

THE CLIMATE REPORT



INITIALLY...

■ SUPREME COURT HOLDS THAT CLEAN AIR ACT DISPLACES FEDERAL COMMON LAW ON GREENHOUSE GAS EMISSIONS

On June 20, 2011, the United States Supreme Court issued a decision barring state and private parties from bringing federal common law nuisance actions based on alleged contribution to climate change through greenhouse gas emissions. *American Electric Power Co. v. Connecticut*, 546 U.S. ____ (2011). The Court held 8–0 that the federal Clean Air Act displaces any federal common law cause of action that may have existed against greenhouse gas emitters. Justice Sotomayor recused herself from the case, having previously served on the panel that heard oral arguments in the case when it was before the U.S. Court of Appeals for the Second Circuit.

In *American Electric Power Co.*, eight states, the city of New York, and three private land trusts originally filed suit against a group of utility companies 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 nonjusticiable political questions that could not properly be adjudicated by federal courts. See *Connecticut v. American Electric Power Co.*, 406 F. Supp. 2d 265 (S.D.N.Y. 2005). In 2009, the Second Circuit reversed. 582 F.3d 309 (2d Cir. 2009). The Supreme Court granted certiorari on December 6, 2010, and oral arguments were held on April 19, 2011.

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Writing for the Supreme Court, Justice Ginsburg first addressed the claim that the federal courts lacked the authority to hear the case. On the question of plaintiffs' Article III and prudential standing, the Court was equally divided. Four members of the Court concluded that at least some of the plaintiffs had Article III standing and that neither prudential standing nor political question considerations would bar a court from asserting jurisdiction over the case, while four other justices held a contrary view. The 4–4 tie resulted in a nonprecedential affirmance of the Second Circuit's exercise of jurisdiction.

On the merits, the Court began by noting that federal common law, in the past, had provided a cause of action “by one State to abate pollution emanating from another State,” but recognized that the Supreme Court had never decided whether private citizens or political subdivisions of a state could “invoke the federal common law of nuisance to abate out-of-state pollution.” The Court elected not to reach the issue of whether such a federal common law cause of action could exist, because such a claim would be displaced by the Clean Air Act, which the Court, in *Massachusetts v. EPA*, 549 U.S. 497 (2007), held authorizes U.S. EPA to regulate greenhouse gas emissions.

Justice Ginsburg began her displacement analysis by discussing the boundaries of statutory displacement of federal common law causes of action. Unlike preemption of state law, displacement does not rest on legislative intent. Rather, the focal point of displacement analysis is whether Congress has enacted legislation that “speaks directly to the question at issue.” Justice Ginsburg concluded that the various statutory provisions of the Clean Air Act governing pollutant emissions from existing stationary sources covered the very type of emitters that plaintiffs had sought to enjoin in the instant case. Accordingly, the Court held that:

[T]he Clean Air Act and the EPA actions it authorizes displace any federal common law right to seek abatement of carbon-dioxide emissions from fossil-fuel fired power plants. *Massachusetts* made plain that emissions of carbon dioxide qualify as air pollution subject to regulation under the Act.... And we think it equally plain that the Act “speaks directly” to emissions of carbon dioxide from the defendants' plants.

The Supreme Court also rejected the Second Circuit's rationale that EPA must actually exercise its regulatory authority for displacement to occur. Relying on *Milwaukee v. Illinois*, 451 U.S. 304 (1981), the Court reaffirmed that the proper test for displacement is legislative occupation of the field. The EPA's decision to regulate or not to regulate greenhouse gas emissions is immaterial: “The critical point is that Congress delegated to the EPA whether and how to regulate carbon-dioxide emissions from power plants; the delegation is what displaced federal common law.”

Although the Court explicitly eschewed the question of whether the Clean Air Act also preempts state law nuisance claims, the opinion highlighted several reasons why courts are ill-suited to set emission standards by judicial fiat. Picking up on one of the petitioners' arguments, the Court noted that regulation of greenhouse gas emissions requires a careful assessment of competing economic and social interests. An expert agency is entrusted with performing this complex balance, because “federal judges lack the scientific, economic, and technological resources an agency can utilize in coping with issues of this order.... Judges may not commission scientific studies or convene groups of experts for advice, or issue rules under notice-and-comment procedures inviting input from any interested person, or seek the counsel of regulators in the States where the defendants are located.” However, noting that none of the parties had briefed preemption or otherwise addressed the availability of state nuisance claims, the Court remanded the case for further consideration of this issue.

Justice Alito wrote an opinion, which Justice Thomas joined, concurring in part and concurring in the judgment agreeing with the Court's displacement analysis on the assumption that the Court's interpretation of the Clean Air Act in *Massachusetts v. EPA* was correct.

What Happens Next? The Supreme Court's decision will certainly have ramifications for other pending climate change litigation. For example, in *Native Village of Kivalina v. ExxonMobil Corp.*, 663 F. Supp. 2d 863 (N.D. Cal. 2009), a native Alaskan village brought a suit against two dozen defendants (including some of the same utilities named as defendants in *American Electric Power Co.*) alleging that severe weather generated by climate change caused injuries

related to coastal erosion. Unlike *American Electric Power Co.*, the *Kivalina* case seeks damages rather than injunctive relief. The district court dismissed the case as involving a nonjusticiable political question and for lack of standing. The village appealed to the Ninth Circuit Court of Appeals. While the *American Electric Power Co.* decision should mandate affirmance for lack of a federal common law cause of action, the *Kivalina* appellants have requested an opportunity to brief the impact of the Supreme Court's decision.

Meanwhile, the plaintiffs in *Comer v. Murphy Oil USA* refiled their suit in the Southern District of Mississippi on May 27, 2011. The case was previously dismissed by the district court, and plaintiffs' appeal was dismissed by the Fifth Circuit Court of Appeals. *Comer v. Murphy Oil USA*, 607 F.3d 1049 (5th Cir. 2010). A petition for a writ of mandamus to the Supreme Court also was denied. *In re Comer*, U.S. No. 10-294 (Jan 10, 2011). No answers or responsive motions have yet been filed in the refiled case, as plaintiffs are still attempting to effectuate service or process on the numerous defendants against whom they assert federal and state common law claims.

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■ **EPA ISSUES CONFIDENTIALITY RULE FOR CERTAIN GREENHOUSE GAS DATA FROM COMPANIES**

On May 26, 2011, the United States Environmental Protection Agency issued a final rule setting forth confidentiality determinations for certain types of data required under EPA's Greenhouse Gas Reporting Program, codified at 40 C.F.R. Part 98. The new rule includes final Part 98 amendments that allow EPA to release or withhold greenhouse gas data in accordance with those confidentiality determinations. Data deemed entitled to confidential treatment under the new rule will not be publicly available after emitters submit the first round of greenhouse gas reports to EPA on September 30, 2011, except in an aggregate format not attributable to specific reporting entities.

EPA evaluated whether various data categories are likely to cause substantial harm to a reporting entity's competitive position, if released to the public. EPA decided that data in some categories, such as data on production, throughput, and raw materials consumed by direct emitters, should be entirely confidential. Other data categories, like unit and process operating characteristics, were deemed to contain both confidential and nonconfidential information. Still other categories, including emissions data that is prohibited from confidential treatment under the Clean Air Act, were deemed entirely nonconfidential. A detailed list of the data required under Part 98, along with U.S. EPA's confidentiality determinations, is available in a memorandum included in the rulemaking docket.

The new rule does not include any confidentiality determinations for inputs to emission equations. EPA has issued a proposal to defer the reporting of emission equation inputs until March 31, 2014, to allow time for consideration of public comments that disclosure of such information would reveal trade secrets and strategic commercial information. Although EPA is still considering these comments, the new rule

narrowed the scope of the data considered emission equation inputs by reassigning certain data elements that are not actual inputs to any Part 98 emissions calculations. Where such data elements were reassigned, the new rule will apply the final confidentiality determination for the newly assigned data category.

The final rule establishes how EPA will treat data submitted by all but the following eight types of reporting entities: Electronics Manufacturing (Subpart I); Fluorinated Gas Production (Subpart L); Petroleum and Natural Gas Systems (Subpart W); SF6 and PFCs from Electrical Equipment at an Electric Power System (Subpart DD); Importers and Exporters of Fluorinated Greenhouse Gases in Pre-Charged Equipment or Closed-Cell Foams (Subpart QQ); Geologic Sequestration of CO2 (Subpart RR); SF6 and PFCs from Electrical Equipment Manufacture and Refurbishment (Subpart SS); and Injection of CO2 (Subpart UU). EPA plans to repropose and finalize confidentiality determinations for these subparts before the March 31, 2012 reporting deadline.

For additional background on EPA's Greenhouse Gas Reporting Program, view our recorded webcast, "Beyond Cap and Trade: Climate Change Regulation Under the Clean Air Act Arrives," available at www.jonesday.com/beyond-cap-and-trade/.

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■ PHASE II OF THE TAILORING RULE EXPANDS UNIVERSE OF SOURCES SUBJECT TO GREENHOUSE GAS PERMITTING

As of July 1, 2011, Phase II of the EPA tailoring rule became effective. As a consequence, the construction or modification of major sources of greenhouse gas air emissions may now require prevention of significant deterioration ("PSD") pre-construction permits and/or Title V operating permits based solely on their greenhouse gas emissions. During Phase I, which ran from January 2, 2011 until July 1, 2011, covered

sources were required to obtain only PSD or Title V permits addressing greenhouse gas emissions if such permits were otherwise required based on the source's emissions of regulated air pollutants other than greenhouse gases.

For PSD permitting purposes, this means that, regardless of the emission of other pollutants, a PSD permit is now required for (a) the construction of any source with the potential to emit greenhouse gases exceeding both the applicable statutory threshold of 100 or 250 tons per year ("tpy") (without applying carbon dioxide equivalencies) and 100,000 tpy on a carbon dioxide equivalency basis; or (b) the modification of any existing major source of greenhouse gases that will increase the source's potential to emit greenhouse gases by 75,000 tpy of carbon dioxide equivalents or more. For Title V permitting purposes, this means that a Title V permit is now required for any source with the potential to emit 100 tpy of greenhouse gases (without applying carbon dioxide equivalencies) and the potential to emit at least 100,000 tpy on a carbon dioxide equivalency basis.

Further information regarding the tailoring rule can be found in the Jones Day White Paper, "Climate Change Regulation Via the Clean Air Act: EPA's New Greenhouse Gas Rule for Facilities," and recorded webcast, "Beyond Cap and Trade: Climate Change Regulation Under the Clean Air Act Arrives," available at www.jonesday.com/beyond-cap-and-trade/.

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■ U.S. EPA DEFERS GREENHOUSE GAS PERMITTING REQUIREMENTS FOR SOME BIOGENIC EMISSIONS

On July 1, 2011, U.S. EPA finalized an amendment to the federal greenhouse gas permitting regulations that will temporarily exclude certain biogenic carbon dioxide emissions from consideration in determining whether a source's level of emissions trigger permitting requirements under the Prevention of Significant Deterioration ("PSD") and Title V permit programs. The deferral of regulation of carbon dioxide

emissions resulting from the combustion or decomposition of biologically based materials other than fossil fuels and mineral sources of carbon will last up to three years while EPA conducts a scientific study of the atmospheric impacts from such emissions and completes additional rulemaking based on the results of that study.

The deferral is not limited to emissions from specific categories of sources but will be of greatest benefit to landfills, wastewater treatment facilities, and manure management operations that produce significant carbon dioxide from biological decomposition, along with utilities and other facilities that burn wood, agricultural wastes, or biogas in place of fossil fuels to fuel industrial boilers. The deferral does not apply to biofuel emissions from mobile sources and does not apply to other greenhouse gases, most notably methane and nitrous oxide, often emitted when biological materials are burned or decompose.

The new rulemaking excludes biogenic carbon dioxide emissions from EPA's definition of emissions "subject to regulation" under the PSD and Title V programs, and will apply immediately upon publication in the Federal Register to sources in states that are subject to a federal implementation plan for greenhouse gas permitting and in states whose air regulations incorporate by reference the federal definition of "subject to regulation." The deferral will not apply to other state air permitting programs unless and until those states elect to amend their regulations.

The new exclusion does not apply retroactively, so permitted sources that would not have been subject to permitting if the regulation had previously been in effect must continue to comply with their existing permits. Conversely, facility construction projects that avoid PSD preconstruction permit requirements during the term of the deferral will not become subject to permitting when the deferral expires, unless and until some new activity, such as a major modification to the source, occurs.

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■ STATES WITHDRAW FROM REGIONAL CAP AND TRADE PROGRAMS

Several states have recently announced plans to withdraw from regional greenhouse gas cap and trade programs, such as the Regional Greenhouse Gas Initiative, a cooperative effort to reduce greenhouse gas emissions from utility sources in Connecticut, Delaware, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island, and Vermont. These 10 northeastern states originally agreed to cap and reduce energy sector carbon dioxide emissions by 10 percent by 2018. Although still in its early years, RGGI has come under attack for both the effectiveness of the program and its adverse impact on electrical ratepayers.

As a result, lawmakers in at least three participant states have signaled a desire to withdraw from the RGGI. In May of this year, Governor Christie of New Jersey announced that state's intention to unilaterally withdraw from the initiative. This announcement prompted a contingent of the New Jersey legislature to challenge the withdrawal legislatively, and the issue is not yet resolved.

Similar moves to withdraw have been made by legislatures in New Hampshire and Maine. House lawmakers in New Hampshire have passed two bills since March of this year in an attempt to withdraw the state from RGGI. The first bill failed to secure Senate support. While the second secured support in both houses of the legislature, Governor John Lynch vetoed the legislation on July 6, 2011. A similar effort in Maine ultimately resulted in a narrower change, clarifying that Maine's continued participation in RGGI is contingent on a minimum threshold of participation by other states in the region.

RGGI is not the only regional greenhouse gas program facing state defections. The Western Climate Initiative is designed to reduce regional greenhouse gas emissions to 15 percent below 2005 levels by 2020 among Arizona, California, Montana, New Mexico, Oregon, Utah, Washington, and several Canadian provinces. At least two of these states may soon end their involvement. In 2010, Arizona Governor Jan Brewer signed an executive order withdrawing the state from the

program. New Mexico Governor Susana Martinez has also expressed dislike of the program, which New Mexico joined under her predecessor's administration, but has not yet withdrawn her state. It remains to be seen what, if any, impact will result from the loss of participant states from these greenhouse gas programs.

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■ **PROMINENT INVESTOR GROUPS ISSUE JOINT GLOBAL INVESTOR SURVEY ON CLIMATE CHANGE**

On June 13, 2011, three large climate change investor groups issued a joint report, prepared by Mercer, analyzing global investor actions, strategies, and policies related to climate change risks and opportunities. The Report, entitled "Global Investor Survey on Climate Change: Annual Report on Actions and Progress 2010," analyzes a wide range of investment management issues as they relate to potential climate change risks and presents key findings regarding strategies, trends, and challenges for asset owners and managers. As summarized below, the Report concludes that the trend of heightened investor attention to climate change risks and opportunities continues, although in differing patterns by region. Additionally, increased investor analysis and action has occurred despite continuing challenges faced by asset owners and managers in quantifying and predicting climate change risks and opportunities, due to data gaps, data ambiguities, and regulatory uncertainty.

Three Climate Change Investor Groups Lead Research Effort. The wide variety of asset classes managed by the three investor groups that sponsored the Mercer Report, together with distinct regional differences between investors represented by each, allowed a broad look at the issues, as well as by region around the globe. To better place the survey findings into context, the following briefly describes each of the participating groups, with links to each group's web site, where additional information on the group's mission, agenda, and policies can be found:

- Based out of Europe, the Institutional Investors Group on Climate Change has 70 members representing more than \$10 trillion in managed assets.

- Based out of North America, the Investor Network on Climate Risk provides support for climate-related investment practices and disclosure policies, and it is coordinated by CERES, one of the leaders of the activist investor movement. INCR's membership represents more than \$10 trillion in managed assets.
- Based out of Australia/New Zealand, the Investor Group on Climate Change serves both to educate investors on climate change risks and to encourage awareness of these issues in investment decisions.

The range in types of assets and regions covered by these groups created a unique opportunity for Mercer to evaluate investor policies and patterns on a global scale, but with regional comparisons as well.

Findings Show Continued Trend of Heightened Investor Focus on Climate Change Issues. The study included survey results from 100 asset owners and managers with collective assets of more than \$12 trillion, with most respondents from Europe and Australia/New Zealand, and about 15 percent based in North America. The key findings reported by Mercer include the following:

- **Investor Focus:** Globally, 87 percent of surveyed asset managers and 98 percent of surveyed asset owners view climate change issues as “a material investment risk/opportunity” in their investment portfolios. (Report at 13) Consistent with these findings, Mercer reports that the majority of asset managers and owners now include provisions for climate change risk in their investment policy. Globally, investors identified real estate as the asset class facing the greatest potential impact of climate change risks on investment returns, due to extreme weather risks, as well as energy and water concerns.
- **Role of Public Policy:** The greater regulatory certainty in Europe and Australia/New Zealand (for example, established carbon pricing and markets, providing predictability in the low-carbon economy) resulted in heightened integration of climate change analysis in investor decision-making in these regions. Not surprisingly, in regions

with a less predictable regulatory atmosphere, investors often found it hard to develop methods for analyzing future climate change risks and future investment opportunities. As Mercer had concluded in an earlier study, “climate policy uncertainty could contribute to as much as 10 percent of the risk for a representative portfolio over the next 20 years,” indicating that the very uncertainty that makes risk analysis difficult further exacerbates the overall investment risk. (Report at 21) Perhaps due in part to this relationship between uncertainty and risk, the Report found that 85 percent of surveyed asset managers and 91 percent of surveyed asset owners engaged in review of at least one issue related to climate change policy in 2010. (Report at 22)

- **Key Challenges:** Mercer finds that the key challenge to investor analysis and understanding of investee climate change risks and of climate change-related investment opportunities lies in investors’ lack of knowledge. This incomplete understanding is driven, according to Mercer, by data gaps, climate change data ambiguities, and a difficulty quantifying how climate volatility affects a particular asset class. The Report found that asset owners/managers overcome these challenges through greater participation in investor groups (such as the study sponsors), education of investors, and greater communication with investees regarding climate change issues.

The full Report offers detailed explanation of these general conclusions and provides additional insight on the trends in investor review and quantification of climate change risks in investment decisions. Mercer’s findings in particular offer insight for investee representatives, such as corporate investor relations departments, on potential avenues for improving investor confidence regarding the company’s identification and management of potential climate change risks.

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■ **CARBON DISCLOSURE PROJECT QUESTIONNAIRES
COLLECT CLIMATE CHANGE INFORMATION FROM
THOUSANDS OF COMPANIES**

One source of significant data on greenhouse gas emissions by issuers is the Carbon Disclosure Project, which conducts an annual survey of thousands of companies around the globe. The survey asks for detailed information about greenhouse gas emission inventories and reduction targets, including information on corporate governance and physical risks, as well as competitive impacts of climate change.

The Carbon Disclosure Project has been sending questionnaires to issuers since 2003. The number of issuers receiving, and responding to, questionnaires has expanded substantially over that time, from 235 responses to the first questionnaire to 3,050 responses from companies in 60 countries last year. There is no legal requirement for a company that receives a questionnaire to respond to it. Although participation is voluntary, as a practical matter, a high percentage of the companies that receive questionnaires provide a response because of the perception that investors will punish issuers that do not respond. This amounts to a 65 percent overall response rate, including an 82 percent response rate among the Global 500 companies.

There are several different types of questionnaires issued by the Carbon Disclosure Project, and each has a different response deadline. The main questionnaires and the associated deadlines are Investor (May 31), Water Disclosure (June 30), and Supply Chain and Public Procurement (July 31).

Preparing a response to a Carbon Disclosure Project questionnaire requires careful coordination among an issuer's environmental and securities experts. The environmental experts must provide accurate information on greenhouse gas emissions inventories and future expectations about emissions levels. The securities experts must compare the information to be provided in the response to existing disclosures in securities filings. The response to the Carbon Disclosure Project questionnaire should not contain material information unless the information already has been disclosed in securities filings.

The responses to the questionnaires have provided the Carbon Disclosure Project with a wealth of information about greenhouse gas emissions. In 2010, the Carbon Disclosure Project issued more than 40 reports summarizing the information provided in the responses. Some of the reports provide information on companies in a particular country or geographic region. Others provide information on particular categories of issuers such as the S&P 500, while still other reports provide information on particular industrial sectors, such as utilities.

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■ SOLAR, BIOMASS, AND GEOTHERMAL DEVELOPMENT OPPORTUNITIES EMERGING IN TEXAS

Renewable energy development in Texas has been dominated by wind energy, but new opportunities are opening up for solar, biomass, and geothermal developers. New regulations proposed by the Public Utilities Commission of Texas would create a space for these sorts of projects and diversify Texas's renewable energy portfolio.

Texas established its Renewable Portfolio Standard, or "RPS," program in 1999, with implementation commencing January 2002. Utilities in the state are required to obtain and retire Renewable Energy Credits, or "RECs," to meet their market-share based requirements established under the RPS. One REC is created for each megawatt-hour ("MWh") of electricity produced from an eligible renewable facility. The RECs are tradable and may be bought or sold separately from the underlying electricity from which they were generated. Texas was the first state to adopt such a system.

Texas's RPS program was widely successful, so much so that new renewable energy capacity has consistently exceeded Texas's goals. The Texas Legislature originally set a goal of 2,000 MW of additional renewable generation capacity to be built by 2009. That goal was met by 2005, so in 2005, the Legislature increased the RPS target to 5,880 MW by 2015 and 10,000 MW by 2025. However, by the end of 2009, Texas had 9,410 MW of operating wind generation. As the REC market became flooded with wind-based RECs, the price of RECs collapsed due to a glut of supply, which in turn curtailed use of the existing REC market to promote non-wind generation.

Due to the large amount of new wind capacity added in a short amount of time, the Texas REC market buckled as supply outstripped demand. The oversupply of RECs, with the resulting collapse in prices, undermined the ability of the REC market to spur new renewable energy generation, as renewable energy generators could not expect the RECs to be

produced by new and existing projects to provide much cash flow. As a result, almost all of the new renewable energy generation capacity developed in Texas has been wind-based, driven by a federal production tax credit and the prolific wind resources of West Texas.

The domination of wind in Texas's renewable energy expansion has concerned some who felt the state had not done enough to promote other renewable resources, such as solar and biomass. In a nod toward this concern, the Texas Legislature incorporated in the state's RPS a nonbinding goal of adding 500 MW of non-wind capacity by 2015.

To encourage diversification of its renewable energy portfolio resources and meet the 500 MW goal, the Public Utilities Commission of Texas proposed in January 2011 to segment the REC market into three tiers. Tier 1 would be reserved for new solar generation, and Tier 2 would be reserved for new biomass and geothermal generation. Tier 3 would encompass all renewable energy that is neither solar, biomass, nor geothermal (such as wind). Under the proposal, utilities would be required to acquire RECs from all three tiers, thus creating demand for solar, biomass, and geothermal generation by preventing utilities from relying solely on wind power to meet their RPS obligations. The Commission is currently undecided on how to allocate the 500 MW target among solar and other non-wind renewable energy resources, leaving the major winners of this RPS shake-up to be determined.

The Texas Legislature's goal of diversifying the state's renewable energy portfolio may soon become a reality with the implementation of this proposal. If that occurs, a viable market for solar, biomass, and geothermal energy will be carved out of the wind-dominated Texas landscape, and developers of these resources should take notice.

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■ **DISTRICT COURT DESCRIBES ENDANGERMENT FINDING FOR AIRCRAFT GREENHOUSE GAS EMISSIONS AS “COMPULSORY”**

On July 5, 2011, the United States District Court for the District of Columbia issued an opinion suggesting that U.S. EPA has an obligation to make an “endangerment finding” with respect to greenhouse gas emissions from aircraft. In *Center for Biological Diversity v. United States Environmental Protection Agency*, No. 10-00985 (HHK) (D.D.C.), plaintiffs have raised claims that EPA unreasonably delayed in responding to plaintiffs’ rulemaking petitions, filed in 2007 and 2008, and in failing to determine whether greenhouse gas emissions from marine vessels, non-road vehicles and engines, and aircraft engines “cause or contribute” to dangerous air pollution. EPA moved to dismiss the claims regarding failure to make endangerment findings.

On July 5, 2011, the district court granted in part and denied in part EPA’s motion to dismiss. The court found that the permissive language addressing emissions from non-road vehicles and engines in Section 213 of the Clean Air Act, 42 U.S.C. § 7547, did not require EPA to conduct endangerment findings. The court therefore dismissed the claims related to marine vessels and non-road vehicles and engines.

Emissions from aircraft engines, however, are addressed in Section 231 of the Clean Air Act, 42 U.S.C. § 7571, which provides that EPA “shall, from time to time, issue proposed emission standards applicable to the emission of any air pollutant from any class or classes of aircraft engines which in [its] judgment causes, or contributes to, air pollution which may reasonably be anticipated to endanger public health or welfare.” In denying EPA’s motion to dismiss the claim related to aircraft engines, the district court stated that this mandatory language “strongly suggest[s] that Congress intended the predicate endangerment finding to be a compulsory step.”

The statutory language cited by the district court is almost identical to language in Section 202 of the Clean Air Act,

dealing with emission standards from on-road motor vehicles. In April 2010, EPA relied upon that language to establish greenhouse gas standards for emissions from passenger vehicles and light-duty trucks. According to the U.S. Department of Transportation, domestic aircraft account for nine percent of all transportation-related greenhouse gas emissions in the United States.

The court did not, however, take the step at this stage of the litigation of ordering EPA to make such an endangerment determination for aircraft emissions. A motion for summary judgment on plaintiffs’ remaining claims is pending, with EPA’s response due by July 27, 2011.

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■ **CALIFORNIA AIR RESOURCES BOARD RELEASES ANALYSIS OF CAP AND TRADE ALTERNATIVES**

In response to a San Francisco Superior Court order, on June 13, 2011, the California Air Resources Board (“CARB”) released a supplement to its prior environmental analysis of the Scoping Plan developed under California’s climate change law, AB 32, setting out the measures to reduce the state’s greenhouse gas emissions to 1990 levels by the year 2020. The original Scoping Plan was approved by CARB in December 2008. One of the major components of the Scoping Plan is a cap and trade program, which sets greenhouse gas emission caps on covered entities and allows covered entities to trade compliance instruments (such as emission allowances and offset credits). Accompanying the 2008 approval was a “Functional Equivalent Document” that evaluated the environmental impact of the Scoping Plan, including the cap and trade program, under the California Environmental Quality Act (“CEQA”).

As discussed in our March 2011 *Commentary*, 13 petitioners challenged CARB’s adoption of the Scoping Plan, asserting that CARB failed to comply with CEQA. On March 18, 2011, the San Francisco Superior Court determined in *Association of Irrigated Residents v. California Air Resources Board* that CARB had not adequately evaluated alternative approaches

to achieving greenhouse gas emission reductions as required by CEQA, and enjoined implementation of the Scoping Plan (including the cap and trade program) until CARB complied with CEQA.

On June 24, 2011, a California Court of Appeal stayed enforcement of the Superior Court's order, *California Air Resources Board, et al. v. Association of Irrigated Residents et al.*, Cal. Ct. App., No. 132165 (June 24, 2011), meaning that CARB may proceed to implement the Scoping Plan, including the cap and trade program, pending further consideration of the appeal. Because the appeal is still pending, and the Court of Appeal has not yet made a decision on the merits, we expect CARB to proceed with review and approval of its supplemental environmental analysis, thereby addressing the shortcomings of the 2008 Functional Equivalent Document, as identified by the Superior Court.

The supplement analyzes five alternative measures for reducing greenhouse gas emissions to 1990 levels by 2020: (1) a "no project alternative" that considers the greenhouse gas reduction actions currently in place and those reasonably expected to occur in the foreseeable future; (2) a cap and trade program; (3) source-specific regulatory requirements that would establish specific emission limits or performance standards; (4) a carbon fee or tax; and (5) a variation of the above four proposed strategies or measures. The fifth alternative is made up of three components: (a) existing source-specific emission limitations or performance standards, along with an added regulation strengthening new vehicle emission standards; (b) a cap and trade program on large sources; and (c) an emission fee on transportation fuels, residential and commercial fuels, and fuels used by smaller sources not subject to the cap and trade program.

As required by CEQA, the supplement evaluates the potential environmental impact of each of the five alternatives on aesthetics, agricultural and forest resources, air quality, biological resources, cultural resources, geology, energy, water quality and supply, hazardous materials, land use, employment and housing, noise, public services, transportation, recreation, and utility systems. The supplemental analysis concludes that the cap and trade alternative and combined measures (fifth alternative) have a high likelihood of enabling the state to reach the target of 1990 emission levels by 2020, while

source-specific regulation and a carbon fee or tax are less likely to achieve that target because of the potential for substantial emissions "leakage" through sources moving out of state. It also concludes that the "no project" alternative has a low likelihood of achieving the objectives of AB 32.

Release of the supplemental environmental analysis triggers a 45-day public review and comment period, extending to July 28, 2011. CARB staff will consider, and provide written responses to, the comments received. A CARB hearing on the supplemental analysis is scheduled for August 24, 2011.

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■ **NONPROFIT ORGANIZATIONS DEMAND GREENHOUSE GAS REDUCTIONS UNDER PUBLIC TRUST DOCTRINE**

On May 4, 2011, a coalition of youth-oriented climate change advocacy and other groups filed suit in federal and state court against federal and state officials, and filed petitions for administrative rulemaking in all 50 states, seeking to use the so-called "public trust doctrine" as a means to address climate change. The plaintiffs/petitioners argue that the atmosphere is a public trust resource and the governments in question therefore have a fiduciary duty to protect the atmosphere from greenhouse gas pollution for the benefit of current and future generations, and they have breached this duty by not regulating such emissions. In the lawsuits, the plaintiffs ask the courts to order the governmental defendants to reduce carbon dioxide emissions, such that such global emissions will peak by the end of 2012 and decline by at least 6 percent per year beginning in 2013. In the administrative petitions, the petitioners ask state environmental bodies to initiate rulemakings to accomplish the same reductions.

According to the plaintiffs/petitioners, the U.S. Supreme Court, in *Illinois Central Railroad v. Illinois*, 146 U.S. 387 (1892),

recognized the doctrine as applicable to governmental protection of navigable waterways as a public trust. They also claim that many states have since adopted similar doctrines for other natural resources.

So far, the public trust strategy has not fared well. On June 15, 2011, the Montana Supreme Court agreed with the State of Montana that it did not have original jurisdiction over such a claim and dismissed the case. On June 16, 2011, the Nevada State Environmental Commission was the first state agency to act on one of the administrative petitions. After a full public hearing, the Commission denied the petition. A number of other states have recently held or have scheduled public hearings on the rulemaking petitions. Given the Supreme Court's displacement holding in *American Electronic Power Co. v. Connecticut*, it will be interesting to see how far the public trust lawsuits proceed and what, if any, regulatory action results from the petitions.

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■ MEXICO PURSUES COMPREHENSIVE LEGAL FRAMEWORK TO ADDRESS CLIMATE CHANGE

Because Mexico is particularly vulnerable to the effects of climate change, the government led by President Felipe Calderón has actively sought to combat the effects of this phenomenon in the short, intermediate, and long term.

Mexico's approach to climate change regulation arises under several laws that govern productive sectors and activities related to the environment and energy:

Constitution. The Mexican Political Constitution governs the functions of the state in relation to use of and benefit from natural resources, care of the environment, and prevention of contamination. Mexicans have a constitutional right to an environment adequate for their development and welfare.

International Treaty. As a signatory of the Kyoto Protocol, Mexico has made its commitment to reduce greenhouse gas emissions, as well as its commitment to promote efficient use of natural resources and energy efficiency. Reducing greenhouse gas emissions through implementation of projects under the Protocol's Clean Development Mechanism, particularly renewable source electricity-generating projects (wind, biomass, hydro, solar), is among the goals of Mexico's 2007–2012 National Development Plan.

General Laws. The general laws that address climate change are (1) the General Law of Ecological Equilibrium and Environmental Protection; (2) the General Law for Comprehensive Handling and Prevention of Waste; (3) Law Regulating Constitutional Article 27 in the Field of Petroleum; (4) Law for Use of Renewable Energy Sources; and (5) Public Electricity Service Law.

To fulfill its goal of reducing greenhouse gas emissions, the Mexican government has sought to establish an appropriate legal framework that will permit the orderly implementation of

projects with flexibility and efficiency. The so-called “energy reform” was published in 2008 as part of the government’s efforts to provide this legal framework. Its purpose is, among others, to promote the use of clean energy, contribute to safekeep the environment, and foster energy sustainability.

Among the efforts made by the Mexican government to combat the effects of climate change is the recent submission of the General Law on Climate Change, an initiative that would amend more than 30 existing laws and regulations, including the General Law of Ecological Equilibrium and Environmental Protection and the Law for Use of Renewable Energy Sources. This proposal seeks to concentrate in a single legal instrument various provisions regarding climate change that are now dispersed through several instruments, which would make compliance with the climate change obligations far simpler. The initiative also addresses recommendations for policies, strategies and goals for climate change mitigation and adaptation, and processes for evaluation and follow-up of actions and their impact.

The proposal also provides for distributing climate change responsibilities among various levels of government, including the creation of:

- **The National Climate Change System.** The purpose of the System will be to group the different institutions related to the subject, integrate public policy instruments with those now in force, distribute information, and contribute to the creation of citizen awareness.
- **Climate Change Commission.** The Commission, which will replace the Inter-Secretarial Climate Change Commission, will be responsible for coordinating the formulation and implementation of a national climate change policy, including public consultations based on Commission resolutions.
- **The Climate Change Council.** The Council, a permanent body responsible for monitoring and evaluating the System, will be made up of members from civil society, private organizations, and academic bodies.

Both the Commission and the Council will have an obligation to submit annual reports to the Legislative Power. The

Mexican government has, with this action, sought to lay the foundation to mitigate in an effective form the impact of climate change in Mexico.

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■ JAPAN'S FUKUSHIMA DISASTER HAS A MAJOR EFFECT ON GERMAN PLANS FOR NUCLEAR ENERGY

In September 2010, following long and public discussions, the ruling coalition of Germany’s Christian Democrats and the Liberals reached an agreement to extend the licenses of nuclear reactors built prior to 1980 by eight years and the licenses of nuclear reactors built after 1980 by 14 years.

These arrangements were thrown into doubt following the Fukushima nuclear disaster in Japan and the rise of the anti-nuclear movement to a level not seen since the 1980s. In March 2011, after intense debate in Germany over the pros and cons of nuclear energy, the government imposed a three-month “moratorium” on nuclear energy in Germany, ordering seven nuclear reactors to shut down. At the same time, an ethics commission set up by Chancellor Merkel was instructed to review and evaluate the future of Germany’s energy supply.

Although all operators complied with the shutdown order under the three-month moratorium, RWE, the second-largest energy company in Germany, filed a lawsuit challenging the moratorium. The company, which was required to shut down its Biblis A reactor, argued that there was no legal basis for the shutdown. This view has been publicly supported by a number of German legal experts. The German government, on the other hand, argues that the moratorium is permissible under the German Atomic Energy Act, although the law was initially intended mainly to cover emergency shutdowns in case of safety concerns.

With the moratorium coming to an end in May of this year, the German government announced a roadmap to shut down all nuclear reactors in the country by 2022. According to this plan, all nuclear plants must go offline by the year 2021,

provided that if the transition to non-nuclear energy sources (mainly renewable energy) does not go as planned, three nuclear plants may continue in operation until 2022 to cover potential shortfalls. The plan further provides for one nuclear plant (likely Biblis B or Philippsburg I) to be kept on “standby” to produce extra energy when needed, such as on cold, gray winter days with little solar energy available and insufficient energy available for import from neighboring countries. However, it is unclear whether (and if so, how) a nuclear plant can be efficiently operated in a standby mode.

The roadmap has been heavily criticized from all sides as being either too ambitious or not ambitious enough. Industry has criticized the plan as bearing a significant risk, mainly to German manufacturing locations. Legally, concerns have been voiced that the proposed roadmap may be unconstitutional, unless energy suppliers are compensated for losses resulting from no longer being able to operate their nuclear plants. At this stage, it seems likely that any final decision will be made by the German Federal Constitutional Court (*Bundesverfassungsgericht*).

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■ WORLD TRADE ORGANIZATION RULES AGAINST CHINA ON MINERAL EXPORT RESTRICTIONS

In the Spring 2011 edition of *The Climate Report*, we reported how companies that manufacture green technology products face a growing challenge in securing sufficient quantities of a critical category of raw material, known as rare earth metals. China currently produces approximately 97 percent of the world's supply of rare earth metals and has in recent years limited the export of these green-technology dependent resources. On July 5, 2011, the World Trade Organization issued a ruling that provides some hope to non-Chinese manufacturers dependent on rare earth metals.

Responding to challenges filed in 2009 by the United States, the European Union, and Mexico, the WTO found China's high export customs and actual limits on the export of mineral resources to be contrary to the WTO's rules. China had

attempted to rely on Article XX of the General Agreement on Tariffs and Trade 1994, which generally permits countries to impose duties and quotas for reasons that include environmental protection and conservation of exhaustible natural resources. However, the WTO panel was unable to find how the challenged Chinese restrictions helped to address either of these issues. China is expected to appeal the ruling.

Although this WTO ruling does not specifically address rare earth metals, the restrictions placed by China on exports of rare earth metals are no different than those that were the subject of the ruling. Bringing some hope to green technology manufacturers, China announced the day after the WTO ruling that its Ministry of Commerce will study its rare earth export regime in light of the WTO's rules.

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