



Climate Change Update

RECENT DEVELOPMENTS REGARDING CLIMATE CHANGE

June 2010

Climate Change Update is a publication of Weil, Gotshal & Manges that provides timely and practical updates on significant legal, business and political developments related to domestic and international efforts to reduce greenhouse gas emissions and how those efforts impact corporations.

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Summer Recess Approaches – Immediate Future of Climate Change Legislation and Regulation Uncertain

On the Hill

Senate Democrats announced last week a new strategy for moving ahead with climate and energy legislation before the August recess. The plan calls for linking a politically-sensitive climate bill to a measure introduced on June 21 by Senators Jeff Bingaman (D-NM) and Lisa Murkowski (R-AK) that would reform offshore drilling rules and increase oversight of companies engaged in offshore oil and gas exploration, with the hope of attracting votes for the broader package by including drilling reforms that would be difficult to oppose in light of the ongoing oil spill in the Gulf of Mexico. Democrats, however, have yet to select which climate bill will be coupled with the drilling reform proposal, and they have several to choose from.

The American Power Act, sponsored by Senators John Kerry (D-MA) and Joe Lieberman (I-CT), is perhaps the most aggressive option, which provides for an industry-wide cap-and-trade system to reduce greenhouse gas (“GHG”) emissions. Senator Lieberman claims to have secured 50 votes for his bill, but attracting 10 additional votes to overcome a filibuster is a daunting task, particularly as most Republicans and a handful of Democrats from coal-producing and coal-burning states have announced their opposition to any cap-and-trade proposal. Another option being discussed is a more limited cap-and-trade provision that applies only to electric utilities, similar to the Regional Greenhouse Gas Initiative (“RGGI”) already in effect in several northeastern states. The utility-only option is being considered as something of a test run on an industry already familiar with cap-and-trade systems, which have been applied to utilities in certain states under RGGI and nationally under the federal rules aimed at curbing acid rain. Such a proposal is currently being drafted by Senator Bingaman, Chairman of the Senate Energy and Natural Resources Committee and has attracted interest from at least one Republican Senator in Olympia Snowe (ME). The utility-only legislation, however, does not mollify critics from coal-producing and coal-burning states since coal-burning power plants will be affected the most by any cap-and-trade plan as they emit the largest quantities of GHGs.

Another option on the table is forgoing any restriction on GHG emissions and instead pushing forward with a bill focused on providing stimulus and demand for renewable energy sources. Senator Bingaman ushered such a bill (S. 1462, the American Clean Energy Leadership Act) through the Energy and Natural Resources Committee last June that would impose a national renewable electricity standard, provide federal financing for “clean energy” projects, and establish new energy

efficiency measures. Many Senators believe that an “energy only” climate bill coupled with restrictions on offshore oil and gas exploration stands the best chance of passage, however, President Obama, at a White House meeting on June 29, 2010, expressed his strong preference for legislation that “puts a price on” GHG emissions. While a bill without cap-and-trade or similar provisions restricting GHG emissions would not meet the President’s standard, an “energy only” bill may in fact be a fallback position in the event that a cap-and-trade bill can not attract enough votes.

No matter which approach Democrats choose to advance, it now appears that the full Senate will soon consider climate legislation, likely before the August recess. The Senator Majority Leader, Harry Reid (D-NV), is crafting a bill to bring to the Senate floor after the July 4th recess and has all but dared Republicans to vote against any measure that aims to prevent future catastrophic oil spills. This suggests a high level of confidence amongst Democratic leaders that, when forced to take a public position, some Republicans, and most Democratic fence-sitters, will support whatever measure accompanies offshore drilling reforms. While such tactics worked earlier this year when the Democrats passed health care reform legislation, it remains to be seen whether climate legislation will enjoy a similar fate as time winds down on the 111th Congress.

At the Agency

Despite lack of Congressional progress to mandate the reduction of GHG emissions, the United States Environmental Protection Agency (“EPA”) has responded to the Supreme Court’s decision in *Massachusetts v. EPA* and promulgated numerous regulations intended to mitigate climate change,¹ including its:

- Endangerment and Cause or Contribute Findings for GHGs under Section 202(a) of the Clean Air Act (“Endangerment Finding”), which found that the current and projected concentrations of GHGs in the atmosphere threaten the public health and welfare of current and future generations and that the combined emissions of GHGs from new motor vehicles and new motor vehicle engines contribute to the GHG pollution, which threatens public health and welfare;²
- Mandatory GHG Reporting Rule, which requires suppliers of fossil fuels or industrial GHGs, manufacturers of vehicles and engines and facilities that emit 25,000 metric tons or more per year of GHG emissions to submit annual reports to EPA detailing their GHG emissions data;³
- Tailpipe emissions regulation, which sets new standards to improve fuel efficiency and reduce GHG emissions from cars and light duty trucks; and
- The Prevention of Significant Deterioration and Title V GHG Tailoring Rule (“Tailoring Rule”), which will require large emitters to address their GHG emissions in their construction and operating air permits.

EPA will continue to advance its GHG regulatory agenda unless Congress or the judiciary removes EPA’s authority to do so. Congress could conceivably exclude GHGs from the scope of the Clean Air Act, although we note that on June 10, 2010, the Senate voted 53-47 against a resolution sponsored by Lisa Murkowski that would have stripped EPA of its authority to regulate GHGs. A federal court could also hold that EPA has not followed the proper federal procedures with respect to promulgating its GHG rules.

Opponents of GHG regulation are looking to use the court system to delay or prevent EPA’s ability to regulate GHGs by challenging the validity of the Endangerment Finding, which gives rise to EPA’s ability to regulate in this area, and also by challenging EPA’s actual GHG regulations on an individual basis.

As of today, no less than 38 suits challenging the validity of EPA regulations related to climate change have been filed in the U.S. Court of Appeals for the D.C. Circuit on behalf of almost 100 parties, including 15 states and 15 members of Congress. The substance of most plaintiffs’ complaints is that the Clean Air Act is ill-suited to regulate a substance that is emitted as widely as carbon dioxide, and many believe that Congress, as opposed to EPA, is best suited to decide if and how GHG emissions should be regulated. Although not all of the Plaintiffs’ challenges have yet to be substantively briefed, they are likely to focus on the quality of the scientific evidence that EPA relied upon in making its Endangerment Finding due to the recent controversies surrounding the climate science underpinning EPA’s finding. For example, one of the basic allegations in the State of Texas’ brief is that the temperature datasets that EPA relied on in making its finding lack integrity because of various measurement flaws and failures to observe proper scientific methods. Moreover, some plaintiffs have argued that EPA violated the Administrative Procedure Act by failing to consider the potential impacts of GHG regulation on jobs, businesses and local economies. Although the Endangerment Finding alone does not impose GHG restrictions, EPA’s ability to regulate GHG emissions becomes especially tenuous if the legal challenges to EPA’s Endangerment Finding are successful.

Opponents are not limiting their challenges to the Endangerment Finding, but rather also are attempting to halt, or at least limit, the scope of GHG regulation promulgated by EPA. Two lawsuits have challenged EPA's rule that sets GHG emissions standards for cars and trucks even though EPA developed the rule on a consensus basis with the states, the Department of Transportation and the auto industry.⁴ The auto industry, which prefers a uniform emissions standard, has already intervened on the part of EPA and any additional challenges to the tailpipe emission standards must be filed by July 6, 2010. Similar lawsuits have been filed regarding the Mandatory GHG Reporting rule and parties, such as the Coalition for Responsible Regulation, have already filed lawsuits challenging EPA's Tailoring Rule, which was only finalized six weeks ago.⁵ We suspect that numerous other challenges to EPA's tailoring rule will be filed prior to the August 2, 2010, filing deadline.

Other Judicial Challenges

Proponents of GHG emissions regulation also are turning to the judiciary for help in tackling potential impacts related to climate change. Plaintiffs are increasingly suing governmental agencies with regulatory control over specific projects, such as coal-fired power plants, or the issuance of permits related to those projects. Although many of these plaintiffs likely prefer that Congress or EPA issue comprehensive GHG legislation or regulation, they are pressing the issue one project or permit at a time. Although, to date, many of these challenges have failed in their attempts to block a proposed new coal-fired power plant or modifications to an existing facility, at least two power plant developers recently have accepted GHG

emissions limitations in their air permits. In December 2009, a coal gasification power plant developed by Southeast Idaho Energy, LLC accepted enforceable limits on carbon dioxide as part of a settlement with the Sierra Club and Idaho Conservation League. In addition, in February 2010, Calpine received approval to build the first domestic power plant with a federal limit on GHG emissions in California. The project's prevention of significant deterioration permit was the final regulatory approval that was needed for the project to proceed.

In addition to challenges to regulations and permits, several tort-based lawsuits seeking to directly limit defendants' GHG emissions or impose damages based on common law theories such as nuisance continue to wind their way through three separate federal circuits. While *Connecticut, et al. v. American Electric Power Co.*, No. 05-5104 (2nd Cir. 2009) ("AEP")⁶ and *Native Village of Kivalina, and the City of Kivalina v. ExxonMobil Corporation et al.*, No. 08-1138 (N.D. Cal. Sept. 30, 2009) ("Kivalina")⁷ are at varying stages in the appeal process, an unusual procedural development has occurred in the Fifth Circuit in the *Comer v. Murphy Oil USA, et al.*, 585 F.3d 855 (5th Cir. 2009) ("Comer") matter. In *Comer*, 14 private plaintiffs sued numerous industrial defendants under legal theories including private nuisance, trespass and negligence alleging that the defendants' carbon dioxide emissions contributed to human-caused global warming, which warmed the waters in the Gulf of Mexico and increased the frequency and severity of hurricanes, including Hurricane Katrina. Until recently, the Fifth Circuit was set to hear defendants' petition for rehearing *en banc* of its decision to reverse an earlier District Court decision to dismiss the case on procedural grounds. Oral argument before the Fifth Circuit was

scheduled to occur on May 24, 2010; however, the Fifth Circuit court canceled the *en banc* hearing due to a judge's recusal that left the court without a quorum to consider the matter. After directing the parties to submit letter briefs as to how the court should proceed, a five member majority of the remaining judges who had not recused themselves issued an order dismissing the defendants' petition for rehearing, which effectively reinstated the district court's dismissal of plaintiffs' lawsuit.

The Fifth Circuit's dismissal in *Comer* has created a conflict between the Fifth and Second Circuits on the issues of standing and the application of the political question doctrine with respect to climate change cases. Unlike the Fifth Circuit's decision in *Comer*, the Second Circuit refused in the *AEP* case to grant defendants' petition for rehearing *en banc* on its decision that a number of states and environmental groups could seek injunctive relief against several electric utility companies under common law theories of nuisance and trespass. The *AEP* case defendants are expected to file a certiorari petition with the U.S. Supreme Court by July 6, 2010. Likewise, the *Comer* plaintiffs have until August 26, 2010 to do the same with respect to the Fifth Circuit's dismissal. Assuming the *Comer* plaintiffs file a petition, and the Supreme Court grants review, the question of whether large emitters can be held liable by private plaintiffs for damages related to climate change will be examined by the high court sooner than most had envisioned.

This escalating climate change-related litigation combined with the inability of Congress to pass legislation on the matter is forcing many businesses, particularly large emitters, to decide on whether, and how best, to allocate capital to comply with actual and

potential GHG emissions regulations against a mounting backdrop of regulatory uncertainty. The numerous lawsuits filed to challenge EPA's GHG rules will likely delay, and could ultimately restrict EPA's ability to regulate over climate change. Plaintiffs' challenges to EPA's regulatory ambitions, coupled with permit challenges and tort-based challenges related to climate change, all but guarantee a larger role for the court system in resolving climate change-related disputes. We will continue to monitor significant developments in climate change litigation in order to advise our clients on how to best assess the uncertainty and manage the risk inherent in this expanding area of law.

- 1 In *Massachusetts v. EPA*, 549 U.S. 497 (2007), the Supreme Court ruled that GHGs are air pollutants under the Clean Air Act, and consequently EPA must regulate emissions of GHGs from new motor sources if those pollutants may reasonably be anticipated to endanger public health or welfare.
- 2 Although the Endangerment Finding itself did not impose any requirements on industry or other entities, it was a prerequisite to finalizing the EPA's proposed GHG emission standards for light-duty vehicles.
- 3 EPA recently has completed its rule for expanding GHG reporting requirements to several industry sectors – including underground coal mines, landfills, industrial wastewater and magnesium production sites.
- 4 Although petitioners have submitted petitions for review with respect to the Light Duty Vehicle GHG Emission Standards and Corporate Average Fuel Economy Standards, petitioners have not substantively briefed the issues underlying their challenge.
- 5 Although petitioners have submitted petitions for review with respect to the Tailoring Rule, petitioners have not substantively briefed the issues underlying their challenge.
- 6 The *AEP* plaintiffs allege that the energy utility defendants are the largest emitters of carbon dioxide in the United States, and are collectively responsible for ten percent of worldwide carbon dioxide emissions from human activities. Plaintiffs seek to force each of the electric utilities to abate its contribution to the nuisance by capping its emissions of carbon dioxide and then reducing those emissions by a specified percentage per year for at least a decade.
- 7 In *Kivalina*, the community of Kivalina, Alaska, brought a public nuisance action against 24 large emitters of GHGs for the cost of relocating the island community. The plaintiffs allege that the defendants' GHG emissions contributed to climate change, which, in turn, caused the breakup of sea ice that previously protected the island.

UNFCCC Talks – Bonn Session

The United Nations Framework Convention on Climate Change (“UNFCCC”) negotiations resumed in June in Bonn in the first significant meeting of the parties since the much-criticised conference in Copenhagen in December of last year. The non-binding Copenhagen Accord produced in December by a small group of countries, led by the US and China, contained a commitment to holding temperature rises down to 2° C but provided few, if any, indications as to how this would be achieved and was merely noted rather than adopted at the Copenhagen conference.

The Bonn meeting was one of several sessions scheduled in the run up to the 16th Conference of the Parties to the UNFCCC in Cancun this December at which it is hoped that the Copenhagen Accord will be translated into meaningful commitments under international law. Opinion appears divided over whether

any progress was made at Bonn or is possible in Cancun.

Observers comment that the atmosphere was much improved compared with Copenhagen. In the words of the UN's outgoing climate chief, Yvo de Boer, “countries were talking to each other rather than at each other.” However many countries have difficulties with the draft treaty text that emerged at the end of the two-week session in Bonn as a basis for further UNFCCC discussion.

The draft treaty text proposes that rich countries cut their emissions between 25-40% by 2020 and outlines a goal of cutting global emissions by at least 50-85% from 1990 levels by 2050 with emissions peaking in 2020. These targets are arguably more ambitious than those proposed at the Copenhagen climate summit last December and are likely to prove difficult for the US to accept given

that legislation to achieve much more modest cuts is currently stalled in the US Senate. Nor do they satisfy developing countries who are concerned that the targets are not enough to avoid climate change effects to which they are most vulnerable, but which they did not cause. Developing countries are also concerned about the proposal that all countries emissions should “peak” in 2020. This would constrain poorer countries' growth at a time when they need to develop rapidly to improve living standards. The consensus among poor countries appears to be that the emerging treaty text is biased against them.

The draft treaty text will be debated and developed at further sessions in Bonn and Beijing before the next full conference in Cancun in December. The atmosphere may be an improvement on that in Copenhagen,

but many suspect that a new legally binding deal is out of reach for 2010 and is now more likely to occur in 2011 or even later. It remains to be seen whether a comprehensive multilateral deal under the UNFCCC will be preferable to deals between like-minded countries along the lines of the Copenhagen Accord for many of the negotiating parties.

EU Carbon Tax Stalls

Proposals for an EU-wide carbon tax were revived recently only to be kicked immediately back into the long grass. The European Commissioner for Taxation, Algirdas Semata, proposed a tax of up to 20 euros per tonne of CO₂ at a meeting of EU commissioners in Brussels on June 23. The proposal is an echo of plans raised by his predecessor, Lazlo Kovacs, and is supported by EU member states such as Finland and Sweden who already have national carbon taxes in place and who want to ensure a level playing field for their economies. France is also supportive after its own proposals for a domestic carbon tax were struck down by its Constitutional Court last year.

However, unanimity among member-states is required for the adoption of EU-wide tax rules and there is strong opposition in some quarters. The UK and Ireland have a range of domestic

environmental taxes, including in Ireland's case a carbon tax, but believe that tax issues like this must be determined by domestic governments alone. Germany and Poland, both countries with significant heavy coal and steel industries, fear that their economies would be harmed. The meeting of EU Commissioners agreed that an impact assessment was needed to take account of the effects of such a tax in the present economic downturn and Mr. Semata has been asked to look into this, without any specific deadline. As a result, it may be some time before the issue is raised again in the EU.

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Absent U.S. Senate action on climate legislation or another significant development in this area, we will resume publication of Climate Change Update in September.

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