

SOUTH COAST AIR QUALITY MANAGEMENT DISTRICT

SCAQMD's Revised NSR Offset Tracking System

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PROPOSED SCAQMD NSR OFFSET TRACKING SYSTEM

BACKGROUND

In general, the Federal and California Clean Air Acts require that, among other things, emission increases of non-attainment air pollutants from new and modified major sources be offset with emissions reductions. The SCAQMD has implemented an NSR tracking system to demonstrate adequate emission reductions for sources exempt from emission offsets requirements under Regulation XIII – New Source Review, which are otherwise subject to offset requirements under federal and state NSR programs. SCAQMD staff has prepared annual reports which track credits and debits for each year and present the remaining balances of credits in SCAQMD’s offset accounts. The NSR tracking reports go back to the year 1990, which reflects the year when major amendments were made to SCAQMD’s Regulation XIII. A key source of credits in the tracking system has been “orphan” shutdowns of major sources. Other credit sources have been “negative NSR balances” resulting from permit actions prior to 1990, and the “BACT discount” currently required by Regulation XIII when banking emission reduction credits (ERCs).

In 2002 SCAQMD adopted an Offset Budget rule (Rule 1309.2 – Offset Budget) as part of SCAQMD’s NSR program to address some of the shortage problems with ERCs. As part of the discussions with EPA regarding Rule 1309.2, EPA has raised some questions related to the credits in SCAQMD’s offset accounts for use in the Offset Budget rule. Among the key issues raised by EPA are the following:

- creditability of pre-1990 emission reductions, particularly reductions for which no records are currently available;
- creditability of reductions resulting from the BACT discount of newly-banked ERCs, since the discount is presumably also used to satisfy the federal time of use discount requirement;
- baseline calculation procedures to assure an “actual” baseline;
- surplus adjustment at time of use of credits in the tracking system; and
- consistency of credit use with assumptions in the SIP.

EPA staff has stated that these issues must be resolved in order for the federal agency to approve amendments to Regulation XIII as a result of adoption of Rule 1309.2, which establishes an “Offset Budget.” EPA staff has also requested that SCAQMD adopt a rule specifying how the tracking of debits and credits will occur in the future. The purpose of this document is to address issues raised by EPA with SCAQMD’s offset account credits and to propose an NSR offset tracking system to be used for the tracking of all future credits. Based on this, SCAQMD will then develop a new rule for tracking of NSR debits and credits and submit it to EPA so that EPA can SIP approve this rule along with Rule 1309.2 – Offset Budget.

PROPOSAL SUMMARY

After numerous meetings and conference calls with EPA, SCAQMD staff agreed to review the offset accounts in consideration of EPA's comments. Since that time, SCAQMD staff has spent over 6,000 person-hours reviewing the offset records in the NSR tracking system. In addition, SCAQMD Executive and senior management and other staff have spent hundreds of hours evaluating offset accounts and the tracking system. In order to resolve EPA's comments, SCAQMD staff is proposing several modifications to procedures used in the tracking system. In the revised procedures SCAQMD has proposed elimination of all credits for which SCAQMD no longer retains documentation. SCAQMD has also included additional classes of credits in the tracking system, namely orphan shutdowns of minor sources and other surplus reductions. As a result of these proposed modifications, and even with the inclusion of the minor source orphan shutdowns and other surplus reductions, SCAQMD's previously-reported 2002 NSR federal offset account balances for all pollutants, except for NO_x, will be reduced, depending on the pollutant, by from about 12 % to 74 %. Several elements of the proposed revisions to SCAQMD's tracking system contribute to these reductions, as discussed below, but the single element of the proposal with the greatest contribution is the reevaluation of pre-1990 credits and proposed elimination of all credits for which SCAQMD no longer retains documentation. As a result of this proposed change, SCAQMD's pre-1990 credits will be reduced, depending on the pollutant, by from 7 % to 92 %. The specific amounts of reductions for each pollutant for the pre-1990 credit account balances and the 2002 NSR federal offset account balances are shown in Table 1.

Table 1
Reductions in SCAQMD's Pre-1990 Credit Account and 2002
NSR Federal Offset Account Balances Resulting from
Implementation of Proposed Changes to the NSR Tracking System

	VOC	NO _x	SO _x	CO	PM ₁₀
Reduction in SCAQMD's Pre-1990 Credit Account Balances	58 %	7 %	56 %	76 %	92 %
Reduction in SCAQMD's 2002 NSR Federal Offset Account Balances	34 %	-40 %	44 %	67 %	83 %

The proposed modifications to SCAQMD's NSR tracking procedure are described in more detail below. Also, the detailed line-by-line adjusted credit balances that result from the proposed modified procedures are shown in Attachment 1: *SCAQMD's NSR Offset Tracking—Federal Running Balances*. We anticipate that changes to the SCAQMD's NSR tracking procedures for all future credit accounting will be incorporated into a proposed tracking rule that will be subject to a public workshop prior to final adoption.

In summary, the key elements of SCAQMD's proposal are as follows:

Sources of Credits.

The tracking system uses credits derived from reductions not required by federal law. These primarily include “orphan shutdowns,” *i.e.* real, permanent, enforceable, surplus, and quantifiable emission reductions resulting from shutdowns of sources for which no ERCs were issued. In addition, these will also include surplus emission reductions otherwise not required by the federal NSR program. SCAQMD has in the past only utilized orphan shutdowns of major sources as credits. This in part has been due to the fact that SCAQMD's offset account has held a large balance of credits and there has been no need for additional sources of credits to fund the offset account. The current proposal, however, also includes use of credits derived from orphan shutdowns of non-major sources for which no ERCs were issued and other surplus emission reductions otherwise not required by the federal NSR program in order to better utilize the sources of credits used for SCAQMD's offset accounts.

The proposed SCAQMD tracking system is also based on past use of a portion of the pool of credits which has been validated and generated through emission reductions at permitted stationary sources that occurred prior to 1990. As is described below, all of the pre-1990 CO and PM10 credits and a large portion of VOC and NOx pre-1990 credits were depleted in the mid 1990's—prior to the time of EPA's most recent SIP approval of Regulation XIII in 1996. On the other hand, only a small portion of the pre-1990 SOx credits has been consumed because there is little demand for SOx offsets from major non-RECLAIM sources. As part of this proposal and to address EPA's comments regarding the use of pre-1990 credits, SCAQMD proposes retroactive elimination of all pre-1990 credits for which SCAQMD no longer retains documentation and in addition not to utilize from now on any remaining pre-1990 credits.

Another source of credits used by SCAQMD in the past has been the BACT discount of the post-1990 ERCs issued by SCAQMD. As part of this new proposal, and specifically to address EPA's comments, SCAQMD proposes to discontinue deriving credits from the “BACT discount” of emission reductions banked as ERCs. This credit was specifically authorized according to the Technical Support Document for EPA's approval of Regulation XIII in 1996. EPA, however, has brought up the point that the BACT discount is used for another purpose—in lieu of a time of use discount, and thus should not be used as a tracking system credit.

Furthermore, as part of this proposal and again specifically to address EPA's comments, SCAQMD proposes from now on to further adjust the orphan shutdown credits by reducing their value to address EPA's comments about actual emissions and to further adjust any orphan shutdown credits not used in the same time frame they are generated via a BARCT adjustment at time of use to address EPA's comments regarding surplus adjustment at time of use.

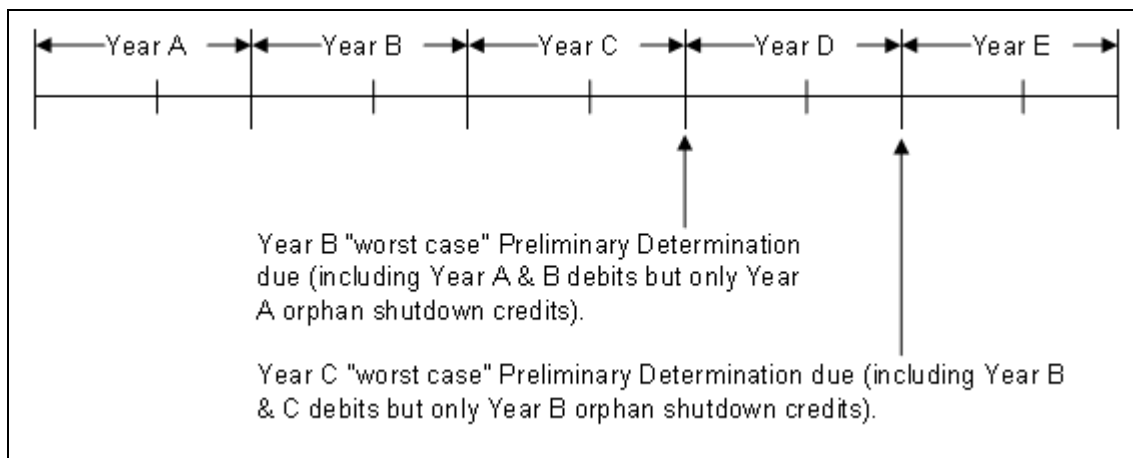
Use of Credits

The above-described credits will be used to fund the new Offset Budget as adopted by SCAQMD in Rule 1309.2, in addition to the previous use of credits to provide offsets for sources that are exempt from offset requirements under Regulation XIII (Rules 1304 – Exemptions and 1309.1 – Priority Reserve), which are otherwise subject to the offset requirements under federal NSR, as part of the demonstration of equivalency to federal NSR requirements. A complete list of Regulation XIII offset exemption provisions for which credits need to be used to demonstrate equivalency if offsets are otherwise required is included in Attachment 2.

Tracking and Backstop

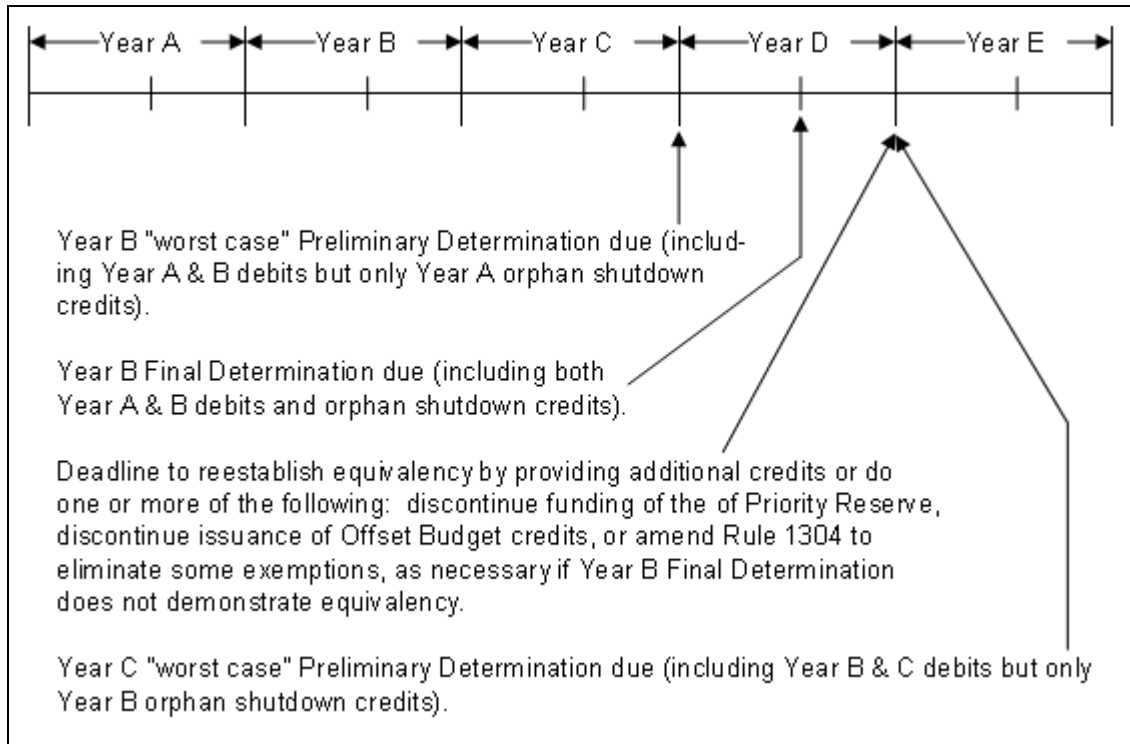
SCAQMD will make an annual equivalency demonstration in two steps. In step one, SCAQMD proposes to make a preliminary annual determination of equivalency within twelve months of the close of each reporting period which will also be reflected in a tracking rule that it will develop and adopt. Such preliminary annual determination will be a very conservative determination based on the combined debits from the previous year but will not include the orphan shutdowns (credits) from that reporting period. Therefore, the preliminary annual determinations will represent “worst case” analyses. Provided the preliminary annual determination demonstrates equivalency, the orphan shutdowns for each reporting period will be reported (and credited) in the subsequent preliminary annual determination, as illustrated in Figure 1. However, if the preliminary

Figure 1
Equivalency Demonstration Timeline
(Preliminary Determination Demonstrates Equivalency)



annual determination does not demonstrate equivalency, SCAQMD proposes as step two to make a final annual determination of equivalency, which will include the reporting period's orphan shutdown credits. The final equivalency determination will be prepared within six months of the preliminary equivalency determination time frame, as illustrated in Figure 2. For example, the preliminary

Figure 2
Equivalency Demonstration Timeline
(Preliminary Determination Does Not Demonstrate Equivalency)



annual determination for reporting year B (including all debits for years A and B and only orphan shutdown credits for year A) will be completed by the end of reporting year C. Provided this preliminary annual determination for year B demonstrates equivalency, the year B orphan shutdowns will be included in the preliminary annual determination for year C (to be completed by the end of year D). On the other hand, if the preliminary annual determination for year B does not demonstrate equivalency, a final annual determination incorporating year B's orphan shutdown credits will be prepared within six months of the end of year C. The offset accounting will be conducted in the following order:

1. Year B's debits are first subtracted from any remaining pre-1990 credits (1990-2005 timeframe only); then
2. Any debits remaining after step 1 are subtracted from any post-1990 credits remaining from year A; then
- 3a. If there are no remaining debits the post-1990 credits remaining from step 2 are discounted as described in the discussion of Surplus Discount at Time of Use. Year B's credits are then added to the discounted post-1990 credits remaining from the year A.

- 3b. If there are any remaining debits from step 2 (meaning there are not any post - 1990 credits remaining) the year B's remaining debits are subtracted from year B's credits.

Each preliminary annual determination (and each final annual determination, as needed to demonstrate equivalency) will be presented to SCAQMD's Governing Board in a report from the Executive Officer ("Board Letter") at a public meeting of the SCAQMD Governing Board. The annual equivalency determination will include the balance in SCAQMD's offset account for each pollutant, as well as summaries of credit and debit data by category such as Priority Reserve, Community Bank, and Rule 1304 exemptions.

In addition, SCAQMD proposes to evaluate the future availability of credits in SCAQMD's offset accounts by conducting a two-year projection of debits, credits, and account balances in conjunction with (but not as a part of) each annual equivalency demonstration. This analysis will include projected debits, credits, and offset account balances for the two years following the period covered by the Board Letter for purposes of predicting if there will or will not be sufficient credits in SCAQMD's offset accounts. The projection for each pollutant will be based on the average of the previous five years' credits and debits for that pollutant. The Executive Officer will not make quarterly allocations to the Priority Reserve for any pollutant during a time when SCAQMD's offset account for that pollutant is not projected to remain positive¹. The purpose of the projections is to prospectively determine if sufficient offsets remain in SCAQMD's accounts to continue funding the Priority Reserve; they are not intended to demonstrate equivalency retrospectively. SCAQMD is currently developing amendments to Rule 1309.1 – Priority Reserve which will clarify this procedure and authority for the Executive Officer and the tracking rule (also under development) will call for these projections and direct the Executive Officer to exercise this authority when equivalency is not projected.

SCAQMD will also propose, as part of the tracking rule, backstop provisions to be triggered in the event that the final annual determination does not demonstrate equivalency. In such an event, the backstop provisions would require SCAQMD to take one or more of the following actions to the extent necessary to correct the credit shortfall:

¹ Offsets provided from the Priority Reserve are debited from SCAQMD's offset accounts for the period during which the permit was issued (*i.e.*, for the timeframe they are used) whereas the quarterly allocations made to the Priority Reserve pursuant to Rule 1309.1(a) do not constitute debits from SCAQMD's offset accounts. The newly-proposed future years' projections of balances in SCAQMD's offset accounts will include projected use of Priority Reserve offsets as well as offsets used through the Community Bank and for sources exempted pursuant to Rule 1304. In addition, a significant portion of the quarterly allocations to the Priority Reserve are used by sources which are not subject to federal offset requirements (*i.e.*, federal minor sources) and, therefore, do not need to be debited from SCAQMD's offset accounts for the purpose of federal equivalency demonstration. Furthermore, the portion that is subject to federal offset requirements and which needs to be debited from SCAQMD's offset accounts is already included in the two future years' projections done with each annual equivalency demonstration.

- Provide additional credits within six months of the final annual determination; such credits could be derived through SCAQMD purchase of credits, through SCAQMD funding of emission reduction projects using quantification protocols approved by EPA on a case-by case or programmatic basis, application of LAER in excess of federal requirements², or other approved sources of credits.
- Suspend issuance of both Priority Reserve and Offset Budget credits (Rules 1309.1 and 1309.2) within 90 days and not resume the issuance of any such credits until SCAQMD has demonstrated that equivalency has been reestablished. Equivalency may be reestablished through procurement of additional offsets and/or appropriate program modifications.
- Amend Rule 1304 to eliminate certain categories of offset exemptions to be identified during the rulemaking process.

The following is a more detailed description of the proposed changes.

SOURCES OF CREDITS

SCAQMD has described in its annual status reports on Regulation XIII a 1990 starting balance for federal and state offset accounts based on data available in 1990. While a large portion of pre-1990 credits were used years ago, EPA staff has requested an accounting of the validity of such credits to ensure that such credits were creditable. To that end, EPA staff has raised questions about the availability of all records relating to the pre-1990 credits. To address the issues raised by EPA, SCAQMD staff spent several thousand staff hours reviewing and evaluating all available data for the pre-1990 credits in its 1990 starting balances. The following is a description of sources of credits in SCAQMD's tracking system organized by time period of credit generation including: pre 1990, 1990-2005, and post 2005. This division is due to differing provisions of SCAQMD rules applicable to generation of credits in these time periods, and to new tracking system elements proposed for post-2005 credits.

Technical Support Document

EPA issued a *Technical Support Document for EPA's Notice of Final Rulemaking for the California State Implementation Plan South Coast Air Quality Management District New Source Review* (TSD) October 24, 1996 in support of EPA's approval of SCAQMD 1996 New Source Review amendments into California's State Implementation Plan (SIP). The TSD identifies specific sources of emission reductions and emission increases that are approved for inclusion in SCAQMD's tracking system for purposes of demonstrating equivalency between the federal Clean Air Act (CAA) and SCAQMD's SIP-approved

² Precise quantification of all surplus credits generated through application of LAER in excess of federal requirements may be extremely resource intensive. Therefore, SCAQMD may, with EPA approval, demonstrate that such application of LAER has generated at least enough surplus reductions to make up for the shortfall using very conservative assumptions to estimate the surplus reductions.

NSR program. The various approved sources of emission decreases (credits) referred to throughout this document are briefly discussed below:

- **Surplus Reductions Resulting from use of ERCs by Minor Sources**
Rule 1303 – Requirements specifies that minor sources must offset their emission increases by surrendering ERCs unless otherwise exempt pursuant to Rule 1304 but the CAA does not require emission offsets from minor sources. Therefore, emission offsets supplied by minor sources in the form of ERCs represent creditable, surplus reductions. The TSD only specifically identifies this source of emission reductions/credits for minor VOC sources, but the underlying logic applies equally to minor sources of NO_x, SO_x, CO, and PM₁₀.
- **Surplus Reductions Resulting from use of ERCs by Major Sources of SO_x, CO, and PM₁₀**
Rule 1303 requires use of ERCs to offset increases of SO_x, CO, and PM₁₀ emissions from major sources at a 1.2 to 1.0 offset ratio while the CAA requires such increases to be offset at a ratio of at least 1.0 to 1.0. Therefore, the difference in ERCs surrendered as SO_x, CO, and PM₁₀ offsets between 1.0 to 1.0 and 1.2 to 1.0 is creditable.
- **Surplus Reductions Resulting from Orphan Shutdown of Major and Minor Sources**
When permitted equipment operating at a major source is shutdown it results in creditable emission reductions. If these reductions are not used internally by the source or banked as an ERC, they are creditable to SCAQMD's tracking system. Similarly, when permitted equipment operating at a minor source is shutdown it results in creditable emission reductions. If these reductions are not used internally by the source or banked as an ERC, they are creditable to SCAQMD's tracking system. Note that the TSD does not differentiate between major sources and minor sources with regard to orphan shutdowns, but simply states that "emission reductions obtained from orphaned shutdowns" are creditable (page 17).
- **Zero BACT Threshold**
Rule 1303 requires that all new and modified sources resulting in an emission increase apply BACT (federal LAER), but the CAA only applies this requirement to major sources. That is, SCAQMD requires BACT (federal LEAR) on all sources (no matter how small) with any increase in emissions (no matter how small). This is distinct from SCAQMD's application of BARCT requirements to minor sources (which makes SCAQMD eligible for a 1.2 to 1.0 offset ratio for ozone precursors rather than a 1.5 to 1.0 offset ratio). Therefore, SCAQMD staff believes that the emission reductions resulting from applying BACT (federal LEAR) to minor sources are creditable. However, as part of this proposal, SCAQMD is not requesting to use such credits and understands that when and if SCAQMD wants to use such credits it will be necessary to hold further discussions with EPA.
- **Discounting Newly-Banked ERCs to BACT**
Rule 1309 – Emission Reduction Credits and Short Term Credits specifies that the amount of emission reductions banked as a new ERC not be "greater than the

equipment would have achieved if operating with current Best Available Control Technology (BACT).” No similar requirement exists in the CAA. Therefore, the amount of any otherwise qualifying emission reductions not issued as an ERC due to implementation of this provision are surplus. However, SCAQMD uses the BACT discount at time of use in lieu of the federally-required BARCT discount at time of use. Therefore, EPA has stated that SCAQMD cannot take credit into its offset accounts for the BACT discount of ERCs because doing so would constitute a form of double counting. On the other hand, the TSD specifically identifies “Best Available Control Technology discounting (Rule 1306(c)) of emission reduction credits generated”³ as an approved source of emission reductions for the tracking system. Therefore, SCAQMD’s position is that BACT discount of ERCs should be creditable from 1990 through 2004 (when EPA made SCAQMD aware of EPA’s new position regarding this source of credits), but should not be creditable in the post-2004 timeframe. Nevertheless, in the interest of reaching consensus with EPA and proceeding with the approval processes for the 2001 and 2002 amendments to Regulation XIII, SCAQMD agrees to retroactively remove all credits generated from BACT discount of ERCs from its tracking system, except such credits which SCAQMD has demonstrated (or demonstrates in the future) exceed the discount that would be required by approved SIP rules and rules scheduled to be approved by SCAQMD in the following year’s rule cycle⁴. SCAQMD shall notify EPA when making this alternative discount. Specifically, SCAQMD has identified 6.67 tons of CO per day of BACT discount of ERC credits from 1991 in SCAQMD’s offset account which are beyond approved SIP rules and rules scheduled to be approved by SCAQMD in the following year’s rule cycle at the time of use⁵. SCAQMD will, therefore, retain these offsets (which were used in the early 1990s).

³ Page 17.

⁴ SCAQMD does not anticipate frequent use of BACT discount of ERCs based on demonstrations of reductions beyond approved SIP rules and rules scheduled for the following year’s rule cycle—in fact it is currently only seeking to use one project out of many hundreds of projects in the last fifteen years to generate BACT discount credits for AQMD’s offset accounts. However, it is conceivable that ERCs can be issued for the shutdown of a source where the BACT discount at the time of generation is beyond approved SIP rules and rules scheduled for the following year’s rule cycle. In such cases, because the BACT discount at the time of generation is used as a surrogate to the federally-required discount at time of use, it is appropriate to credit the difference between the BACT discount and the time of use discount to our offset accounts. The determination that the BACT discount is beyond approved SIP rules and rules scheduled for the following year’s rule cycle at the time of use will be based on a first in/first out analysis to determine when the resulting credits are used—if they continue to be surplus at that time then they are creditable.

⁵ The 6.67 tons of CO per day that SCAQMD has claimed as BACT discount credits which were beyond approved SIP rules and rules scheduled for the following year’s rule cycle at the time of use resulted from the shutdown of internal combustion engines (ICEs). In particular, Southern California Edison (SCE) arranged for various operators to remove their ICEs from service in 1991 as a means of mitigating the then-proposed merger between SCE and San Diego Gas and Electric. However, the PUC denied the merger request, so SCE applied for ERCs for the shutdown engines. According to the first in/first out analysis on the resulting BACT discount CO credits, the credits were completely used by the 1997-98 reporting period. The rule limit for CO emissions from ICEs was 2,000 ppm during the 1991 through 1998 timeframe and all of the subject ICEs were in compliance with this limit prior to being removed from service. BACT for CO emissions from ICEs was 250 ppm during the same timeframe. Furthermore, there were not only no approved SIP rules and no rules scheduled for adoption in the following year’s rule cycle, but there were even no control measures in SCAQMD’s Air Quality

Pre-1990 Credits

Pre-1990 Permitting Program

SCAQMD had a robust stationary source permitting program for both major and minor sources in place well before 1990. Key elements of that program are summarized below:

- **Permit Rules**
Since prior to 1976, the year that SCAQMD adopted its initial NSR rules, virtually any construction or modification of a source has required the operator to obtain a permit to construct from SCAQMD (Rule 201 – Permit to Construct). The only exceptions to these permit requirements are, and at all times were, specified in SCAQMD Rule 219 – Equipment not Requiring a Written Permit Pursuant to Regulation II, which exempts certain equipment from permit requirements due to minimal potential to affect air quality. With the exception of the specific exemptions in Rule 219, there has never been an exemption from permit requirements for sources emitting even relatively small amounts of air contaminants; that is, *all* sources with potential to emit or control air contaminants, including all major and non-major sources, have been required to obtain permits when constructed or modified unless specifically exempted by Rule 219.
- **New Source Review Rules**
SCAQMD adopted its initial New Source Review rules in October, 1976 even prior to the adoption of the New Source Review requirements into the CAA. Originally included in Rule 213 – Standards for Permits to Construct: Air Quality Impact, the NSR rules were moved into a series of rules in Regulation XIII – New Source Review in 1979. The rules required offsetting of emissions increases that exceeded certain thresholds. The thresholds were decreased over time pursuant to rule amendments. For example, for volatile organic compounds and nitrogen oxides, the offset threshold initially was 250 pounds per day, and was reduced by rule amendments during the 1980's to 150 pounds per day, 75 pounds per day, 30 pounds VOC per day and 40 pounds NOx per day, and finally down to zero, requiring no net increase in emissions, unless specifically exempt from offset requirements pursuant to NSR rules.
- **NSR Balance**
Prior to 1990, in order to implement the offset requirements, SCAQMD kept a running “NSR balance” for each facility with permitted sources. The NSR balance included an entry for every increase and every decrease in emissions at the facility that resulted from a permit action. The entries in the NSR balance were *maximum allowable* emissions, *i.e.* the maximum amount of emissions that a source could emit given its physical capabilities and permit limitations and rule requirements. However, the NSR balance was initially determined for each piece of equipment

Management Plan seeking CO emission reductions from ICEs during that timeframe. Therefore, the 1991 BACT discount of the resulting ERCs was available for credit to SCAQMD's offset accounts at the time of use (1998 and earlier).

which had not previously undergone NSR analysis (*i.e.*, pre-NSR equipment) from an *actual* emissions baseline for that equipment. Any subsequent NSR activity for such equipment was conducted on a potential-to-potential basis. Therefore, a pre-NSR source modified under NSR would be subject to NSR on an actual-to-potential basis (*i.e.*, actual pre-modification emissions to potential post-modification emissions)—a very conservative approach.

Prior to 1990, emissions offsets were required when a permit was sought for construction of a new source, or for modification of an existing source, that would cause the sum of increases and decreases at a facility (*i.e.* the NSR balance) to exceed the pre-1990 offset threshold levels.

NSR balance entries had to be quantifiable and enforceable. Such entries only occurred pursuant to permit applications with sufficient substantiating data to ensure quantifiability, after evaluation by SCAQMD engineers and review by multiple supervisory staff pursuant to Regulation XIII rules and implementing policies established by the agency, and upon issuance of permits or permit modifications which were enforceable under state law.

SCAQMD applied substantial resources to implementing these rules. For example, from 1985 through 1989 SCAQMD's engineering staff which processed permits consisted of between 97 and 175 professional engineers and supervisory and management staff. In sum, at all times including, but not limited to, prior to 1990, SCAQMD has had a robust air quality permitting system—a system which we believe was qualitatively superior in terms of quantification and reliability to any other NSR permitting system in the nation.

- Compliance with Federal NSR Requirements

In addition to being reliable, the above-described pre-1990 SCAQMD NSR rules fully complied with all federal requirements. Indeed, SCAQMD's NSR rules were more stringent than required by federal law in the following important respects: (1) offset thresholds were lower than required by federal law and a 1.2 to 1.0 offset ratio was used for all sources; (2) unlike federal requirements which allowed "bubbling" or netting out of BACT, SCAQMD's BACT requirement (equivalent to LAER) applied to any emissions increase from an individual piece of equipment; *i.e.*, there was no netting out of LAER; (3) offset ratios for SO_x, CO, and PM₁₀ were greater than 1 to 1 (*i.e.*, were at 1.2 to 1); (4) SCAQMD had a zero BACT threshold; and (5) the fact that the NSR balance was initially based upon an actual emissions baseline ensured that any increase in potential emissions that exceeded the actual emissions baseline resulted in total potential emissions in excess of the offset threshold amount (which, again, was more restrictive than federally required) would be subject to NSR requirements. Additionally, EPA SIP-approved SCAQMD's Rule 201 as amended January 5, 1990, and SCAQMD's NSR rules as adopted or amended on the dates identified in Table 2.

Table 2
SIP-Approved Revisions of SCAQMD's NSR Rules

Rule	SCAQMD Adoption Date(s)
213	10/8/1976 (Rescinded by SCAQMD 6/28/1990)
1300	(Rescinded by SCAQMD 6/28/1990)
1301	12/7/1995
1302	12/7/1995, 6/13/1997
1303	5/10/1996
1304	6/14/1996
1305	4/6/1984 (Rescinded by SCAQMD 6/28/1990)
1306	6/14/1996
1307	(Rescinded by SCAQMD 6/28/1990)
1308	10/5/1979 or 3/7/1980 or 4/4/1980 or 7/11/1980 (Rescinded by SCAQMD 6/28/1990)
1309	12/7/1995
1309.1	12/7/1995 (2001 and 2002 Amendments Pending SIP Approval)
1309.2	(Pending SIP Approval)
1310	12/7/1995
1311	10/5/1979 (Rescinded by SCAQMD 6/28/1990)
1312	(Rescinded by SCAQMD 6/28/1990)
1313	12/7/1995

▪ **Negative Balances**

By 1990, some facilities had negative NSR balances. These negative balances were the result of equipment shutdowns or process changes since October 1976 which resulted in reductions in emissions from a source. The majority of negative balances resulted from equipment shutdowns. Like all entries in the NSR balance, negative balances only occurred pursuant to permit actions—*i.e.* either modification of a SCAQMD permit or use of reductions for mitigations. Negative balances were quantified by SCAQMD engineers based upon the physical capabilities of the modified or shut down equipment and applicable permit requirements.

Existing Pre-1990 Accounting

SCAQMD's offset accounts were established with starting balances based on pre-1990 emissions reductions. The primary source of these pre-1990 reductions was a portion of facilities' negative NSR balances which were discounted as specified in the 1990 amendments to Regulation XIII (described below). The 1990 Regulation XIII amendments also directed the Executive Officer to recall all existing pre-1990 ERCs which had resulted from shutdowns, discount them by eighty percent, and issue new ERCs at twenty percent of their original values. The eighty percent discount of the pre-1990 shutdown ERCs was deposited into SCAQMD's offset accounts along with the amounts derived from the discount of pre-1990 negative balances (further explanation of the implementation of the 1990 amendments to Regulation XIII is provided with the discussion of SCAQMD's proposed revisions to its pre-1990 accounting). **All of SCAQMD's annual status reports prepared to date have included the starting**

balances from these sources (discount of pre-1990 negative balances and pre-1990 shutdown ERCs); SCAQMD has not taken credit for any other pre-1990 sources of credits, such as the zero BACT threshold, use of ERCs by minor sources, or the additional 20 % of ERCs provided by major sources for SO_x, CO, and PM₁₀ at a ratio of 1.2 to 1.0 compared to 1.0 to 1.0.

Proposed Adjustments to Pre-1990 Accounting

SCAQMD is now proposing to significantly reduce (by more than 60 % overall) its pre-1990 emission credits by eliminating any present or past use of any credits for which SCAQMD presently has no records and cannot re-verify the validity of such credits and to only utilize the portion of the previously-reported pre-1990 emission reductions which has been originally validated in 1990/91 and revalidated in 2004/05 as credits in its tracking system and for which SCAQMD has all or some records. Most of such NO_x reductions (almost 2/3) and all of such CO and PM₁₀ reductions were utilized as offsets in SCAQMD's tracking system during the 1990's; however, some of the pre-1990 NO_x reductions and a significant portion of the pre-1990 VOC and SO_x reductions remain in SCAQMD's offset account. The emission reductions that underlie those credits occurred between 15 and 29 years ago, and not all records related to them are available today. In many cases, however, summary data based on previous analyses are available. While not all records are available, SCAQMD at all relevant times prior to and after 1990 had a sufficiently robust permitting program and record validation procedure to provide confidence regarding the validated emission reductions for which SCAQMD proposes to take pre-1990 credits. This conclusion is supported by the preceding discussion of SCAQMD's pre-1990 permitting program and the following summary of the 1990 Regulation XIII amendments and their implementation:

- **1990 Regulation XIII Amendments**
SCAQMD substantially modified Regulation XIII in 1990. The offset threshold was dropped to zero, although relatively small emitting facilities (*e.g.* less than 30 pounds per day of VOC or 40 pounds per day of NO_x) were eligible to obtain needed credits from a new "Community Bank." Under the 1990 amendments, negative balances were to be "verified by the Executive Officer" and discounted by 80%. The rules specified that "upon validation" the remaining amount was to be issued to the permit holder in the form of an ERC (Rule 1309(a)).
- **Implementation of 1990 Amendments**
Shortly after adoption of the 1990 amendments to Regulation XIII, SCAQMD staff drafted a detailed internal guidance document titled "Regulation XIII – New Source Review Guidance Manual" (copy provided in Attachment 3) specifying how the amendments would be implemented by agency permit processing engineers. (*Section 1, Regulation XIII Transition*). The required treatment of negative balances was described on pages 40 to 48 and page 68 of this document. The transition document specified that negative balances would have to be "verified" in accordance with standard procedures. Page 68, titled "NSR Database Validation," specified that each facility's NSR account would be searched by computer to determine if any "forgivenesses" (*i.e.* negative entries due to prior rule amendments lowering offset

thresholds) contributed to the facility's negative balance. The document further provided that NSR balances "shall be recalculated" since these forgivenesses were not "real" emission reductions and therefore did not qualify for an ERC pursuant to Rule 1309(b)(1) (p.40). The transition document also specified that any negative particulate matter emissions balances would be converted to PM10 by multiplying the particulate matter emissions by an average factor of 0.5 (p.40). Finally, the document stated that any facility with a negative balance of 500 pounds per day or greater was to have each negative entry "confirmed by reviewing the application file which resulted in the negative NSR entry" (p. 68). The vast majority of negative balances at the time (in excess of 80%) were associated with facilities with negative balances exceeding 500 pounds.

In 1991, SCAQMD's engineering staff commenced the verification and validation processes described in the transition document. The result of these processes was a substantial reduction in the amount of the negative balances for some pollutants, even prior to the 80% discount. These reductions were the result of (1) addressing the "forgivenesses," (2) determinations that some reductions were required by SCAQMD rules and thus ineligible for ERCs, and (3) in some cases simple data entry errors. Table 3 presents the 80 % portion of the 1990 negative balances that were deposited in SCAQMD's offset accounts. The larger amount shown for each pollutant is the amount originally deposited as the result of this process in the early 1990s and which has been previously reported as the 1990 starting balance in the annual NSR status reports and the lower amount is revised based upon recent (2003) re-validation of these numbers by SCAQMD staff based on records that are still available to address EPA's comments and consistent with EPA policy guidance which allows use of pre-1990 credits that are explicitly included and quantified as growth in the SIP. Such guidance provides that the permitting agency must maintain information including, at a minimum, the name of the source that generated the credit, the source category, credit quantity, specific action that generated the credit, date the credit was generated and "enough other information to determine the creditability" (Memorandum from John Seitz to David Howekamp August 26, 1994).

Table 3
Pre-1990 Credits Deposited in SCAQMD's Offset Accounts
Tons per Day

	VOC	NOx	SOx	CO	PM10	Overall
Previously-Reported Pre-1990 Credits	92.4	25.8	18.4	34.9	34.5	206
Revised Pre-1990 Credits Verified with Records or Validation Procedures	38.46	23.92	8.04	8.45	2.67	81.5
Percent Reduction in Pre-1990 Credits	58 %	7 %	56 %	76 %	92 %	60 %

Records for pre-1990 emission credits are from 15 to 29 years old. SCAQMD staff recently conducted an extensive review of the pre-1990 credits and determined that

the types of records available today include printouts of NSR data captured in SCAQMD's permitting database at the time of permit issuance and complete engineering files, which include the materials and documentation submitted by the applicant and SCAQMD's engineering evaluation (refer to Attachment 4 for examples of available pre-1990 NSR data).

In this proposal, SCAQMD is proposing to only use the revised and verified pre-1990 credits (as set forth in Table 3). There are pre-1990 credits which can reasonably be concluded to be creditable based on presently available records. In some cases, such conclusion can be reached because all of the information described in the 1994 Seitz memorandum is currently available. In other cases, all of such information is not currently available, but the above-described permitting procedures provide "enough other information to determine the creditability" However, for the majority of the pre-1990 emission reduction credits (more than 60 % overall), the SCAQMD cannot substantiate the validity of the records based on the available records. SCAQMD is now proposing to significantly reduce its pre-1990 emission reduction credits by eliminating any past or present use of any credits for which SCAQMD presently cannot substantiate the validity of such records.

- **Remaining Pre-1990 Credits**

SCAQMD's NSR tracking system has not previously specified the age of credits held in SCAQMD's offset accounts. However, in response to EPA's comments about the use of pre-1990 credits, staff has completed a "First In/First Out" analysis of these accounts. This analysis shows that significant portions of the pre-1990 VOC and SO_x credits remain in SCAQMD's accounts, about one quarter of the pre-1990 NO_x credits remained in SCAQMD's accounts as of July 2002, and all of the pre-1990 CO and PM₁₀ credits were depleted by 1997⁶. In order to address EPA's comment regarding continued use of pre-1990 credits from SCAQMD's accounts, SCAQMD proposes to eliminate any unused pre-1990 VOC, NO_x, and SO_x credits remaining in its account at the end of the 2004-2005 reporting period and not use any pre-1990 credits in its accounts post 2005.

- **Other Potential Credits**

SCAQMD is not proposing to take any credits for pre-1990 sources of credits such as the zero BACT threshold, use of ERCs by minor sources, the additional 20% of ERCs provided by major sources of SO_x, CO, and PM₁₀ at a ratio of 1.2 to 1.0 compared to 1.0 to 1.0.

⁶ All data for 1991 to 1997 is aggregated, so it is uncertain when in this time period the 1990 starting account balances for CO, and PM₁₀ were depleted. However, by assuming that these credits were consumed at an approximately constant rate, it is estimated that PM₁₀ was depleted in 1994, and CO was depleted in 1995.

1990-2005 Credits

Existing 1990-2005 Accounting

SCAQMD's NSR tracking system currently takes credit for orphan shutdowns from major sources but not from minor sources. The existing tracking system credits orphan shutdowns to SCAQMD's offset accounts based upon the allowable permitted level of emissions of the shutdown source, and no further discount/adjustment is applied to the credits to specifically account for surplus at the time of use. It also does not take credit for surplus reductions of SO_x, CO, or PM₁₀ provided as ERCs by major sources as a result of the differences in federal and local offset requirements for these pollutants (local requirement is 1.2 to 1.0 while federal law does not specify an offset ratio in excess of 1.0 to 1.0 for SO_x, CO, or PM₁₀) or for surplus reductions resulting from minor sources providing ERCs as emission offsets. The tracking system also does not take credit for SCAQMD's zero BACT threshold. BACT discounts applied to newly-banked ERCs are credited to SCAQMD's offset accounts. Offsets are debited from SCAQMD's accounts at 1.2 to 1.0 for all five pollutants when major sources that are not exempt pursuant to the CAA are permitted using Rule 1304 exemptions or the Priority Reserve, including replacement of ODCs with VOC.

Proposed Adjustments to 1990-2005 Accounting

The proposed changes to the sources of credits to and debits from SCAQMD's offset accounts for the 1990-2005 time period are summarized below:

- **Minor Source Orphan Shutdowns**
The NSR tracking system has only used "orphan" shutdowns of major sources post-1990 to fund SCAQMD's offset accounts. However, shutdowns of permitted *minor* sources also can meet the federal requirements that credits be real, permanent, enforceable, quantifiable, and surplus in the same way as do major source shutdowns. ERCs generated from minor sources are commonly used to fulfill the offset requirements for emission increases at major sources which are not exempt from offset requirements under SCAQMD's NSR rules. Therefore, although SCAQMD has not previously used these credits due to the large balances available in its offset accounts, it is appropriate to include emission reductions from minor source orphan shutdowns as credits in SCAQMD's offset accounts.

SCAQMD's Rule 201 requires written authorization from the Executive Officer (*i.e.*, a permit to construct) before a person may build, erect, install, alter or replace any equipment, the use of which may cause the issuance of air contaminants or the use of which may eliminate, reduce or control the issuance of air contaminants. Rule 203 – Permit to Operate similarly prevents the operation or use of such equipment without a permit issued by the Executive Officer. The only exceptions to these requirements are specifically identified in Rule 219. However, all of the minor sources which SCAQMD proposes to use as sources of orphan shutdown credits as described above have been through the permitting process. In fact, such minor sources are subject to

the same Regulation IV - Prohibitions, Regulation XI - Source Specific Standards, and Regulation XIII rule requirements as are major sources. In some cases the operators of these sources go through the necessary steps to quantify and generate ERCs when they experience real, permanent, enforceable, quantifiable, surplus emission reductions (*e.g.*, equipment or facility shutdown or modification). Such minor source ERCs are fully valid and eligible for use as major source offsets. Therefore, in cases where the operators do not go through the steps to generate ERCs from their emission reductions, it is appropriate for SCAQMD to treat these orphan shutdowns in the same manner as it does orphan shutdowns at major sources.

- **Major Source Use of SO_x, CO, and PM₁₀ ERCs**
The tracking system will be updated to include credit for the 20 % additional SO_x, CO, and PM₁₀ ERCs provided by major sources as emission offsets at a ratio of 1.2 to 1.0 pursuant to Rule 1303 rather 1.0 to 1.0. The 20 % above a 1.0 to 1.0 offset ratio is creditable because the CAA only requires a 1.2 to 1.0 offset ratio for precursors to ozone; the required offset ratio for SO_x, CO, and PM₁₀ pursuant to the CAA and the TSD is “at least 1 to 1” (TSD, pages 14 and 15).
- **Offset Ratio for Exempt Major Sources of SO_x, CO, and PM₁₀**
SCAQMD proposes to change the offset ratio for major sources of SO_x, CO, and PM₁₀ offset from SCAQMD’s offset accounts from 1.2 to 1.0 to 1.0 to 1.0. This change is consistent with the CAA and the TSD, which only require a 1.2 to 1.0 offset ratio to precursors of ozone.
- **ERCs Provided by Minor Sources to Offset Emission Increases**
The CAA does not require minor sources to provide offsets for their emission increases. Therefore, the ERCs that these sources provide to offset their increases pursuant to Rule 1303 are creditable to SCAQMD’s offset accounts.
- **Discounting Newly-Banked ERCs to BACT**
Rule 1309 – Emission Reduction Credits and Short Term Credits specifies that the amount of emission reductions banked as a new ERC not be “greater than the equipment would have achieved if operating with current Best Available Control Technology (BACT).” No similar requirement exists in the CAA. Therefore, the amount of any otherwise qualifying emission reductions not issued as an ERC due to implementation of this provision are surplus. However, SCAQMD uses the BACT discount at time of use in lieu of the federally-required BARCT discount at time of use. Therefore, EPA has stated that SCAQMD cannot take credit into its offset accounts for the BACT discount of ERCs because doing so would constitute a form of double counting. On the other hand, the TSD specifically identifies “Best Available Control Technology discounting (Rule 1306(c)) of emission reduction credits generated”⁷ as an approved source of emission reductions for the tracking system. Therefore, SCAQMD’s position is that BACT discount of ERCs should be creditable from 1990 through 2004 (when EPA made SCAQMD aware of EPA’s new position regarding this source of credits), but should not be creditable in the post-

⁷ Page 17.

2004 timeframe. Nevertheless, in the interest of reaching consensus with EPA and proceeding with the approval processes for the 2001 and 2002 amendments to Regulation XIII, SCAQMD agrees to retroactively remove all credits generated from BACT discount of ERCs from its tracking system, except such credits which SCAQMD has demonstrated (or demonstrates in the future) exceed the discount that would be required by approved SIP rules and rules scheduled to be approved by SCAQMD in the following year's rule cycle. SCAQMD shall notify EPA when making this alternative discount. Specifically, SCAQMD has identified 6.67 tons of CO per day of BACT discount of ERC credits from 1991 in SCAQMD's offset account which are beyond approved SIP rules and rules scheduled to be approved by SCAQMD in the following year's rule cycle at the time of use. SCAQMD will, therefore, retain these offsets (which were used in the early 1990s).

Inventory Issues Related to Minor Source Orphan Shutdowns

Emissions from small permitted sources (*i.e.*, less than 4 tpy of any criteria pollutant or 100 tpy of CO) are treated as area sources in the AQMP inventory. A detailed description of the area source inventory methodology for each source category tracked in the AQMP is provided in Attachment 5. Typically, a base year inventory is prepared based on the historical activity data and projected to future years based on the socioeconomic data provided by SCAG. The surrogates used for emission growth projection are documented in Appendix III, Table 2-3 of the 2003 AQMP. The growth factors for source categories are mostly greater than 1 with a few exceptions. When the growth factor is greater than 1, emissions are projected to grow without taking into account any potential NSR constraint that offsets may not be available. By the same token, if the growth factor is less than 1, future emissions are estimated to be lower than the base year emissions.

EPA staff raised an issue that shutdown credits from source categories that are projected to decrease in the AQMP may not be appropriate to be used as offsets, since the AQMP has already reflected such decrease. This position suggests the potential for double counting in such situations. However, closer examination of the AQMP process and the assumptions made in the Plan reveals that use of shutdown credits from source categories with even negative projected growth does not result in double counting of emissions reductions. The AQMP assumes negative growth in some categories and positive growth in others. Further, the positive growth assumptions include no constraints on growth posed by cost or availability of emission offsets (and existing ERCs are also assumed to be "in the air" independent of the growth projections). Inherent in these AQMP assumptions is the assumption that emission decreases, including decreases associated with negative growth, result in emission credits that can be used to offset emission increases. Therefore, movement of potential emissions from a negative growth category to a positive growth category via appropriately quantified and discounted credits is entirely consistent with the AQMP and its assumptions. Furthermore, even though SCAQMD has never experienced actual growth greater than that projected in the AQMP, SCAQMD reevaluates the AQMP with each AQMP revision and makes appropriate changes and corrections as a part of this process (and commits to continue to do so consistent with state law). Finally, there is no restriction on the generation of ERCs by

sources in categories with negative projected growth or on the use of such ERCs by sources within other categories. The standard for credits in SCAQMD's accounts should not be higher than for privately held credits.

Other Potential Credits

SCAQMD is not proposing to take any credits for 1990-2005 sources of credits such as the zero BACT threshold or application of LAER in excess of federal requirements at this time. SCAQMD understands that, if it decides to pursue these sources of excess reductions in the future, further discussion with EPA will be required.

Post-2005 Credits

Existing Post-2005 Accounting

SCAQMD's tracking system currently takes credit for orphan shutdowns from major sources but not from minor sources. It also does not take credit for surplus reductions of SO_x, CO, or PM₁₀ provided as ERCs by major sources as a result of the differences in federal and local offset requirements for these pollutants (the local requirement is 1.2 to 1.0 while federal law does not specify an offset ratio in excess of 1.0 to 1.0 for SO_x, CO, or PM₁₀) or for surplus reductions resulting from minor sources providing ERCs as emission offsets. The tracking system also does not take credit for SCAQMD's zero BACT threshold. Pre-1990 credits remaining in SCAQMD's offset accounts continue to be usable in the tracking system. BACT discounts applied to newly-banked ERCs are credited to SCAQMD's offset accounts. The existing tracking system credits orphan shutdowns to SCAQMD's offset accounts based upon the allowable permitted level of emissions of the shutdown source, and no further discount/adjustment is applied to the credits to specifically account for surplus at the time of use. SCAQMD's portion of the California SIP does not include assumptions reflecting the NSR tracking system or commitments to make up any shortfall in SCAQMD's offset accounts. Additionally, the tracking system does not take credit for surplus reductions resulting from modifications at major sources that do not constitute "major modifications" pursuant to the new NSR Reform Regulations. Credits are withdrawn from SCAQMD's accounts at 1.2 to 1.0 for all five pollutants when major sources that are not exempt pursuant to the CAA are permitted using Rule 1304 exemptions or Rule 1309.1 offsets, including replacement of ODCs with VOC.

Proposed Post-2005 Accounting

The proposed changes to the sources of credits to and debits from SCAQMD's offset accounts for the post-2005 time period are summarized below:

- **Minor Source Orphan Shutdowns**
The tracking system will be updated to include credit for future (post-2005) minor

source orphan shutdowns adjusted to 80% of potential emissions to represent actual emissions, as described above for the 1990 to 2005 time period.

- **Minor Source Use of ERCs**
The tracking system will be updated to include credit for future ERCs provided by minor sources as emission offsets pursuant to Rule 1303 because such offsets are not required pursuant to the CAA.
- **Major Source Use of SO_x, CO, and PM₁₀ ERCs**
The tracking system will be updated to include credit for the 20 % additional SO_x, CO, and PM₁₀ ERCs provided by major sources as emission offsets at a ratio of 1.2 to 1.0 rather than 1.0 to 1.0 pursuant to Rule 1303. The 20 % above a 1.0 to 1.0 offset ratio is creditable because the CAA only requires a 1.2 to 1.0 offset ratio for precursors to ozone; the required offset ratio for SO_x, CO, and PM₁₀ pursuant to the CAA and the TSD is “at least 1 to 1” (TSD, pages 14 and 15).
- **Pre-1990 Credits in SCAQMD’s Offset Accounts**
Eliminate any future use of any remaining pre-1990 credits, even though records were re-verified by SCAQMD in 2004-05, in its offset accounts which remain unused at the end of the 2004-2005 reporting period rather than use them to offset future emission reductions.
- **BACT Discount of ERCs**
EPA has raised an issue about the use of the amount of BACT discounts from ERCs issued by SCAQMD as credits in SCAQMD’s offset accounts. Although SCAQMD believes that this provision was specifically approved by EPA to be used as credits in the TSD (page 17), in order to resolve the outstanding issues raised by EPA, SCAQMD proposes to no longer take any credits for BACT discount of ERCs in SCAQMD’s offset accounts except such credits which SCAQMD specifically demonstrates are beyond approved SIP rules and rules scheduled to be approved by SCAQMD in the following year’s rule cycle at the time of use.
- **Surplus Discount at Time of Use**
Credits in SCAQMD’s accounts that resulted from post-1990 orphan shutdowns and which, based on a first-in/first-out analysis, are not used in the same timeframe they are banked are proposed to be subject to a BARCT at the time of use adjustment. This will be accomplished based on rule control requirements that become effective each year. Specifically, SCAQMD is proposing that each year all credits in SCAQMD’s offset accounts carried over from the previous year be discounted by the amount of the percentage reduction in overall permitted emissions⁸ projected to be achieved as a result of implementation of control requirements that become effective during the year for the pollutant in question. This analysis will be performed on an aggregate basis each year for credits carried over from the previous year.

⁸ Permitted emissions data is derived primarily from permitted facilities emitting more than four tons of VOC, NO_x, SO_x, or PM per year or more than 100 tons of CO per year.

- Actual Emissions Baseline

It is not feasible for SCAQMD to discount orphan shutdown credits to actual emissions because the actual emission data generally are unavailable. Therefore, staff proposes to use an average discount factor to account for the difference between potential and actual emissions. Since 1997, SCAQMD has used a twenty percent discount to convert potential emissions to estimated actual emissions for purposes of compliance with state “no net increase” requirements. This procedure has been used with concurrence of the California Air Resources Board. We propose to use the same factor for federal NSR tracking purposes. In light of the methodology used to quantify potential emissions (explained in more detail below), staff’s engineering judgment indicates that, on average, a twenty percent reduction from potential emissions is a reasonable estimate of actual emissions. Actual emissions for individual sources will range from the sources’ potential emissions down to less than eighty percent of potential emissions, but eighty percent of potential emissions represents an acceptable estimate of aggregate actual emissions. The use of eighty percent of potential emissions as a surrogate for actual emissions is well documented in SCAQMD’s annual status reports regarding Regulation XIII. The most recent three such reports are included in Attachment 6 (for example, refer to Table 7—“Debits from AQMD’s State Offset Accounts”—in each of these reports).

Facilities with potential to emit in excess of the Rule 1304 exemption thresholds (4 tons per year for VOC, NO_x, SO_x, and PM₁₀ and 29 tons per year for CO), provide ERCs to offset their increases in potential emissions so they have a strong incentive to keep their potential emissions in line with actual emissions at times of high production. Smaller facilities with potential to emit below the exemption thresholds may be inclined to request permits based potential emissions at the exemption threshold levels because the offsets are provided by SCAQMD at no cost to the facility. However, SCAQMD engineers perform a thorough evaluation of each permit application prior to recommending issuance of a permit to construct or a permit to operate. These evaluations include a determination of the actual controlled emission rate (based on source test results, VOC content of coatings, or sulfur content of fuel, for example) or expected actual controlled emission rate (based on established emission factors or manufacturers’ guarantees, for example). This data is then combined with the maximum anticipated production rate to determine the equipment’s potential to emit. Note that the maximum production rate used in these calculations is based on what is reasonably expected for the facility and source in question during periods of high production and is not based on either “24-7” operations (except for those facilities that actually do operate in such a manner) or an artificially highest permissible emission level for each source. Therefore, actual emissions are not expected to be considerably different than potential emissions and 80 % of potential emissions provides a reasonable estimate of actual emissions. This conclusion is further supported by potential to emit data for facilities at or below the exemption thresholds. Table 4 shows that there are far more facilities with potentials to emit below the exemption thresholds than at the exemption thresholds.

Table 4
Ratio of Numbers of Facilities with Potential to Emit (PTE) Below Exemptions
Thresholds to Numbers of Facilities with PTE at Exemption Thresholds

Pollutant	Facility Count			Ratio (Below Threshold: At Threshold)
	PTE Range A ¹	PTE Range B ²	PTE C ³	
VOC	1,336	1,348	601	4.5:1
NOx	2,021	1,534	363	10:1
SOx	545	180	32	23:1
CO	2,789	330	10	310:1
PM10	1,686	940	188	14:1

¹ PTE Range A is greater than zero but less than 2 tons per year for VOC, NOx, SOx, and PM10 and is greater than zero but less than 15 tons per year for CO.

² PTE Range B is greater than or equal to two but less than four tons per year for VOC, NOx, SOx, and PM10 and is greater than 15 but less than 29 tons per year for CO.

³ PTE C is four tons per year for VOC, NOx, SOx, and PM10 and is 29 tons per year for CO.

- **Offset Ratio for Exempt Major Sources of SOx, CO, and PM10**
 SCAQMD will provide offsets to major sources of SOx, CO, and PM10 which are exempt from offset requirements pursuant to Rule 1304 or which receive Rule 1309.1 offsets but which are not exempt from offset requirements pursuant to the CAA at a ratio of 1.0 to 1.0, rather than 1.2 to 1.0.
- **SIP Inventory and Growth Assumptions**
 To date, the SCAQMD has incorporated a sufficient portion of available tracking system credits into the AQMP at the time of plan revision to assure that the growth assumptions in the plan are consistent with NSR credits used. In order to assure that the SIP assumes that all necessary credits are “in the air,” the SCAQMD proposes to provide EPA an enforceable commitment to make up any shortfall in the amount of credits assumed to be “in the air” at the time of the next triennial plan revision required by state law.
- **Other Potential Credits**
 SCAQMD is not proposing to take any credits for post-2005 sources of credits such as application of LAER in excess of federal requirements⁹ to any increase in emissions at a major stationary source for non-ozone precursors such as SOx, CO and PM10 or the zero BACT threshold. In this proposal SCAQMD is not requesting to use such credits and understands that when and if SCAQMD wants to use such credits it will be necessary to hold further discussions with EPA. SCAQMD is also not presently proposing to take any benefits for not having to deduct emission increases resulting from modifications at major sources that do not constitute major modifications pursuant to the NSR Reform Regulations at this time. However, SCAQMD would like to be able to use such provisions if a project can be

demonstrated to not be subject to NSR since it is not a “federal major modification” under NSR reform. SCAQMD is also currently investing funds resulting from the mitigation fees provided by electrical generating facilities pursuant to Rule 1309.1 – Priority Reserve in various emission reduction projects. Therefore, SCAQMD may discuss mechanisms for taking credit for such emission reductions with EPA in the future.

Summary

SCAQMD believes that the proposed revisions to the NSR credit tracking procedures represent a very conservative proposal in an effort to address EPA’s questions related to credits used for Priority Reserve, Offset Budget, and NSR equivalency purposes. As indicated earlier, the proposed revisions will reduce SCAQMD’s previously-reported pre-1990 credits from a 7 % reduction in NOx to a 92 % reduction in PM10 and will change the previously-reported 2002 NSR federal offset account from a 40 % actual increase in NOx credits to an 83 % reduction in PM10 credits. The overall impact on emission credits resulting from the proposals described above are summarized in Table 5 for both the 1990 starting balance and July 2002 running balance.

Table 5
Summary of SCAQMD’s Offsets Account
Tons per Day

	VOC	NOx	SOx	CO	PM10
Previously-Reported 1990 Starting Balance	92.4	25.8	18.4	34.9	34.5
Final Proposed Revised 1990 Starting Balance	38.46	23.92	8.04	8.45	2.67
Reductions in SCAQMD’s Pre-1990 NSR Federal Account Balances	58 %	7 %	56 %	76 %	92 %
Previously-Reported 2002 Running Balance	107.65	21.60	18.76	24.09	41.24
Final Proposed Revised 2002 Running Balance	70.60	30.16	10.56	7.89	6.92
Reductions in SCAQMD’s 2002 NSR Federal Account Balances	34.4 %	-39.6 %	43.7 %	67.2 %	83.2 %

In addition, SCAQMD’s proposed post-2005 emission credits adjustments, as described above, will address all of the issues raised by EPA prospectively.

Table 6 summarizes the changes between SCAQMD’s existing and proposed revised NSR tracking systems. This table summarizes the existing and proposed revised NSR tracking system for pre-1990, 1990-2005, and post-2005 emission reductions.

Table 6
Summary of Changes between SCAQMD'S Existing and
Proposed Revised NSR Tracking Systems

Pre-1990 Emission Reductions

SCAQMD's Existing NSR Offset Account and Tracking System	SCAQMD's Proposed Revised NSR Offset Account and Tracking System
<ul style="list-style-type: none"> Starting Balance based on data generated in 1990 from facilities' (both major and minor sources) emission reductions recorded as negative NSR balances. This data has been used and previously reported in all annual NSR status reports. 	<ul style="list-style-type: none"> Initial Starting Balance based on data from facilities' (both major and minor sources) emission reductions recorded as negative NSR balances <u>which were originally verified in 1990/91 and re-verified in 2004/05 and all or some records currently exist.</u>
<ul style="list-style-type: none"> No credit taken for surplus reductions from SOx, CO, and PM10 offsets provided (at 120 %) as ERCs for minor sources⁽¹⁾. 	<ul style="list-style-type: none"> No credit taken for surplus reductions from SOx, CO, and PM10 offsets provided (at 120 %) as ERCs for minor sources⁽¹⁾. (No Change)
<ul style="list-style-type: none"> No credit taken for the 20 % additional SOx, CO, and PM10 offsets (ERCs) for major sources provided at a ratio of 1.2 to 1.0 compared to 1.0 to 1.0⁽²⁾. 	<ul style="list-style-type: none"> No credit taken for the 20 % additional SOx, CO, and PM10 offsets (ERCs) for major sources provided at a ratio of 1.2 to 1.0 compared to 1.0 to 1.0⁽²⁾. (No Change)
<ul style="list-style-type: none"> No credit taken for emission reductions created from the application of zero BACT threshold⁽¹⁾. 	<ul style="list-style-type: none"> No credit taken for emission reductions created from the application of zero BACT threshold at this time⁽¹⁾. (No Change)

⁽¹⁾ EPA's Technical Support Document (TSD) dated 10/24/96 for EPA's Notice of Final Rulemaking (Federal Register 12/4/96) for SIP Approval of SCAQMD NSR Rules allows for such credits, page 17.

⁽²⁾ TSD, pages 14 and 15.

1990-Present (2005) Emission Reductions

SCAQMD's Existing NSR Offset Account and Tracking System	SCAQMD's Proposed Revised NSR Offset Account and Tracking System
<ul style="list-style-type: none"> BACT discount credit portion of newly-issued ERCs eligible for crediting to SCAQMD's offset accounts (as previously approved by EPA)⁽¹⁾. 	<ul style="list-style-type: none"> No BACT-discount credits from newly-issued ERCs will be eligible for crediting to SCAQMD's offset accounts except those for specific projects for which staff has demonstrated or will demonstrate that the BACT discount is beyond approved SIP rules and rules scheduled to be approved by SCAQMD in the following year's rule cycle at the time of use of the credits.
<ul style="list-style-type: none"> No credit taken for orphan shutdowns from minor sources. 	<ul style="list-style-type: none"> Orphan shutdowns include shutdowns of both major and minor sources.

Table 6 continued

1990-Present (2005) Emission Reductions (continued)

SCAQMD's Existing NSR Offset Account and Tracking System	SCAQMD's Proposed Revised NSR Offset Account and Tracking System
<ul style="list-style-type: none"> No further discount/adjustment for orphan shutdowns due to BARCT at time of use. 	<ul style="list-style-type: none"> All orphan shutdowns will be discounted/adjusted to BARCT at time of use by discounting balances "carried over" from one year to the next.
<ul style="list-style-type: none"> No further discount/adjustment applied to estimate actual emissions. 	<ul style="list-style-type: none"> All orphan shutdowns will be discounted/adjusted to further reflect actual emissions.
<ul style="list-style-type: none"> VOC and NOx offsets provided by SCAQMD for federal sources exempted by SCAQMD at a ratio of 1.2 to 1.0. 	<ul style="list-style-type: none"> VOC and NOx offsets provided by SCAQMD for federal sources exempted by SCAQMD at a ratio of 1.2 to 1.0. (No Change)
<ul style="list-style-type: none"> No credit taken for surplus reductions from SOx, CO, and PM10 offsets provided by SCAQMD for federal sources exempted by SCAQMD at a ratio of 1.2 to 1.0 compared to 1.0 to 1.0. 	<ul style="list-style-type: none"> SOx, CO, and PM10 offsets provided by SCAQMD for federal sources exempted by SCAQMD at a ratio of 1.0 to 1.0⁽¹⁾.
<ul style="list-style-type: none"> VOC offsets provided by SCAQMD at a ratio of 1.2 to 1.0 for federal sources exempted by SCAQMD which switch from ozone depleting compounds to VOCs. 	<ul style="list-style-type: none"> VOC offsets provided by SCAQMD at a ratio of 1.2 to 1.0 for federal sources exempted by SCAQMD which switch from ozone depleting compounds to VOCs. (No Change)
<ul style="list-style-type: none"> No credit taken for surplus reductions created from offsets (ERCs) provided (at 120 %) by minor sources which are not exempt from offset requirements under SCAQMD NSR rules (<i>i.e.</i>, > 4 but < 10 TPY of VOCs and NOx, etc.). 	<ul style="list-style-type: none"> Credit taken for surplus reductions created from offsets (ERCs) provided (at 120 %) by minor sources which are not exempt from offsets requirements under SCAQMD rules⁽²⁾ (<i>i.e.</i>, > 4 but < 10 TPY of VOCs and NOx, etc.).
<ul style="list-style-type: none"> No credit taken for surplus reductions created from the 20 % additional SOx, CO, and PM10 offsets (ERCs) provided by major sources at 1.2 to 1.0 ratio compared to 1.0 to 1.0 ratio. 	<ul style="list-style-type: none"> Credit taken for surplus reductions created from the 20 % additional SOx, CO, and PM10 offsets (ERCs) provided by federal major sources at a ratio of 1.2 to 1.0 compared to 1.0 to 1.0 ratio⁽¹⁾.

⁽¹⁾ EPA's Technical Support Document (TSD) dated 10/24/96 for EPA's Notice of Final Rulemaking (Federal Register 12/4/96) for SIP Approval of SCAQMD NSR Rules, pages 14, 15, and 17.

⁽²⁾ TSD, page 17.

Future (Post-2005) Emission Reductions

SCAQMD's Existing NSR Offset Account and Tracking System	SCAQMD's Proposed Revised NSR Offset Account and Tracking System
<ul style="list-style-type: none"> No credit taken for emission reductions created from the application of zero BACT threshold⁽²⁾. Remaining pre-1990 credits still eligible for use. 	<ul style="list-style-type: none"> No credit taken for emission reductions created from the application of zero BACT threshold at this time⁽²⁾. (No Change) No pre-1990 credits will be used post-2005.

Table 6 continued

Future (Post-2005) Emission Reductions (continued)

SCAQMD's Existing NSR Offset Account and Tracking System	SCAQMD's Proposed Revised NSR Offset Account and Tracking System
<ul style="list-style-type: none"> ▪ BACT discount credit portion of newly-issued ERCs eligible for crediting to SCAQMD's offset accounts (as previously approved by EPA)⁽¹⁾. 	<ul style="list-style-type: none"> ▪ No BACT-discount credits from newly-issued ERCs will be eligible for crediting to SCAQMD's offset accounts except those for specific projects for which staff demonstrates that the BACT discount is beyond approved SIP rules and rules scheduled to be approved by SCAQMD in the following year's rule cycle at the time of use of the credits.
<ul style="list-style-type: none"> ▪ Orphan shutdowns credited to SCAQMD's offset accounts in the past only included shutdowns of major sources. 	<ul style="list-style-type: none"> ▪ Post-1990 orphan shutdowns will include shutdown of both major and minor sources.
<ul style="list-style-type: none"> ▪ No further discount/adjustment for orphan shutdowns due to BARCT at time of use. 	<ul style="list-style-type: none"> ▪ All orphan shutdowns will be discounted/adjusted to BARCT at time of use by discounting balances "carried over" from one year to the next.
<ul style="list-style-type: none"> ▪ No further discount/adjustment applied to estimate actual emissions. 	<ul style="list-style-type: none"> ▪ All orphan shutdowns will be discounted/adjusted to reflect estimated actual emissions.
<ul style="list-style-type: none"> ▪ VOC and NOx offsets provided by SCAQMD for federal sources exempted by SCAQMD at a ratio of 1.2 to 1.0. 	<ul style="list-style-type: none"> ▪ VOC and NOx offsets will be provided by SCAQMD for federal sources exempted by SCAQMD at a ratio of 1.2 to 1.0. (No Change)
<ul style="list-style-type: none"> ▪ No credit taken for surplus reductions from SOx, CO, and PM10 offsets provided by SCAQMD for federal sources exempted by SCAQMD at a ratio of 1.2 to 1.0 compared to 1.0 to 1.0. 	<ul style="list-style-type: none"> ▪ SOx, CO, and PM10 offsets will be provided by SCAQMD for federal sources exempted by SCAQMD at a ratio of 1.0 to 1.0⁽¹⁾.
<ul style="list-style-type: none"> ▪ VOC offsets provided by SCAQMD at a ratio of 1.2 to 1.0 for federal sources exempted by SCAQMD which switch from ozone depleting compounds to VOCs. 	<ul style="list-style-type: none"> ▪ VOC offsets provided by SCAQMD at a ratio of 1.2 to 1.0 for federal sources exempted by SCAQMD which switch from ozone depleting compounds to VOCs. (No Change)
<ul style="list-style-type: none"> ▪ No credit taken for surplus reductions created from offsets (ERCs) provided (at 120 %) by minor sources which are not exempt from offset requirements under SCAQMD NSR rules (<i>i.e.</i>, > 4 but < 10 TPY of VOCs and NOx, etc.). 	<ul style="list-style-type: none"> ▪ Credit will be taken for surplus reductions created from offsets (ERCs) provided (at 120 %) by minor sources which are not exempt from offsets requirements under SCAQMD rules⁽²⁾.

⁽¹⁾ EPA's Technical Support Document (TSD) dated 10/24/96 for EPA's Notice of Final Rulemaking (Federal Register 12/4/96) for SIP Approval of SCAQMD NSR Rules, pages 14, 15, and 17.

⁽²⁾ TSD, page 17.

Table 6 continued

Future (Post-2005) Emission Reductions (continued)

SCAQMD's Existing NSR Offset Account and Tracking System	SCAQMD's Proposed Revised NSR Offset Account and Tracking System
<ul style="list-style-type: none"> No credit taken for surplus reductions created from the 20 % additional SO_x, CO, and PM₁₀ offsets (ERCs) provided at 1.2 to 1.0 ratio compared to 1.0 to 1.0 ratio. 	<ul style="list-style-type: none"> Credit will be taken for surplus reductions created from the 20 % additional SO_x, CO, and PM₁₀ offsets (ERCs) provided by federal major sources at a ratio of 1.2 to 1.0 compared to 1.0 to 1.0 ratio⁽¹⁾.
<ul style="list-style-type: none"> No SIP adjustment for NSR tracking system. 	<ul style="list-style-type: none"> Appropriate assumptions in the SIP to reflect NSR tracking system with commitment to make up any shortfall in next AQMP revision pursuant to state law.
<ul style="list-style-type: none"> No credit taken for emission reductions created from application of zero BACT threshold⁽²⁾. 	<ul style="list-style-type: none"> No credit taken for emission reductions created from application of zero BACT threshold at this time⁽²⁾. (No Change)
<ul style="list-style-type: none"> No credit taken for surplus reductions created from offsets (ERCs) provided (at 120 %) by modifications to major sources, which are otherwise not defined as "major modifications" to a major source pursuant to Rule 1306 – Federal Major Modifications. 	<ul style="list-style-type: none"> No credit will be taken for surplus reductions created from offsets (ERCs) provided (at 120 %) by modifications to major sources, which are otherwise not defined as "federal major modifications" to a major source pursuant to Rule 1306 – Federal Major Modifications at this time, unless a specific determination of "non-major modification" is made for such a project.
<ul style="list-style-type: none"> No credit taken for application of LAER in excess of federal requirements to any increase in emissions at a major stationary source for non-ozone precursors (SO_x, CO, and PM₁₀). 	<ul style="list-style-type: none"> No credit taken for application of LAER in excess of federal requirements to any increase in emissions at a major stationary source for non-ozone precursors (SO_x, CO, and PM₁₀) at this time. If SCAQMD decides to pursue use of such credits in the future, further discussions with EPA will be necessary.

⁽¹⁾ EPA's Technical Support Document (TSD) dated 10/24/96 for EPA's Notice of Final Rulemaking (Federal Register 12/4/96) for SIP Approval of SCAQMD NSR Rules, pages 14, 15, and 17.

⁽²⁾ TSD, page 17.

Table 6 continued**NSR Equivalency Demonstration**

SCAQMD's Existing NSR Offset Account and Tracking System	SCAQMD's Proposed Revised NSR Offset Account and Tracking System
<ul style="list-style-type: none"> Equivalency demonstration typically completed within two years of the close of the reporting period. 	<ul style="list-style-type: none"> Preliminary (worst case) equivalency demonstration completed within one year of the close of the reporting period. If preliminary equivalency demonstration does not verify equivalency, final equivalency demonstration completed within six months of the preliminary equivalency demonstration timeframe.
<ul style="list-style-type: none"> No projections of future equivalency done with annual equivalency demonstrations 	<ul style="list-style-type: none"> All annual equivalency demonstrations (preliminary and final) will be accompanied by projected NSR offset account balances for the two years following the subject reporting period. These projections are for the purpose of prospectively determining if sufficient offsets remain in SCAQMD's accounts to continue providing Priority Reserve offsets and will not constitute a part of the equivalency demonstrations.
<ul style="list-style-type: none"> Funding of Priority Reserve conducted quarterly on an automatic basis without utilization of any projections of SCAQMD's offset account balances. 	<ul style="list-style-type: none"> Executive Officer to exercise the option to discontinue funding the Priority Reserve upon finding that SCAQMD's offset accounts do not include sufficient credits. This will include discontinuation of funding when offset account balance projections in the most recent equivalency demonstration do not indicate equivalency for the current reporting period.

Table 6 continued**Backstop Measures**

SCAQMD's Existing NSR Offset Account and Tracking System	SCAQMD's Proposed Revised NSR Offset Account and Tracking System
No backstop measures identified for addressing potential shortfalls in SCAQMD's offset accounts.	<p>Several backstop provisions identified in a tracking rule, one or more to be implemented as needed to return SCAQMD's NSR program to equivalency with federal NSR requirements and correct any credit shortfall:</p> <ul style="list-style-type: none"> ▪ Provide additional credits within six months of the final annual determination; to be derived from SCAQMD purchase of credits, SCAQMD funding of emission reduction projects using quantification protocols approved by EPA, application of LAER in excess of federal requirements, or other EPA-approved credit sources. ▪ Suspend issuance of both Priority Reserve and Offset Budget credits within 90 days, not to be resumed until equivalency has been reestablished. ▪ Amend Rule 1304 to eliminate certain offset exemptions.

USE OF CREDITS

The above-described credits will be used to fund the Offset Budget as adopted by SCAQMD in Rule 1309.2 in addition to the current use of credits to provide offsets for sources subject to federal offset requirements but which are exempt from offset requirements under SCAQMD Regulation XIII (Rule 1304) and to provide Priority Reserve offsets (Rule 1309.1) in order to provide equivalence to federal NSR requirements. As indicated earlier, a list of Regulation XIII provisions for which sources are exempt from offset requirements and SCAQMD uses its internal offset account credits may be used to demonstrate equivalency is presented in Attachment 2.

TRACKING AND BACKSTOP

SCAQMD will make an annual equivalency demonstration in two steps. In step one, SCAQMD proposes to make a preliminary annual determination of equivalency within twelve months of the close of each reporting period which will also be reflected in a tracking rule that it will develop and adopt. Such preliminary annual determination will

be a very conservative determination based on the combined debits from the previous year but will not include the orphan shutdowns (credits) from that reporting period. Therefore, the preliminary annual determinations will represent “worst case” analyses. Provided the preliminary annual determination demonstrates equivalency, the orphan shutdowns for each reporting period will be reported (and credited) in the subsequent preliminary annual determination, as illustrated in Figure 1. However, if the preliminary annual determination does not demonstrate equivalency, SCAQMD proposes as step two to make a final annual determination, which will include the reporting period’s orphan shutdown credits. The final equivalency determination will be prepared within six months of the preliminary equivalency determination time frame, as illustrated in Figure 2. For example, the preliminary annual determination for reporting year B (including all debits for years A and B and only orphan shutdown credits for year A) will be completed by the end of reporting year C. Provided this preliminary annual determination for year B demonstrates equivalency, the year B orphan shutdowns will be included in the preliminary annual determination for year C (to be completed by the end of year D). On the other hand, if the preliminary annual determination for year B does not demonstrate equivalency, a final annual determination incorporating year B’s orphan shutdown credits will be prepared within six months of the end of year C. The offset accounting will be conducted in the following order:

1. Year B’s debits are first subtracted from any remaining pre-1990 credits (1990-2005 timeframe only); then
2. Any debits remaining after step 1 are subtracted from any post-1990 credits remaining from year A; then
 - 3a. If there no remaining debits the post-1990 credits remaining from step 2 are discounted as described in the discussion of Surplus Discount at Time of Use. Year B’s credits are then added to the discounted post-1990 credits remaining from the year A.
 - 3b. If there are any remaining debits from step 2 (meaning there are not any post - 1990 credits remaining) the year B’s remaining debits are subtracted from year B’s credits.

Each preliminary annual determination (and each final annual determination, as needed to demonstrate equivalency) will be presented to SCAQMD’s Governing Board in a report from the Executive Officer (“Board Letter”) at a public meeting of the SCAQMD Governing Board. The annual equivalency determination will include the balance in SCAQMD’s offset account for each pollutant, as well as summaries of credit and debit data by category such as Priority Reserve, Community Bank, and Rule 1304 exemptions.

In addition, SCAQMD proposes to evaluate the future availability of credits in SCAQMD’s offset accounts by conducting a two-year projection of debits, credits, and account balances in conjunction with (but not as part of) each annual equivalency demonstration. This analysis will include projected debits, credits, and offset account balances for the two years following the period covered by the Board Letter for purposes of predicting if there will or will not be sufficient credits in SCAQMD’s offset accounts.

The projection for each pollutant will be based on the average of the previous five years' credits and debits for that pollutant. The Executive Officer will not make quarterly allocations to the Priority Reserve for any pollutant during a time when SCAQMD's offset account for that pollutant is not projected to remain positive¹⁰. The purpose of the projections is to prospectively determine if sufficient offsets remain in SCAQMD's accounts to continue funding the Priority Reserve; they are not intended to demonstrate equivalency retrospectively. SCAQMD is currently developing amendments to Rule 1309.1 – Priority Reserve which will clarify this procedure and authority for the Executive Officer and the tracking rule (also under development) will call for these projections and direct the Executive Officer to exercise this authority when equivalency is not projected.

SCAQMD will also propose, as part of the tracking rule, backstop provisions to be triggered in the event that the final annual determination does not demonstrate equivalency. In such an event, the backstop provisions would require SCAQMD to take one or more of the following actions to the extent necessary to correct the credit shortfall:

- Provide additional credits within six months of the final annual determination; such credits could be derived through SCAQMD purchase of credits, through SCAQMD funding of emission reduction projects using quantification protocols approved by EPA on a case-by case or programmatic basis, application of LAER in excess of federal requirements¹¹, or other approved sources of credits.
- Suspend issuance of both Priority Reserve and Offset Budget credits (Rules 1309.1 and 1309.2) within 90 days and not resume the issuance of any such credits until SCAQMD has demonstrated that equivalency has been reestablished. Equivalency may be reestablished through procurement of additional offsets and/or appropriate program modifications.
- Amend Rule 1304 to eliminate certain categories of offset exemptions to be identified during the rulemaking process.

¹⁰Offsets provided from the Priority Reserve are debited from SCAQMD's offset accounts for the period during which the permit was issued (*i.e.*, for the timeframe they are used) whereas the quarterly allocations made to the Priority Reserve pursuant to Rule 1309.1(a) do not constitute debits from SCAQMD's offset accounts. The newly-proposed future years' projections of balances in SCAQMD's offset accounts will include projected use of Priority Reserve offsets as well as offsets used through the Community Bank and for sources exempted pursuant to Rule 1304. In addition, a significant portion of the quarterly allocations to the Priority Reserve are used by sources which are not subject to federal offset requirements (*i.e.*, federal minor sources) and, therefore, do not need to be debited from SCAQMD's offset accounts for the purpose of federal equivalency demonstration. Furthermore, the portion that is subject to federal offset requirements and which needs to be debited from SCAQMD's offset accounts is already included in the two future years' projections done with each annual equivalency demonstration.

¹¹Precise quantification of all surplus credits generated through application of LAER in excess of federal requirements may be extremely resource intensive. Therefore, SCAQMD may, with EPA approval, demonstrate that such application of LAER has generated at least enough surplus reductions to make up for the shortfall using very conservative assumptions to estimate the surplus reductions.

ATTACHMENT 1
SCAQMD'S NSR OFFSET TRACKING—FEDERAL RUNNING BALANCES

ATTACHMENT 2:
LIST OF SOURCES EXEMPT FROM OFFSET REQUIREMENTS AND
PROVISIONS COVERED BY EQUIVALENCY SHOWING

Rule 1304 - Exemptions:

- (1) Replacements need to be tracked because of PTE Baseline in 1304 (a)(1)
Emissions will generally be lower due to BACT. SCAQMD will demonstrate through representative analysis that emission reductions from BACT exceed those needed for offsets pursuant to actual – potential analysis.
- (2) Relocations need to be tracked because of PTE baseline in 1304(c)(1)
Emissions will generally be lower due to BACT.
- (3) Abrasive Blasting Equipment
- (4) Air Pollution Control Strategies
- (5) Emergency Equipment
- (6) Portable Internal Combustion Engines
- (7) Methyl Bromide Fumigation
- (8) Replacement of Ozone Depleting Compounds
- (9) Portable Equipment
- (10) Regulatory Compliance
- (11) Regulatory Compliance for Essential Public Services
- (12) Facility Exemption (VOC, NO_x, SO_x, or PM₁₀ PTE less than 4 tons per year or CO PTE less than 29 tons per year)
- (13) Resource Recovery
- (14) Electric Utility Boilers Alt Energy

Rule 1309.1 - Priority Reserve

The Priority Reserve, which is funded from SCAQMD's offset accounts, provides a source of emission offsets for certain priority categories of sources. Except as noted below, these offsets are provided by SCAQMD at no cost to the operator. The various categories of sources eligible to access the Priority Reserve are summarized below:

- (1) Innovative Technology
Use of a technology that results in significantly lower emissions than would the use of BACT.

- (2) **Research Operations**
Projects with the purpose of “investigation, [experimentation], or research to advance the state of knowledge or the state-of-the-art.” Limited to at most two years.
- (3) **Essential Public Service**
Sources in the following categories located at facilities where all sources operate at or below BARCT levels
 - Publicly-owned sewage facilities;
 - Prisons;
 - Police facilities;
 - Fire fighting facilities;
 - Schools;
 - Hospitals;
 - Construction/operation of landfill gas control or processing facility;
 - Water delivery operations; and
 - Public transit.
- (4) **Electrical Generating Facilities**
Specified categories of facilities that generate electricity; meet BARCT for all sources; applicant has conducted a due diligence effort to acquire ERCs on the open market; applicant has applied for California Energy Commission certification or SCAQMD permit to construct during calendar years 2000, 2001, 2002, or 2003¹²; and applicant pays the following fee for each pound of Priority Reserve offsets obtained (ROG and NOx not available for these sources):
 - \$25,000 per pound PM10 and day;
 - \$8,900 per pound SOx per day; and
 - \$12,000 per pound CO per day.

Rule 1309.2 - Offset Budget

Sources that are not exempt from offset requirements pursuant to Rule 1304 and are not eligible to obtain offsets from the Priority Reserve may obtain offsets from the Offset Budget provided they meet certain criteria¹³:

- (1) All sources the applicant owns or operates comply with BARCT;
- (2) Applicant has conducted a due diligence effort to acquire ERCs on the open market;
- (3) Applicant pays the appropriate mitigation fee (based on pollutant and pounds of offsets obtained) specified in Regulation III – Fees; and
- (4) Applicant publishes a notice (prepared by SCAQMD’s Executive Officer) in a newspaper of general circulation in each of the four counties in SCAQMD, sends copies of the notice to the Administrator of EPA’s Region IX and the Executive

¹²Staff is currently developing an amendment to Rule 1309.1 to expand the date range for applications eligible to receive Priority Reserve offsets for electrical generating facilities.

¹³The Offset Budget has not been implemented because it has not been approved into the State Implementation Plan.

Officer of the California Air Resources Board, and responds to all public comments received within 30 days of publication.

ATTACHMENT 3:
REGULATION XIII NEW SOURCE REVIEW GUIDANCE MANUAL
(October 1990)

ATTACHMENT 4:
EXAMPLES OF AVAILABLE PRE-1990 PERMIT RECORDS

ATTACHMENT 5
AREA SOURCE INVENTORY METHODOLOGY

ATTACHMENT 6:
STATUS REPORTS ON REGULATION XIII – NEW SOURCE REVIEW COVERING
AUGUST 1999 THROUGH JULY 2002