectively kill the new rule by refusing to allow EPA to spend appropriated budget monies to implement or enforce the new rule revisions.

The NSR reform rules and the NSR spending prohibition are directly related to NSR enforcement actions against electric utilities. They are also linked to Clear Skies. For instance, Section 483 of the Clear Skies bill would exempt utilities from NSR if other emission caps were achieved.

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There is no question the Clean Air Act needs to be fixed. The existing law and regulations that surround it are a disaster for the electric generating industry. Utilities are looking at a dizzying and fast-approaching array of new emission control requirements, such as revision of new source performance standards, multiple-state implementation plan revisions to accommodate ozone transport, new national ambient air quality standard for ozone and fine particulates (acid aerosols), and more Section 126 petitions filed by downwind states complaining of pollution transport from other jurisdictions. Even more threatening, perhaps, are EPA's actions to reduce hazardous air pollutants like mercury, hydrogen chloride and hydrogen fluoride from utility boilers in six to nine years, pursuant to the hazardous air pollutant provisions of the act that mandate maximum achievable control technology) based on the best performing plants in the industry and with no consideration of cost to any particular generator. Coupled with the uncertainty created by NSR applicability, Title V operating permit requirements, like upgraded and less burdensome monitoring, Clean Air Act amendments are desirable.

If the Clean Air Act is amended, electric utilities need, more than anything, regulatory certainty and consistency in Clean Air Act regulation. Public power utilities need relief particularly from MACT requirements, including reasonable mercury reduction targets and some relief valves considering fuel type, level of controls already in place, ability to reduce mercury emissions from coal sources, and perhaps size of the utility etc., in case EPA's predictions about fuel availability, co-benefits from the sulfur dioxide and nitrogen oxide controls and new technology do not pan out. Utilities need a single federal program regulating ozone rather than separate state, ozone transport commissions, and other regional air quality regulatory initiatives.

Many public power utilities own new generation and are therefore cleaner compared to other electric utility sectors. Many systems were built in the last 25 years and installed state-of-the-art air pollution controls. Several public power utilities in the ozone transport region (Midwestern and Northeastern states) have purchased and installed low-nitrogen oxide removal technology. Good deeds should be rewarded, not punished. Therefore, national emission caps should credit early emission reductions based on performance standards (regardless of how the utility got there) and should not penalize regulated sources by blindly requiring across-the-board percentage reductions of actual historical emissions.

Public power utilities need assurance that they can obtain needed emission-reduction allowances at a fair price and from outside their territories. They also need assurance that they can sell emission reductions to facilities in other areas.

Utilities need new source review relief in the guise of clear and reasonable rules that exempt routine repairs. Plants located near parks must be permitted to be refurbished if reasonable environmental controls are installed. Public power utilities also need relief from the uncertainty resulting from EPA enforcement of old, confusing NSR rules.

Many public power entities do not have the same financial flexibility investor-owned utilities have when installing pollution controls. It's often harder for a public power utility to transfer load to other boilers or to buy energy off the grid. Public power utilities also may not have quick recourse to the large amounts of capital that private companies have to finance pollution retrofit projects on a short-term basis. Purchasing off the grid may be far more expansive than self-generation of energy.

While Clear Skies tries to make market-based approaches attractive so emission reductions can be bought or sold, additional mechanisms may be needed to assure that public power utilities can buy emission reductions when needed.

Public power utilities need fair treatment to meet the goals of Clear Skies and other Clean Air Act amendments when considering their service to the local community as a partner to the state and local government. This fair treatment could come in the form of a variety of accommodations in the legislation—sensitivity to certain system size cut-offs, deadline adjustments for differently sized utilities, or tradable tax credits and incentives. These topics will require a great deal of discussion as the legislation heats up in the 108th Congress beginning in January.