

SETTLEMENT AGREEMENT

This Settlement Agreement ("Agreement") is entered into by Public Service Company of Oklahoma ("PSO"), the Secretary of the Environment on behalf of the State of Oklahoma ("Secretary"), the Oklahoma Department of Environmental Quality ("ODEQ"), the United States Environmental Protection Agency ("EPA"), and the Sierra Club. PSO, the Secretary, ODEQ, EPA, and the Sierra Club are hereinafter collectively referred to as "the Parties" for purposes of this Agreement.

RECITALS

- A. On December 28, 2011, EPA issued a final rule entitled, "Approval and Promulgation of Implementation Plans; Oklahoma; Federal Implementation Plan for Interstate Transport of Pollution Affecting Visibility and Best Available Retrofit Technology Determinations," 76 Fed. Reg. 81,728 (Dec. 28, 2011) (the "Final Rule").
- B. The Final Rule partially approved and partially disapproved Oklahoma's state implementation plan ("SIP") submitted under the "visibility" and "interstate transport" provisions of the Clean Air Act ("CAA"), 42 U.S.C. § 7410, 7491, and 7492. The Final Rule included a federal implementation plan ("FIP") establishing Best Available Retrofit Technology ("BART") emission limitations on sulfur dioxide ("SO₂") for Units 3 and 4 of PSO's Northeastern plant ("PSO's Units") to address the visibility and interstate transport provisions of the CAA.
- C. PSO desires to develop and implement a comprehensive strategy to comply with its obligations with respect to the visibility and interstate transport provisions of the CAA as well as its other obligations with respect to the CAA in a coordinated manner.
- D. PSO intends to install low NO_x combustion technologies on both of its Units, retire one of its Units, and install and operate on its other Unit a dry sorbent injection system and baghouse in order to achieve emissions rates that comply with the terms of this Agreement and with its obligations with respect to the visibility provisions of the CAA.
- E. PSO intends to retire one of its Units and install and operate on its other Unit a dry sorbent injection system, a baghouse, and activated carbon injection to achieve emissions rates that comply with the Mercury & Air Toxics Standard that became effective April 16, 2012, 40 C.F.R. § 63.9984 ("the MATS Rule"). Properly designed and operated air pollution control systems consisting of dry sorbent injection system, baghouse, and activated carbon injection can achieve the MATS Rule emission limits. An EPA letter to the ODEQ and PSO dated July 18, 2012, expresses EPA's support of PSO's comprehensive strategy to use the technologies described in the Regional Haze Agreement referenced in Attachment A to this Agreement to achieve the emission limitations prescribed by the MATS Rule. The letter is attached to this Agreement as Attachment B.

- F. On February 24, 2011, PSO timely filed a Petition for Review, challenging the issuance of the Final Rule in *Public Service Company of Oklahoma v. U.S. Environmental Protection Agency, et al.*, No. 12-9524. On March 26, 2012, Sierra Club filed a timely motion to intervene. The motion was granted March 27, 2012.
- G. The CAA and EPA's regulations require States to develop SIPs to implement the CAA's provisions, including the CAA's visibility and interstate transport provisions. See 42 U.S.C. §§ 7410(a)(2)(D)(i)(II), (J), 7491(b)(2); 40 C.F.R. § 50.300(a). ODEQ is the administrative agency in the State of Oklahoma responsible for developing and proposing such SIPs. See 27A O.S. §§ 2-5-105(3), (20), 1-3-101(B)(8), 2-3-101(B)(2). The Secretary, as the Governor's designee for the State of Oklahoma, is responsible for submitting SIPs to EPA for review. See 40 C.F.R. Part 51, Appendix V, Section 2.1(a); 40 C.F.R. § 51.103(a). Because this Agreement requires ODEQ to develop and propose and the Secretary to submit SIP revisions to EPA under the visibility and interstate transport provisions of the CAA, and ODEQ and the Secretary prefer to regulate PSO under such SIP revisions rather than EPA's FIP, ODEQ and the Secretary have an interest in and are essential parties to this Settlement Agreement.
- H. The Parties have negotiated in good faith and have determined that the settlement reflected in this Agreement is in the public interest. If approved and implemented as set forth herein, this Agreement will resolve PSO's Petition for Review.
- I. This Agreement will not impact any other provisions of the Final Rule, and/or any other applicable federal, state, and local laws and regulations. No other claims will be affected by the resolution of the issues related to PSO's Units as set forth herein.

AGREEMENT

- 1. PSO, Sierra Club, and EPA agree that within ten (10) days after this Agreement is executed by the Parties (i.e., signed), but before finalization pursuant to Paragraph 16 of this Agreement, they will jointly move the Court for an order holding in abeyance PSO's Petition for Review pending implementation of the terms of the Agreement.
- 2. Within thirty (30) days of the effective date of this Agreement, PSO shall submit to ODEQ final and complete versions of all information and documentation (including technical supporting documentation for PSO's Units) necessary for the development of the SIP revisions referenced in Paragraphs 3 and 4.
- 3. No later than one hundred-twenty (120) days after PSO provides ODEQ with the information and documentation required in Paragraph 2, ODEQ will develop and propose a SIP revision under the visibility provisions of the CAA, 42 U.S.C. § 7491, and EPA's regional haze regulations, 40 C.F.R. § 51.308, that addresses PSO's Units ("Regional Haze SIP revision") in accordance with the provisions of Attachment A.
- 4. No later than one hundred-twenty (120) days after PSO provides ODEQ with the information and documentation required in Paragraph 2, ODEQ will develop and propose

a SIP revision under the interstate transport provisions of the CAA, 42 U.S.C. § 7410(a)(2)(D)(i)(II), that addresses PSO's Units ("Interstate Transport SIP revision") in accordance with the provisions of Attachment A.

5. No later than one hundred-twenty (120) days after PSO provides ODEQ with the information and documentation required in Paragraph 2, the Secretary shall provide the proposed SIP revisions required in Paragraphs 3 and 4 to EPA and request parallel processing of the SIP revisions from EPA pursuant to 40 C.F.R. Part 51, App. V, Section 2.3.
6. If ODEQ determines, at any time subsequent to PSO's submittal of all information and documentation for PSO's Units as required in Paragraph 2, that additional information and/or documentation is necessary in order to develop the SIP revisions referenced in Paragraphs 3 and 4, ODEQ shall provide PSO with a written request for such additional information and/or documentation with a copy to all Parties. The deadlines associated with the obligations under Paragraphs 3-5 of this Agreement shall be tolled during the period of time between the issuance of the written request and ODEQ's receipt of the requested information and/or documentation.
7. After the opportunity for public hearing and the close of Oklahoma's notice-and-comment period for the Regional Haze and Interstate Transport SIP revisions, but no later than ninety (90) days after the Secretary submits the request for parallel processing referenced in Paragraph 5, ODEQ will consider and if appropriate adopt the Regional Haze and Interstate Transport SIP revisions referred to in Paragraphs 3 and 4. If adopted, the Secretary will submit to EPA those SIP revisions.
8. The Regional Haze and Interstate Transport SIP revisions adopted and submitted to EPA under Paragraph 7 will include the provisions described in Attachment A to this Agreement unless the Parties, by written mutual agreement, amend the provisions described in Attachment A. If the Regional Haze and Interstate Transport SIP revisions adopted and submitted to EPA by the Secretary do not include the provisions described in Attachment A to this Agreement, PSO may file a motion to dissolve the stay of PSO's petition for review and request that a briefing schedule be set. PSO may also pursue any opportunities for administrative or judicial review of the Regional Haze and Interstate Transport SIP revisions adopted by ODEQ and submitted by the Secretary.
9. Within sixty (60) days of EPA's receipt of the final Regional Haze and Interstate Transport SIP revisions EPA will determine whether the revisions meet the requirements of the CAA consistent with 42 U.S.C. § 7410(k)(1)(B) ("completeness finding").
10. EPA will take final action on the Regional Haze and the Interstate Transport SIP revisions as soon as possible, but no later than six (6) months from the date of the completeness finding referred to in Paragraph 9 consistent with 42 U.S.C. § 7410(k)(2).
11. If EPA promulgates a final action approving the provisions of the Regional Haze and Interstate Transport SIP revisions included in Attachment A, as adopted and submitted to

EPA by Oklahoma, PSO, the Sierra Club, and EPA will promptly file a joint stipulation of dismissal of PSO's Petition for Review. The Parties agree that they will not challenge that portion of any final action issued by EPA that fully approves the Regional Haze and Interstate Transport SIP revisions as adopted and submitted to EPA by the Secretary that contain the provisions in Attachment A affecting PSO's Units.

12. Separately from the SIP process, PSO will report biannually to EPA (beginning in 2017 for the period 2015-2016, and every second year thereafter through the end of 2025 or 2026, whenever the last Northeastern unit is retired) on the energy produced by PSO's units and the sources of energy secured under PSO's long-term purchased power contracts. The initial report will include similar information for calendar years 2013-2014. Requests for proposals ("RFPs") for long-term purchase power contracts issued between 2013 and the date the reporting obligation ends will specifically seek bids for energy supplied by natural gas and renewable resources. The biannual reports will include copies of any RFPs issued during the reporting period, and a summary of the capacity or energy secured through any long-term power purchase agreements executed during the reporting period, including the unit(s) providing the purchased power, the amount of capacity or energy secured under the agreement, and the term of each agreement.
13. The Parties may, by written mutual agreement, extend the dates in Paragraphs 2-5, 7, and 9-10 by which actions must be taken to fulfill the Parties' respective obligations under this Agreement.
14. Nothing in the Regional Haze and Interstate Transport SIP revisions as adopted and submitted to EPA by Oklahoma or in this Agreement shall relieve PSO from its obligations to comply with all applicable federal, state, and local laws and regulations, including laws, regulations, and compliance deadlines that become applicable after the date of any revisions to Oklahoma's Regional Haze SIP that may be approved by EPA. Such laws and regulations include, but are not limited to, any EPA rule imposing requirements relevant to interstate transport under 42 U.S.C. § 7410(a)(2)(D) and the MATS Rule. Nothing in Oklahoma's Regional Haze SIP revision, including the BART determination for PSO's Units, should be construed to provide any relief from the emissions limits or deadlines specified in such regulations, including, but not limited to, deadlines for the installation of pollution controls required by any such regulations.
15. If EPA does not take final action approving those aspects of the Regional Haze and Interstate Transport SIP revisions that contain the provisions of Attachment A, as adopted and submitted to EPA by Oklahoma, PSO may file a motion to dissolve the stay of PSO's Petition for Review, and to request that a briefing schedule be set. EPA does not waive or limit any defense relating to such litigation. This shall be the only remedy for EPA's failure to fulfill its obligations under this Agreement. PSO and Sierra Club agree that contempt of court is not an available remedy under this Agreement.
16. The Parties agree and acknowledge that before this Agreement is final, EPA must provide notice in the Federal Register and an opportunity for public comment pursuant to CAA

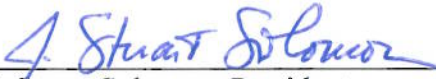
section 113(g), 42 U.S.C. § 7413(g). EPA shall promptly submit said notice of this Agreement to the Federal Register after this Agreement is executed by the Parties (i.e., signed). After this Agreement has undergone an opportunity for notice and comment, the Administrator or the Attorney General, as appropriate, shall promptly consider any such written comments in determining whether to withdraw or withhold their consent to the Agreement, in accordance with section 113(g) of the CAA.

If the United States elects not to withdraw or withhold its consent to this Agreement, EPA shall provide written notice to the Parties as expeditiously as possible. This Agreement shall become final and effective on the date that EPA provides such written notice to the Parties. If EPA does not provide such written notice within sixty (60) days after the notice of the Agreement is published in the Federal Register, the sole remedy shall be the right to file a motion to dissolve the stay of the Petition for Review, and to request that a briefing schedule be set. EPA does not waive or limit any defense relating to such litigation. PSO and Sierra Club agree that contempt of court is not an available remedy under this Agreement.

17. No provision of this Agreement shall be interpreted as or constitute a commitment or requirement that the United States or any of its departments or agencies obligate or pay funds in contravention of the Anti-Deficiency Act, 31 U.S.C. § 1341 *et seq.*, or in violation of any other statute, law, or regulation.
18. Nothing in this Agreement shall be construed to limit or modify the discretion accorded to EPA, ODEQ, or the Secretary by statute, or by general principles of administrative law.
19. Nothing in this Agreement shall be construed to limit or modify the rights of PSO or Sierra Club to seek reconsideration or judicial review of any altered, amended or revised provisions of any final action that ODEQ or EPA may take that differ in any material respect from the provisions described in Attachment A (or as amended by mutual written agreement of the Parties pursuant to Paragraph 8).
20. The undersigned hereby certify that they are duly authorized to bind the Party on whose behalf this Agreement is executed to the terms of this Agreement.
21. The provisions of this Agreement shall apply to and be binding on the Parties, their successors and assigns.
22. This Agreement may be signed in counterparts, and such counterpart signatures shall be given full force and effect.

FOR PETITIONER PSO:

Dated: 10-17-12



J. Stuart Solomon, President
Public Service Company of Oklahoma

FOR STATE OF OKLAHOMA:
SECRETARY OF THE ENVIRONMENT FOR
THE STATE OF OKLAHOMA

Dated: 10/1/12

Gary L. Sherer

FOR OKLAHOMA DEPARTMENT OF
ENVIRONMENTAL QUALITY:

Dated: 9-28-12

Steven A. Thompson

FOR U.S. ENVIRONMENTAL PROTECTION
AGENCY:

IGNACIA S. MORENO
Assistant Attorney General
Environment and Natural Resources Division

Dated: 2/8/13

By: Stephanie J. Talbert
STEPHANIE J. TALBERT
Environmental Defense Section
Environment and Natural Resources Division
U.S. Department of Justice
P.O. BOX 7611
Washington, DC 20044
(202) 514-2617
Fax: (202) 514-8865
Stephanie.Talbert@usdoj.gov

FOR INTERVENOR SIERRA CLUB:

Dated: 10/16/12



ATTACHMENT A

1. Oklahoma, through the Secretary, will submit to EPA a Regional Haze SIP revision that addresses PSO's Units and includes, among other things, the following elements:
 - a. Oklahoma's SIP revision will include a Regional Haze Agreement ("RHA") entered into by ODEQ and PSO to effectuate the BART determination.
 - b. The RHA will require that by no later than December 31, 2013, PSO will complete installation of low NO_x combustion technologies and achieve a nitrogen oxide ("NO_x") emission rate of 0.23 lb/MMBtu on a 30-day rolling average at each of PSO's Units.
 - c. The RHA will require that beginning on January 31, 2014, PSO will comply with a new SO₂ emission rate at each of PSO's Units of 0.65 lb/MMBtu on a 30-day rolling average, and beginning on December 31, 2014, PSO will comply with a new SO₂ emission rate of 0.60 lb/MMBtu on a 12-month rolling average at each of PSO's Units. PSO will maintain those emission rates until controls are installed at one unit as provided in subparagraph (e), and the other unit is retired as provided in subparagraph (d). The RHA will include an alternative operating scenario that addresses potential service disruption of coal supplies during the time period between January 31, 2014 through April 16, 2016.
 - d. The RHA will require that PSO seek all necessary regulatory approvals, and will retire one of the coal-fired generating units at Northeastern Station by April 16, 2016.
 - e. The RHA will require that PSO seek all necessary regulatory approvals, and install and operate a dry-sorbent injection system, activated carbon injection system, and a fabric filter baghouse, and secure further NO_x emission reductions by April 16, 2016 on the coal-fired generating unit at Northeastern Station that will continue to operate. After completion of the installation of the pollution controls required by this subparagraph, PSO will achieve a 0.15 lb/MMBtu emission rate for NO_x on a 30-day rolling average basis, and a 0.40 lb/MMBtu emission rate for SO₂ on a 30-day rolling average basis.
 - f. The RHA will require that during the first year of operation of the controls required under the RHA, PSO will develop and propose a monitoring program to test various operating profiles and other measures, to determine whether increased SO₂ removal efficiencies can be achieved during normal operations. Pursuant to the terms of the RHA, PSO will submit the monitoring program to EPA and ODEQ for review and will implement the monitoring program during the second and third years of operation of the dry sorbent injection system. PSO will evaluate and report the results of the monitoring program to EPA and ODEQ, and if that evaluation demonstrates that the technology is capable of sustainably

achieving an emission rate of less than 0.37 lbs/MMBtu on a 30-day rolling average basis without (i) altering the unit's fuel supply, (ii) incurring additional capital costs, (iii) increasing operating expenses by more than a negligible amount, and/or (iv) adversely impacting overall unit operations, ODEQ will propose to revise the emission rate in the RHA by 60 percent of the difference between 0.40 and the demonstrated emission rate. Upon adoption after notice and opportunity for hearing, Oklahoma, through the Secretary, will submit a Regional Haze SIP revision to EPA for approval. If the demonstrated emission rate is 0.37 lbs/MMBtu or greater, no adjustment will be made to the RHA, and the emission rate from the operating Northeastern coal-fired generating unit in the RHA will remain 0.40 lbs/MMBtu.

- g. The RHA will require that beginning in calendar year 2021, the Annual Capacity Factor (calculated for each calendar year as a percentage of MWH based on a rated capacity of 470 MW times 8760 hours) for the operating coal-fired generating unit at Northeastern Station will be reduced as follows:
 - i. to no more than 70 percent in calendar years 2021 and 2022;
 - ii. to no more than 60 percent in calendar years 2023 and 2024; and
 - iii. to no more than 50 percent in calendar years 2025 and 2026.
 - h. The RHA will require that no later than December 31, 2026, PSO will retire the remaining operating coal-fired generating unit at Northeastern Station. However, in calendar year 2021, the RHA will require PSO to evaluate whether the projected generation from that unit can be replaced at lower or equal total projected costs from natural gas or renewable resources. Pursuant to the RHA, PSO will provide a copy of the evaluation to EPA and ODEQ. If power is available from such resources at a lower projected total cost (including consideration of PSO's need to recover its remaining investment in the units), then the operating unit will retire no later than December 31, 2025.
- 2. Oklahoma, through the Secretary, will submit to EPA an Interstate Transport SIP revision that addresses PSO's Units and includes, among other things, the following elements:
 - a. An enforceable mechanism that addresses SO₂ reductions from sources other than those operated by PSO, to the extent necessary to achieve the anticipated visibility benefits from the 2018 regional modeling; and
 - b. A provision requiring that the enforceable mechanism referred to in Paragraph 2(a) of this Attachment A be implemented if the SO₂ emission rate for the controlled unit at Northeastern is not reduced to 0.30 lbs/MMBtu or less as a result of the Paragraph 1(f) of this Attachment A.



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

JUL 18 2012

OFFICE OF
AIR AND RADIATION

Mr. Stuart Solomon, President
Public Service Company of Oklahoma
212 East 6th Street
Tulsa, OK 74119

Mr. Steve Thompson, Executive Director
Oklahoma Department of Environmental Quality
P.O. Box 1677
Oklahoma City, OK 73101-1677

Dear Mr. Solomon and Mr. Thompson:

I want to express my thanks to both of you and the others who participated in the discussion on Thursday, July 12, 2012 regarding the remaining issues in Public Service Company of Oklahoma's (PSO) forward-looking and comprehensive approach to achieving emission reductions in Oklahoma. I know I speak not only for the EPA Office of Air and Radiation, but also for Sam Coleman and his team in EPA Region 6, in expressing my appreciation for all the hard work and commitment it has taken you to reach this accord.

EPA is pleased with the final agreement made by the State of Oklahoma and PSO to develop its plan for reducing emissions to meet state and federal requirements at the two coal-fired generating units at its Northeastern Station in Oologah, Oklahoma. While this agreement is focused on complying with the visibility requirements of the Clean Air Act, the control technology described in the agreement is also intended to achieve compliance with the Mercury and Air Toxics Standard (MATS). EPA supports such a comprehensive approach. Furthermore the types of controls that PSO plans to install (a combination of Dry Sorbent Injection (DSI) and subbituminous coal to meet the acid gas limits, activated carbon injection and a baghouse to meet the mercury limits, and a baghouse to meet the PM limits) are the types of controls that, when well designed and operated, EPA would expect to be able to meet the MATS limits.

EPA has every confidence that this technology, when properly installed and operated, will provide a means for PSO to meet both the visibility requirements of the Clean Air Act and the MATS requirements. This is exactly the type of agreement that will provide for a cost-effective approach to meet both the visibility requirements of the Clean Air Act and ultimately the MATS rule. EPA is committed to work closely with ODEQ in the development of the proposed SIP revision for a revised BART determination for the PSO plant based on the plan outlined in this agreement.

I look forward to the continued success of our organizations in the implementation of this important agreement.

Sincerely yours,

A handwritten signature in blue ink, appearing to read 'Gina McCarthy', is written over the printed name.

Gina McCarthy
Assistant Administrator