



THE CLIMATE REPORT

U.S. REGULATORY DEVELOPMENTS

Jane K. Murphy, Editor

■ U.S. EPA EXTENDS GREENHOUSE GAS EMISSIONS REPORTING DEADLINE

The United States Environmental Protection Agency announced on March 17 that the deadline for the submission of 2010 greenhouse gas reports has been extended to September 30, 2011. EPA indicated that the extension will allow for the refinement and testing of EPA’s Electronic Greenhouse Gas Reporting Tool (“e-GGRT”), although there has been speculation that EPA could also be examining the reporting rule in light of the recent Executive Order requiring that federal agencies more carefully consider the economic impacts of regulatory requirements.

Entities subject to the reporting requirement are required to designate an authorized representative, registering with e-GGRT at least 60 days before the reporting deadline, or August 1, 2011, if they have not done so already.

Although EPA still intends to release the 2010 greenhouse gas emissions data to the public by the end of 2011, the exact scope of data to be publicly available remains unclear. As we previously reported, EPA proposed in December 2010 to defer until 2014 the reporting (but not the collection) of some inputs to emission calculations for certain reporting entities, in response to concerns that public disclosure

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of the information could cause competitive harm. EPA also requested additional public comment on the public disclosure of this information and received more than 30 comments by the March 7, 2011 deadline. Many of the submissions were from regulated entities arguing that public disclosure of emission data inputs would allow competitors to reverse engineer production processes, resulting in significant competitive harm, particularly if competitors are not based in the United States and therefore not subject to the same disclosure obligations under the reporting rule.

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■ **MEMBERS OF CONGRESS SEEK TO LIMIT U.S. EPA'S GREENHOUSE GAS AUTHORITY**

A number of proposals have been introduced in Congress to reduce or eliminate U.S. EPA's current authority to regulate greenhouse gas emissions. One such initiative, introduced by Senator Lisa Murkowski (R-Alaska), was defeated in 2010. More recent proposals have taken a variety of forms, ranging from an outright prohibition on EPA's authority to a two-year suspension of such authority with respect to stationary sources. On April 6, 2011, the Senate considered, and rejected, several amendments to a small business bill that would have limited EPA's authority.

However, on April 7, 2011, the House of Representatives passed H.R. 910, which would exclude certain greenhouse gases from the definition of "air pollutant" under the Clean Air Act. If enacted, the bill would effectively prohibit EPA from regulating greenhouse gases for climate change purposes and override the Supreme Court's 2007 decision in *Massachusetts v. EPA*, 549 U.S. 497. H.R. 910 has been referred to the Senate Committee on Environment and Public Works. Companion legislation has been introduced in the Senate as an amendment to the Energy Tax Prevention Act of 2011 (S.482) and as a stand-alone bill.

Some members of Congress have raised the Congressional Review Act as a way to limit EPA's authority on climate change issues. The Congressional Review Act, a part of the

Small Business Regulatory Enforcement Fairness Act of 1996, enables Congress to review (within 60 days) a new federal regulation and overrule it by passage of a joint resolution. Due to the 60-day time limit, however, the Act is no longer applicable to most of EPA's prior greenhouse gas actions, including the endangerment finding.

President Obama has previously indicated that he would veto any legislation that limits EPA's authority, and it is unclear whether Congress would be able to override such a veto, which would require a two-thirds majority in both the House and the Senate.

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■ **CALIFORNIA COURT ENJOINS STATE CAP AND TRADE PROGRAM FOR GREENHOUSE GAS EMISSIONS**

On March 18, 2011, the San Francisco Superior Court issued its decision in *Association of Irrigated Residents v. California Air Resources Board*, setting aside and enjoining implementation of the Scoping Plan developed by the California Air Resources Board ("CARB") under California's landmark Global Warming Solution Act of 2006, known as "AB 32." The court held that CARB must first comply with the California Environmental Quality Act ("CEQA"), which requires public agencies to undertake environmental review of certain "projects" that may have a significant effect on the environment. The injunction likely will delay several of CARB's greenhouse gas emission reduction programs, including its cap and trade program.

AB 32 requires CARB to prepare a Scoping Plan for how it will reduce greenhouse gas emissions in California to 1990 levels by the year 2020. After CARB approved a Scoping Plan on December 12, 2008, 13 petitioners, including environmental groups and individuals, challenged CARB's action under both AB 32 and CEQA.

The Superior Court rejected the petitioners' challenge under AB 32. In particular, the court upheld CARB's choice of a cap and trade program as the primary method to achieve the

emission reductions, rejecting petitioners' claim that AB 32 required CARB to show that emission reductions from a cap and trade program will be at least equivalent to reductions that would be achieved through direct regulation.

The Superior Court determined, however, that CARB had not adequately discussed or evaluated alternative approaches to achieving emission reductions, as required by CEQA. CARB prepared a Functionally Equivalent Document ("FED") as its environmental impact report ("EIR"), which the court determined was sufficiently detailed for a program-level environmental document. However, the court found that the discussion of alternatives—including carbon fees or taxes—in the FED was inadequate:

While a program-level EIR need not be as detailed as a project-level EIR, [CARB] must still provide the public with a clear indication based on factual analysis as to why it chose the Scoping Plan over the alternatives. [CARB's] extensive evaluation of the proposed cap and trade program in Chapter II of the Scoping Plan provides the public with information about cap and trade only. CEQA requires that [CARB] undertake a similar analysis of the impacts of each alternative so that the public may know not only why cap and trade was chosen, but also why the alternatives were not.

Association of Irrigated Residents, Case No. CPF-09-509562, Statement of Decision at 30-31.

The Superior Court also determined that CARB had improperly approved the Scoping Plan before completing its environmental review in May 2009, when its staff responded to the public's comments on the FED, thus undermining CEQA's goal of informed decision-making by public agencies. The peremptory writ of mandate enjoins any implementation of the Scoping Plan until CARB has satisfied the requirements of CEQA and CARB's certified environmental review program. Absent a stay of the decision, it is likely that finalization of California's cap and trade program will be deferred until CARB certifies a revised FED.

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For a more detailed analysis of the Superior Court decision, see *Jones Day Commentary*, "California Superior Court Enjoins California's Cap and Trade Program for Greenhouse Gas Emissions," available at http://www.jonesday.com/California_Superior_Court_Enjoins.

For a detailed look at California's proposed cap and trade program, see Jones Day *White Paper*, "California Adopts Cap and Trade Program for Greenhouse Gas Emissions," available at http://www.jonesday.com/California_Adopts_Cap_and_Trade.

■ FERC ISSUES FINAL DEMAND RESPONSE RULE

The Federal Energy Regulatory Commission issued its final rule addressing compensation for demand response in Regional Transmission Organization ("RTO") and Independent System Operator ("ISO") organized wholesale energy markets. "Demand response" means reduced consumption of electric energy by customers from their expected consumption in response to an increase in the price of energy. FERC Chairman Jon Wellinghoff has promoted demand response as a means to create more efficient wholesale energy markets and "reduce the need for putting in very expensive, polluting, peaking generation units." See, e.g., "Resolved: Using Nuclear and Coal Power in an Environmentally Friendly Manner Is the Path Forward in Controlling Climate Change," *The Environmental Forum*, Vol. 27, No. 1 at 50 (Jan/Feb 2010).

Because wholesale energy markets originally were designed to compensate energy production rather than energy reduction, FERC's challenge was to figure out how to properly compensate parties willing to reduce consumption. Under the new rule, demand response resources will be paid the same locational marginal price ("LMP") that RTOs and ISOs pay for generation, but only if their energy reductions result in a net benefit—i.e., the reduced LMP resulting from dispatching the demand response resource exceeds the cost of paying LMP to that resource. Accordingly, the rule directs RTOs and ISOs to develop a mechanism to determine the price level at which the dispatch of demand response resources will be cost-effective. The price threshold must be based on historical data and updated monthly.

The new rule is FERC's most comprehensive effort to date to effectuate the Energy Policy Act of 2005's mandate to eliminate unnecessary barriers to demand response participation in the organized markets. However, the new rule is opposed by some in the electric industry. A variety of groups have filed petitions with FERC seeking rehearing of the final rule.

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■ **ACCESS TO RARE EARTH MATERIALS PRESENTS A GROWING THREAT TO “GREEN” SUPPLY CHAINS**

Executives in all green technology companies, and in many other industries, should be aware of the importance of rare earth materials and increasing concerns regarding their availability to manufacturers. Rare earth materials are a group of 15 to 17 elements on the periodic table used in the production of a wide variety of modern technologies, including wind turbines, electric vehicles, solar cells, and energy efficient lighting. They are commonly found throughout the world but are rarely mined due to cost and radioactive waste resulting from their production. The U.S. was the primary producer of these elements in the 1990s, but production stopped in 2002 due to severe price competition and environmental concerns. China now has a near monopoly on rare earth material production, accounting for more than 97 percent of global production.

As climate change risks create more demand for greenhouse gas emission reductions, many of these technologies are experiencing greater market demand. Worldwide demand for rare earth materials is about 125,000 tons per year. The amount needed varies between products but is significant for green technology products. For example, magnets in state-of-the-art wind turbines require a ton of rare earth elements, and hybrid vehicles require between 20 and 30 pounds. Without rare earth materials, manufactured goods, such as laptops, cell phones, and wind turbines, would be much bigger and heavier.

However, reliance on China for the supply of rare earth materials creates uncertainty about the availability of such materials. Just as demand is increasing, driven by such green technologies as hybrid car engines and wind turbines, access to a reliable supply of rare earth materials is decreasing. China has restricted the export of such materials for many years. China reduced exports 35 percent for the first half of 2011, which followed a 40 percent reduction in 2010, and it recently

indicated it would completely ban the export of dysprosium and terbium (which are vital to wind turbines) but subsequently backed off this policy.

China has also shown a willingness to use access to rare earth materials as a tool in diplomatic disputes. Last year, in response to Japan's seizure of a Chinese fishing vessel in disputed waters, China reportedly froze all exports of rare earth materials to Japan, a major importer of such materials.

Many experts believe China wishes to keep its rare earth materials to support and attract domestic manufacturing. China states it needs time to clean up its mining operations and support its growing domestic demand. In fact, one Chinese official recently predicted China will need to import some rare earth materials to meet domestic demand.

Limitations on access to rare earth materials have far-reaching implications throughout the global supply chain as export tariffs, shrinking export quotas, and increasing demand likely will cause price increases that ripple throughout the supply chain. The ability of producers to bring cost-effective emissions-reducing technologies to market could be greatly affected. In response, industry is searching for sources outside of China, but such efforts face the challenge that it takes seven to 15 years to start a rare earth mine in the U.S., largely due to the requirements of state and federal regulators.

Alarmed by China's tight control over the supply of rare earth materials, Congress has recently considered legislation promoting increased domestic production. During the 111th Congress, the Rare Earths Supply-Chain Technology and Resources Transformation Act of 2010 ("RESTART Act") was introduced into both houses of Congress to boost domestic production. Sen. Murkowski (R-AK) sponsored S. 3521, and Rep. Coffman (R-CO) sponsored H.R. 4866. Both bills died in committee.

In the current Congress, Rep. Miller (D-NC) has introduced H.R. 952, which would authorize the Department of Energy to issue loan guarantees to companies with new processing and refining technologies for rare earth materials to spur private investment. Additionally, Rep. Boswell (D-Iowa) and Sen. Udall (D-CO) have introduced bills, H.R. 618 and S. 383,

that also aim to promote the domestic supply of rare earth minerals.

Legislators have also been lobbying the Executive Branch to take action to ensure adequate access to rare earth materials. In July 2010, 20 senators signed a letter to Energy Secretary Chu urging him to approve loan guarantee applications for the production of such materials. Additionally, in March 2011, Rep. Coffman, with 27 other representatives, sent a letter to U.S. Trade Representative Ron Kirk demanding he file a complaint with the World Trade Organization against China's policy of export quotas on rare earth materials. The U.S. has threatened to file such a complaint, and to help prepare for a possible case, has asked business groups and labor unions to provide evidence that China is restricting access to such materials.

Because of these market uncertainties, companies that manufacture emission-reducing green technologies face a growing challenge in securing these essential materials. To address such risks, green technology executives should be closely evaluating their supply chains, identifying and securing alternative sources, and preparing to deal with price increases and supply disruptions.

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■ CERES CLAIMS SEC GUIDANCE HAS HAD LIMITED IMPACT ON CLIMATE CHANGE DISCLOSURES

A coalition of investors, environmental groups, and others issued a report in February 2011 that sought to evaluate how well companies reported climate change information in their most recent 10-K filings in light of guidance issued by the Securities and Exchange Commission last year. The report, entitled "Disclosing Climate Risks & Opportunities in SEC Filings," concludes that improvements in climate change disclosures were "incremental at best."

As discussed previously in *The Climate Report*, the SEC issued an "interpretive release" providing guidance on the

Commission's existing disclosure requirements as they apply to climate change matters. 75 Fed. Reg. 6290 (February 8, 2010). The guidance listed four topics as examples of how climate change may trigger disclosures under existing SEC rules, consisting of the (1) impact of legislation and regulation; (2) impact of international accords; (3) indirect consequences of regulation; and (4) physical impacts. Considering these four topics, the CERES report identified specific companies and rated them as "poor," "fair," "good," or "excellent" based on their 10-K disclosures in 2009, the most recent year of available 10-Ks. Overall, the report found that disclosures rated "good" were rare, and there were no instances of "excellent" disclosures.

The CERES report also evaluated disclosures related to three other topics in the context of SEC disclosure regulations and the recently finalized ASTM climate change reporting standard (No. E2718-10 - "Standard Guide for Financial Disclosure Attributed to Climate Change"), consisting of: (1) climate change litigation; (2) greenhouse gas emissions; and (3) strategic analysis of climate risks. The second topic addresses the volume of greenhouse gas emissions, which is one of the more unsettled climate change disclosure issues. The report noted that while the SEC guidance does not address when disclosure of greenhouse gas emissions is required under the materiality standard, the guidance does suggest that quantification of greenhouse gas emissions may be necessary to determine a company's exposure to climate risk.

The CERES report gave one company a "fair" rating for its disclosure of greenhouse gas emissions and two companies "good" ratings for their disclosures. It gave one company a "good" rating based upon the company's analysis of climate risks. The report also includes an 11-point checklist to help companies improve disclosures.

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■ REPORT ON THE IMPLICATIONS OF CLIMATE CHANGE ON INVESTMENTS

The corporate consulting company Mercer, in collaboration with institutional investors, industry groups, other consultants, and individuals, issued a report in February 2011 analyzing the impact of climate change on institutional investment portfolios. The report, entitled "Climate Change Scenarios—Implications for Strategic Asset Allocation," also offers a series of factors to consider in making investment allocation decisions.

The report evaluates asset allocation and investment issues under four different scenarios, ranging from the status quo with little action to address climate change, to an aggressive response with a high degree of economic transformation across the global economy. Key findings include the following: (1) private sector response to climate change may produce a substantial number of new investment opportunities in low carbon technologies, in the range of \$3 trillion to \$5 trillion by 2030; (2) the cumulative economic cost of changes to the physical environment, health, and food security could be in the range of \$2 trillion to \$4 trillion by 2030; (3) asset allocation to sustainable equities, efficiency/renewable assets, timberland, and agriculture land could improve portfolio resilience; and (4) the health impacts and population migration risks of climate change are underestimated.

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■ THEFTS OF EU ALLOWANCES ILLUSTRATE LEGAL RISKS AND CONSEQUENCES OF THE CARBON MARKET

On January 19, 2011, following a series of cyber attacks the preceding week on a number of national emissions registries, in particular those of Austria, the Czech Republic, Estonia, Greece, and Poland, the European Commission suspended transactions in all registries within the European Union's Emission Trading System ("EU ETS").

An estimated €30 million (\$41 million) worth of European Union carbon emission allowances, known as EUAs, were stolen in January, when criminals fraudulently transferred around two millions EUAs, which were then swiftly sold on the spot market and dispatched in multiple accounts in several EU jurisdictions. The thefts were apparently the result of computer hacking ("Trojan attacks") and theft of passwords ("phishing"), all facilitated by somewhat light identification requirements for market participants.

A phased resumption of trading on the registries has occurred, allowing countries meeting IT security criteria (similar to those mandated for other sensitive IT systems such as electronic banking) set by the Commission to resume operation, while other countries remain suspended until further notice. As of April 20, 2011, 28 European national registries had resumed normal operations.

In response to the Commission's suspension of transactions in the registries, many stakeholders, such as the European Federation of Energy Traders and the International Emissions Trading Association, requested a complete explanation of what had happened and detailed plans to prevent further circulation of stolen EUAs, together with a list of alleged and confirmed stolen EUAs. In the absence of such list, market participants would be exposed to significant and continuing uncertainty when acquiring EUAs on the spot market.

The Commission's draft communication, entitled "Towards enhanced market oversight framework for the EU Emissions

Trading Scheme," and related discussion papers address approaches to enhance market security. On February 23, 2011, the Commission declared that it would propose amendments to Regulation (EC) No. 994/2008, governing the carbon trading registries in the European Union, to respond to the recent thefts, and it held a "stakeholders' meeting" on March 15, 2011 to discuss the matter. The EC has also declared that it is contemplating use of a delivery delay mechanism for the transfer of EUAs, to increase the likelihood of stopping fraudulent transfers before they are completed. The issues will be discussed at the European Climate Change Programme stakeholders' meeting in May 2011.

While a portion of the stolen EUAs have been identified and returned to their legitimate owners, the majority are still missing and probably held by good-faith buyers who acquired them on the spot market. Market participants may well be tempted to carry on with business as usual, acquiring or transferring EUAs, possibly including contested EUAs. However, such activities would raise a risk of loss or liability because, as pointed out by the Commission, the recovery of stolen allowances is a matter of national law and enforceable on a jurisdiction-by-jurisdiction basis. Some EU countries treat the mere selling of stolen allowances as a potential criminal offense.

In addition, the legal remedies and actions available to a good-faith buyer of stolen EUAs in respect of the seller (in particular if such seller also purchased the EUAs in good faith) depend largely on the laws in the relevant jurisdiction. To address the problem of differing legal regimes, some market players are now requesting the establishment of a global compensation mechanism, so that those that purchase stolen EUAs in good faith can return them to the authorities for replacement EUAs or financial compensation. Various legal proceedings are said to have been started in relation to the thefts.

A list of contested EUAs has already been published by some exchanges. Indeed, the recent Intercontinental Exchange ("ICE") Circular No. 11/038 of March 10, 2011 provides for new delivery procedures for EUAs and other carbon credits. Pursuant to this circular, ICE will maintain a list of serial numbers of "prohibited" carbon credits, "which are not acceptable for delivery." Transfer of such prohibited carbon credits will

not discharge the transferor of its delivery obligations. The list of prohibited carbon credits, posted on the ICE Futures Europe web site, currently includes about three million EUAs. This blacklisting of allowances, however, raises a number of stakeholder concerns, including the need to define how allowances will be deemed to have been stolen and determining who should be liable for losses incurred due to erroneous or falsified disclosure of contested serial numbers.

Certain trading associations, including the International Swap and Derivatives Association, the European Federation of Energy Traders, and the International Emissions Trading Association, also plan to combine and harmonize their efforts to address the risks associated with stolen allowances by amending their standard form emissions trading documentation. These, and the other efforts described above, will bear watching.

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■ **RENEWABLE ENERGY PROJECT DEVELOPERS RUSH TO QUALIFY PROJECTS FOR 30 PERCENT CASH GRANT**

For many renewable project developers, the end of 2010 brought back memories of the anxiety-filled days of the so-called “PTC cliff”—when developers would race to bring projects online before the latest year-end expiration of federal production tax credits. But this time, instead of having to push wind power projects into commercial operation, developers were rushing to start construction of their wind and solar projects before year-end to qualify for valuable cash grants from the Department of Treasury under an expiring program in the 2009 American Recovery and Reinvestment Act (“ARRA”).

Generally, under Section 1603 of the ARRA, renewable project owners could receive a Treasury cash grant, in an amount

equal to 30 percent of eligible project costs, as long as the project “commenced construction” prior to the end of 2010. A last-minute one-year extension of the cash grant program brought a collective sigh of relief from renewable project developers, but such relief is almost certain to be short-lived, as prospects appear dim for a further extension of the program. Absent another extension, the various methods devised by developers to qualify their projects under the cash grant program will surely be revisited for projects expected to enter the construction phase in 2011.

Jones Day was involved in several solar and wind power projects in late 2010 that sought to qualify for a Treasury cash grant. For example, the Firm advised KeyBank National Association on a \$24 million project financing for Western Wind Energy Corp.’s proposed 10.5 MW combined wind and solar power facility in Kingman, Arizona. The Kingman project, consisting of 10 MW of wind energy and 500 kW of solar photovoltaic (PV) capacity, is believed to be one of the first “hybrid” wind and solar energy projects to reach financial close in the U.S.

The senior financing package included a \$16 million, one-year construction loan, convertible into a seven-year term loan at commercial operation, and a \$4.2 million bridge loan to be repaid with the proceeds of the Treasury cash grant. The KeyBank loans are secured by a first priority lien on the assets of the borrower/project owner (a wholly owned subsidiary of Western Wind), including all cash grant proceeds. The package also included a \$4 million subordinated loan provided by a vendor, secured by a second lien on the cash grant proceeds and other assets of the borrower. Tucson Electric Power Company, a subsidiary of Unisource, is purchasing all of the energy and renewable energy credits from the Kingman project under a 20-year power purchase agreement.

Western Wind considered a variety of options for qualifying for the Treasury cash grant, based on the Treasury’s published guidance on what it means to “commence construction” of the renewable energy project. One method for a developer to satisfy the “commenced construction” requirement under the guidance (referred to as having begun “physical work of significant nature”) generally relies on actions,

backed by contractual representations, from equipment vendors or construction service providers either to begin to fabricate the project's equipment or to perform substantial physical work at the project site during 2010. Ultimately, Western Wind opted to qualify by showing that the Kingman project owner and the project's wind turbine supplier had contractually agreed to begin fabricating the wind turbines prior to year-end 2010.

Under the Treasury's guidance, the second method by which to qualify for the cash grant involves a more objective, safe harbor test. Under this approach, a project qualifies for a cash grant if more than 5 percent of the project's eligible costs were paid or incurred by the project's owner (or by its contractor, under a binding written contract) prior to the end of 2010. For example, Jones Day represented Chevron Energy Solutions Company ("CES") in connection with its design and construction of approximately four MW of solar PV energy facilities at three campuses of the Los Angeles Community College District.

Citibank N.A., the owner and lessor of each solar project, required CES to demonstrate that it had paid or incurred in 2010 costs relating to each project equal to at least 5 percent of such project's costs. CES met this obligation by making payments in the required amounts to the PV solar panel vendor in December 2010. CES and the vendor carefully documented the arrangements for the purchase, payment, and delivery of equipment to the each project site (which had to occur within three and a half months of payment for the payment to qualify as having been "incurred" in 2010) to comply with the Treasury's guidance.

The "physical work of significant nature" test is somewhat subjective and presents a number of commercial, legal, and technical challenges to ensure it has been met. Most renewable project developers have opted to qualify their projects for the Treasury cash grant using the alternative "5 percent safe harbor" method.

Given growing doubts that Congress will pass energy policy legislation in 2011, many renewable project developers fear that the Section 1603 cash grant program will end this year. Developers' biggest fear is that the market for energy tax

credit investing, though recovering, may not have the depth to provide the capital necessary for projects that are not due to enter construction until 2012. It is likely, therefore, that developers will be dusting off their Section 1603 compliance strategies in another push to "commence construction" of those projects by year-end 2011.

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■ EPA EXPANSION OF E15 WAIVER VEHICLES DRAWS ADDITIONAL LEGAL CHALLENGES

We previously reported on industry challenges to U.S. EPA's grant of a partial waiver under the Clean Air Act allowing the use of gasoline containing up to 15 percent ethanol by volume ("E15") in model year 2007 and newer light-duty vehicles (*i.e.*, cars, light-duty trucks, and medium-duty passenger vehicles). Additional challenges were filed recently in the U.S. Court of Appeals for the D.C. Circuit after EPA extended the waiver to allow the use of E15 in model year 2001 to 2006 light-duty vehicles. "Partial Grant of Clean Air Act Waiver Application Submitted by Growth Energy to Increase the Allowable Ethanol Content of Gasoline to 15 Percent; Decision of Administrator," 76 Fed. Reg. 4662.

The first petition for review was filed February 16, 2011, *Alliance of Auto. Mfrs. v. U.S. Env'tl. Prot. Agency*, No. 11-1046 (D.C. Cir.); another was filed March 11, 2011, *Grocery Mfrs. Ass'n v. U.S. Env'tl. Prot. Agency*, No. 11-1072 (D.C. Cir.); and a third was filed on March 21, 2011, *Nat'l Petrochemical & Refiners Ass'n. v. U.S. Env'tl. Prot. Agency*, No. 11-1086 (D.C. Cir.). On its own motion, the Court of Appeals consolidated the three new cases with the three existing cases challenging the partial waiver for model year 2007 and newer vehicles.

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■ SUPREME COURT HEARS ORAL ARGUMENT IN GREENHOUSE GAS NUISANCE CASE

Although there have been numerous lawsuits filed challenging U.S. authority to promulgate and implement regulations governing greenhouse gas emissions, perhaps the most significant, and most watched, pending climate change case is *American Electric Power Co. v. Connecticut*, No. 10-174, argued April 19, 2011 before the U.S. Supreme Court.

The Court's decision is expected to address the question of whether states and private land trusts can bring federal common law nuisance actions against utility companies for their alleged contribution to climate change through greenhouse gas emissions.

In *American Electric Power Co.*, eight states, New York City, and three private land trusts filed a suit against a group of electric utilities in the U.S. District Court for the Southern District of New York. The District Court dismissed the lawsuit in 2005, holding that the claims were non-justiciable "political questions" that could not properly be adjudicated by the courts. *See Connecticut v. American Electric Power Co.*, 406 F. Supp. 2d 265 (S.D.N.Y. 2005). In 2009, the U.S. Court of Appeals for the Second Circuit reversed. 582 F.3d 309 (2d Cir. 2009). The U.S. Supreme Court granted a writ of certiorari on December 6, 2010.

On January 31, 2011, Petitioners (*i.e.*, the utility company defendants) filed their opening brief. In their brief, the utilities (American Electric Power Co., Duke Energy Corp., Southern Co., and Xcel Energy Inc.) first argue that Respondents (*i.e.*, the states, city, and private land trusts) lack standing to sue under Article III of the U.S. Constitution. Specifically, Petitioners argue that the particular harms allegedly incurred by Respondents, and the effects of climate change more generally, are not traceable to Petitioners' conduct, because climate change is gradually induced by an undifferentiated mixture of emissions released by billions of independent actors.

Petitioners also assert that the redress sought by Respondents—judicial imposition of emission caps on five utilities—would have no effect on climate change or Respondents' alleged injuries. Petitioners further argue that there is no reason for the Supreme Court to relax standing requirements in this case, because such relaxed standards are available only where Congress has statutorily created an enforceable legal right, a circumstance not presented in Respondents' federal common law suit.

In addition to arguing that Respondents lack standing on Article III grounds, Petitioners claim that Respondents also lack standing based on prudential considerations. According to Petitioners, finding standing under the facts alleged in this

case would allow future suits by, and against, virtually any enterprise on the planet for any injury arising from climatological or meteorological events. Rather than unleashing a deluge of nuisance-based climate change suits, it should be left to Congress to create statutory standards. Until then, courts are ill-equipped to adjudicate such “generalized grievances.”

Petitioners offer several alternative bases for dismissing Respondents’ claims. Petitioners assert that federal courts lack the power to create a federal common law cause of action in the absence of either statutory authorization or constitutional exigency, neither of which exists with respect to global climate change. Petitioners also argue that the provisions of the Clean Air Act displace any federal common law cause of action. By enacting the Clean Air Act and delegating authority to U.S. EPA, Congress directly addressed the issue of greenhouse gas emissions, regardless of any regulatory action to target the types of emissions released by Petitioners.

Finally, Petitioners argue that Respondents’ claims are non-justiciable political questions. In awarding the type of remedy desired by Respondents, a court would be required to make predictions about, and inquire into, the behavior of every sector of the national and international economies, while simultaneously balancing interests outside the court’s expertise.

Also on January 31, 2011, the Department of Justice filed a brief on behalf of Tennessee Valley Authority, a utility corporation owned by the U.S. government. The federal government’s brief supports Petitioners’ position that the Second Circuit’s decision should be reversed and the complaint dismissed on the narrow ground of a lack of prudential standing. The TVA brief states that Respondents’ allegations would otherwise be sufficient to survive dismissal for lack of standing under Article III but argues that the lack of prudential standing means the court need not reach that issue to decide the case.

The TVA brief also takes the position that Respondents’ claims do not fall within the ambit of non-justiciable political questions because the case does not implicate separation of powers concerns but asserts that the Clean Air Act and U.S. EPA’s recently promulgated greenhouse gas regulations

(*e.g.*, endangerment finding and PSD tailoring rule) displace any federal common law cause of action.

The Supreme Court’s announcement setting oral arguments for April 19, 2011 coincided with a flood of amicus briefs, predominantly opposing the Second Circuit’s decision, onto the case’s docket. Among the parties that filed briefs in support of Petitioners were 23 state attorney generals, the United States Chamber of Commerce, the Cato Institute, and Rep. Fred Upton (R-MI), the current Chair of the House Energy Committee.

On March 11, 2011, the state Respondents (joined by New York City) filed their response brief. In their brief, the states maintain that the allegations in their complaint are sufficient to establish Article III standing. According to the state Respondents, the complaint alleges particularized injuries caused by climate change, including injury to natural resources and public health; alleges a “substantial contribution” by Petitioners to climate change; and seeks relief (*i.e.*, emission caps) that would reduce the degree and likelihood of harm. State Respondents also contend that because the case is at the motion to dismiss stage, generalized allegations of harm should suffice. As for prudential standing, state Respondents assert that there is no separate test for prudential standing apart from that needed to satisfy Article III requirements.

State Respondents further dispute that their claims raise non-justiciable political questions, asserting that the political question doctrine is limited to situations in which the judiciary would interfere with matters committed to Congress and the Executive Branch, a circumstance not present in the context of common law causes of action. Finally, state Respondents argue that federal common law governs the public nuisance claims and such claims are well-settled in federal common law as part of the federalist system, in which states relinquished their right to use force to abate nuisances emanating across borders. Further, according to state Respondents, the Clean Air Act does not displace federal common law because the statute fails to impose any limits on carbon dioxide emissions from stationary sources like those operated by Petitioners.

In their response brief, the land trust Respondents proffer nearly identical arguments to those raised by the state Respondents. However, the land trust Respondents highlight the historical underpinnings of public nuisance claims, including the role of public nuisance actions as a means of addressing then-novel public health and public safety concerns in the era preceding the enactment of the major environmental statutes.

On April 11, 2011, Petitioners filed their reply briefs, and oral argument was held on April 19, 2011. A decision in the case is expected before the Supreme Court recesses for the summer.

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■ **EU ADOPTS RULES FOR AUCTIONING GREENHOUSE GAS EMISSION ALLOWANCES**

The EU ETS Directive, which established the European Union's cap and trade program for greenhouse gas emissions, as amended by Directive 2009/29/EC of April 23, 2009, provides that from 2013 onward, EU Member States shall auction all allowances that are not allocated free of charge to stationary sources based in the EU (the aviation sector follows different rules). Such full auctioning is a significant change from the first two trading periods (2005–2012) under the EU ETS, in which allowances were allocated for free.

The EU's full auctioning principle is subject to several exceptions. One exception is for certain types of stationary activities, such as district heating, high efficiency cogeneration, or facilities in business sectors and sub-sectors exposed to a significant risk of carbon leakage (listed in Commission Decision 2010/2/EU of December 24, 2009). In addition, certain electricity production facilities are subject to a transitional free allocation of allowances. Further, the EU has established a reserve of 300 million allowances for new entrants, which is intended to stimulate investment in carbon capture and geological storage projects and in innovative renewable energy technologies in the EU.

At least 50 percent of the revenue generated by the auctioning system is to be dedicated to financing climate-related action, including innovative projects, as agreed during the last European Council of February 4, 2011.

On November 12, 2010, the EU Commission adopted Regulation No 1031/2010 on the timing, administration, and other aspects of auctioning of greenhouse gas emission allowances pursuant to the EU ETS Directive. The Regulation lays down practical and technical rules for the implementation of allowance allocation through auctioning to both aircraft operators and stationary sources.

The Regulation provides that emission allowances shall be offered for sale on an auction platform by means of standardized electronic contracts, known as “auctioned products,” which should mainly take the form of either two-day spots or five-day futures. Both such products will be traded on a single auction platform common to the EU Member States. The Regulation also provides for the possibility to create additional platforms for other allowed auctioned products, such as futures and forwards.

Common platforms will be designated for a maximum of five years, with a common auctioning infrastructure. The choice of a common platform aims to avoid distortions of the internal market and permit allocation of allowances on the basis of fully harmonized conditions. A common infrastructure is expected to be more cost-effective, ensure the predictability of the auction calendar, provide the strongest and clearest carbon price signal, and allow equitable access to small and medium-sized enterprises covered by the EU ETS. Because certain national auction platforms have already been created (such as in Germany and the United Kingdom), EU Member States may opt out of the common auction platform by appointing their own platforms, which should nevertheless be coordinated with the calendar for the common platform.

An auction monitor will control each auction and report to the Commission and EU Member States on the proper implementation of auctions conducted in the preceding month. In addition, each Member State must appoint an auctioneer who will be responsible for the auctioning of allowances, receipt of auction proceeds, and disbursement of such proceeds on behalf of that Member State.

Broad market access is provided to encourage wide participation and thereby ensure competitive auction outcomes. Admission to the auctions will be available to operators of stationary installations and aircraft operators covered by the EU ETS, business groups of such operators (such as partnerships, joint ventures, and consortia acting as agents on behalf of their members), as well as regulated financial entities (such as investment firms and credit institutions). In light of the recent series of successful cyber attacks on national EU ETS allowance registries, ensuring the security of the new auction platform and auctioned products will be a key concern for EU institutions.

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■ UK'S DEPARTMENT FOR ENERGY AND CLIMATE CHANGE PUBLISHES DRAFT “CARBON PLAN”

The United Kingdom's Department for Energy and Climate Change (“DECC”) has published a draft “Carbon Plan,” setting out the UK government's plan of action on climate change for the next five years. The plan is open for consultation with a view to publishing a final version in autumn 2011, after which it will be updated annually.

The Carbon Plan represents ongoing and planned cross-government action with specific deadlines providing for both internal accountability and public transparency. Setting out a vision for moving to a low-carbon economy, the Plan focuses on jobs and economic opportunities and on policies that aim to help insulate the UK from future energy price shocks.

The Plan takes account of the UK's first three five-year “carbon budgets” (covering the period from 2008 to 2022), which have already been set pursuant to the UK's Climate Change Act 2008. DECC has announced that “in recognition that the fourth carbon budget (2023-2027) will be set in law in June 2011, we will publish an updated ‘live’ Carbon Plan in October which takes the four carbon budgets into account.”

The Carbon Plan consolidates various strands of energy and climate change policy into a road map that will be updated as policies arise. The intention is for a quarterly update on progress against actions, with the Plan being published on the Prime Minister's “Number 10” web site.

The Carbon Plan highlights three key changes that would be required across the UK economy:

1. A dramatic shift away from fossil fuels and toward low carbon alternatives in the way that electricity is generated,

including renewable, nuclear, and fossil fuel power stations fitted with carbon capture and storage;

2. A step change in the way homes and businesses are heated and how they are insulated, away from gas boilers to low carbon alternatives such as heat pumps; and
3. A step change in the way people travel, with more people using public transportation and finding substitutes for some journeys. The greatest change would be to road transport, reducing emissions from petrol and diesel engines and moving toward alternative technologies such as electric vehicles.

A range of actions and deadlines that government departments will need to meet are set, including:

- Legislation to create a floor price in carbon brought forward, as appropriate, by April 2011;
- The award of a contract by DECC for the first UK carbon capture and storage demonstration by the end of 2011, together with the identification of further demonstration projects by May 2012;
- A new green investment bank made operational by the Department of Business by September 2012;
- Development by the Department for Transport, by June 2011, of a nationwide strategy to promote the installation of electric vehicle infrastructure;
- A 10 percent reduction in the central government's annual greenhouse gas emissions by May 2011; and
- The launching by the Department for Environment Food and Rural Affairs of a project to develop and trial methods of delivering integrated advice on farming, including advice on reducing greenhouse gas emissions.

Commentators have already suggested that the draft Carbon Plan includes little detail on specific policy mechanisms and almost a total absence of quantitative data. Responses to the draft Plan should be sent to CarbonPlan@dcc.gsi.gov.uk by July 31, 2011.

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