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The Era Of Climate Change Regulation Has Begun

Law360, New York (October 24, 2008) -- After years, if not decades, of anticipation and speculation by environmental lawyers, the era of climate change regulation recently kicked off this summer.

Following on the heels of the landmark April 2007 Supreme Court decision *Massachusetts v. EPA*, in which the Court held the Environmental Protection Agency ("EPA") must consider whether to regulate GHGs, EPA this summer issued the first two of four proposed climate change regulations scheduled for release by the end of the year. The other two proposals are reported to be on track for release by November.

These regulatory developments are advancing parallel with ongoing Congressional action during the recess to advance comprehensive climate change legislation. Meanwhile, a closely watched decision by an administrative law panel any day could require EPA to begin regulating GHGs under the Clean Air Act immediately.

Not taking comfort in any of these developments, environmental groups are implementing a strategy of employing courts to force EPA to take action to control GHGs from numerous sectors of the economy, without waiting for decisions by a McCain or Obama Administration.

Thus, with four proposed rulemakings, several pending court decisions, ongoing Congressional debate, and commitments by NGOs to keep the pressure up, the roadmap for the era of climate change regulation is being drawn now.

The Regulators' Four Tools

As much as the Bush Administration has made it clear that it will not make decisions to regulate GHGs on its watch, the EPA at the same time is engaged in four significant rulemakings that will lay the foundation for the next administration potentially to take broad action to control and mitigate GHG emissions.

Mandating Energy Efficiency Economy Wide: The Advance Notice of Proposed Rulemaking on Greenhouse Gases.

While only an “advance notice” as opposed to a proposed rule, the ANPR is the broadest in scope of these four tools. Released July 11 for a 120 day comment period that closes Nov. 28, the ANPR contains thousands of pages of text in the preamble and supporting documents.

It truly presents a roadmap that undoubtedly will be a constant companion to regulators in the next administration in considering GHG regulation of virtually every sector of the economy, from the largest power plants and manufacturing facilities, to motorcycles and lawnmowers, and everything in between.

EPA’s theme in the ANPR is to reduce GHGs by mandating energy efficiency improvements across all industry sectors.

It proposes to do so in two ways throughout: (1) by mandating energy efficient technologies on specific sectors; and (2) by mandating how technology is operated in each sector to improve energy efficiency.

For each specific industry sector—both mobile and stationary sources—EPA accordingly outlines in detail how existing technologies can be redesigned and operated differently to use less power.

For example, for aircraft EPA offers several specific proposals on how airplanes can be redesigned with lighter weight materials and different aerodynamics to improve efficiency, and also offers ideas for managing air traffic to reduce fuel use. (The author has digested the ANPR and supporting documents for numerous industrial sectors. The digests are available for free download at www.sidley.com/climatechange.)

The ANPR demonstrates that EPA regulation of GHGs is fundamentally different than EPA regulation of any other pollutant it has dealt with. At its essence, EPA proposes to place requirements not on pollutants that are released, but on how companies and industries utilize energy.

EPA proposes to set energy efficiency standards which presumably would be subject to enforcement and penalties if not met through the technology and operational controls mandated by the Agency.

So, in this way, GHG regulation would be more than environmental regulation, but regulation of the use of energy, which observers have translated into economic regulation as well.

Indeed, both industry and environmental groups have observed that in an era of GHG regulation, EPA would become a significant regulator of the economy.

One of the most controversial aspects of GHG regulation under the Clean Air Act pertains to Title I's New Source Review program, particularly the Prevention of Significant Deterioration ("PSD") and nonattainment NSR ("NNSR") provisions.

Under these provisions, permit requirements are triggered by emissions of 250 tons per year of a "regulated pollutant," or for some source categories 100 tons per year.

While these thresholds may be significant for many pollutants, they are relatively slight for GHGs, and one study estimates more than a million additional sources will need to be permitted by EPA using "Best Available Control Technology."

EPA in the ANPR indicates a desire to avoid this involuntary result while recognizing the Clean Air Act leaves little flexibility to avoid such permits be triggered.

Because the Advance Notice of Proposed Rulemaking is exactly that—an advance notice and not a proposed rule—what may be most important at this time is for stakeholders to participate in the public comment period and identify themselves as parties that seek to be consulted in formulated climate regulations moving forward.

While the breadth of the ANPR truly gives the feeling of a "blueprint" by which future proposed and final rules will be created for specific sectors, there are numerous unanswered questions that will require the input of relevant stakeholders.

Further, given that climate change regulation once it comes in final form likely will be in place for decades to come, this may be the most opportune moment to have an early influence into the formation of regulations that may be proposed in the not to distant future.

Reducing Impacts of GHG Emissions: Carbon Capture and Sequestration Proposed Rule, 73 Fed. Reg. 43492 (July 25, 2008).

Many observers believe that beyond shorter term efforts to mandate energy efficiency, a longer term approach toward addressing climate change must include carbon capture and sequestration ("CCS").

Briefly, this approach in theory would capture carbon dioxide from smokestacks and other exhausts before being emitted into the atmosphere, and sequester the CO₂ either underground in deep subsurface rock formations or, in some cases, in formations under the ocean seafloor.

EPA estimates that areas of the United States could store the equivalent of one thousand years of CO₂ emissions from nearly 1,000 coal fired power plants. 73 Fed. Reg. at 43496.

The environmental consequences of CCS focus primarily on potential harm to aquifers and drinking water supplies. In the proposed rule, EPA raises numerous questions

regarding the potential for injected CO₂ to interact with aquifers in ways that could potentially lead to contamination of drinking water.

Thus, in the proposed rule, EPA proposes to create a new classification for underground injection wells “based on the unique challenges of preventing potential endangerment” to water supplies from geologic sequestration. (EPA currently permits some sequestration to aid oil and gas recovery and on an experimental basis, but not at the commercial scale capacity envisioned by the proposed rule.)

EPA, in the proposed rule, also addresses whether CO₂ streams that include impurities should be treated as hazardous substances under other environmental laws.

While the most imminent era of climate change controls likely will focus on energy efficiency, many predict that CCS will become a key component of climate change mitigation once the technology matures, the concerns to drinking water are adequately addressed, and financial liability issues are resolved.

The public comment period on the proposed rule provides an opportunity for those who would seek to advance this technology to offer ideas at this early stage of how EPA and industry can mitigate against both the physical, legal, and financial risks of being early adopters of promoting CCS.

Monitoring GHG Emissions: The Upcoming Greenhouse Gas Inventory Reporting Proposed Rule.

In a 2007 appropriations act, Congress appropriated \$3.5M to EPA to draft a rule requiring the mandatory reporting of GHG emissions above appropriate thresholds in all sectors of the U.S. economy.

Under the appropriations act, EPA was to have published a proposed rule in late September but missed the deadline. The Agency has said in public comments it still intends to issue a proposed rule this fall. The appropriations law also set a deadline to finalize the inventory reporting rule in June, 2009.

A GHG inventory rule would require all sources that emit above a certain threshold to be specified in the rule to report their emissions on at least an annual basis if not more frequently.

EPA presumably would use this data to monitor GHG emission trends but also potentially in developing regulations to control sources of greenhouse gases.

Although not identified in the appropriations law, it is foreseeable that an inventory reporting rule could lead to one of the earliest efforts by EPA to bring enforcement actions for carbon-related emissions, in this instance for violations of monitoring and reporting requirements.

In what may be one of the first enforcement actions brought regarding GHG related issues, the New York Attorney General in August announced a settlement with Xcel Energy for failing to disclose to shareholders “the increased financial, regulatory, and litigation risks” likely to be triggered by construction of coal-fired power plants.

Described by the Attorney General as the “first ... binding and enforceable climate disclosure requirements,” Xcel agreed to include in its Form 10-K filing to the Securities Exchange Commission not only current carbon emissions, but also financial, regulatory, and litigation risks associated climate change.

Reducing the GHG Lifecycle of Fuels: The Upcoming Renewable Fuel Proposed Rule.

In December, 2007, Congress passed the Energy Independence Security Act (“EISA”). The EISA calls for EPA to mandate 36 billion gallons of renewable fuel use by 2022. While the mandates set in the law are specific for each given year until 2022, the law also leaves EPA broad discretion to define key terms that dramatically could affect the qualification of different types of feedstocks such as corn, wood, and cellulosic.

Perhaps the key issue will be how EPA determines the “lifecycle” of different feedstocks. A feedstock’s lifecycle looks beyond just the GHG emissions of the combustion of the fuel in a vehicle to the harvesting and refining of feedstocks, as well as potential changes in land use to facilitate biofuels.

In other words, when one considers GHG emissions from the tractors used to harvest biofuel feedstocks, the trucks needed to transport them and methane released from agricultural soil, the total GHGs released in the cultivation of these feedstocks increases.

EPA likely will propose a rule implementing the EISA this fall. As typical, different parties with different interests will take differing views on how EPA defines key issues.

Those promoting biofuels will argue that the lifecycle analysis should be limited to a “well to wheels” scenario similar to petroleum, where the Agency examines the GHG emissions from the time the feedstock is created to the time it is consumed as a fuel.

Opponents likely will argue that EPA must consider land use changes and other indirect impacts so that the GHG emissions of a conversion of a forest to plant corn for ethanol would be considered as well.

The Courts As Game Changers

EPA’s four-fold regulatory approach could change on a dime depending on how courts decide certain pending issues. These four rules in some way are an outgrowth of the Supreme Court’s decision *Massachusetts v. EPA*, which energized EPA, Congress, environmental groups, and even some industry groups to move forward with developing approaches to reduce GHG emissions.

Following Massachusetts, there are currently several other cases pending in the courts, administrative review boards or headed toward litigation that, depending on their outcome, could dramatically affect the Agency's approaches to climate change.

Perhaps the potentially broadest issue is being considered at the moment by EPA's Environmental Appeals Board in *In re Desert Rock Energy Company, LLC*, PSD 08-03. There, environmental groups challenge EPA's issuance of a coal fired power plant permit for failure to impose CO₂ limits.

The issue hinges on whether, post Massachusetts, CO₂ and other GHGs currently are "regulated pollutants" under the Clean Air Act.

The Agency took the position that, because the Supreme Court decision did not actually call for EPA to regulate GHGs, but merely consider whether to do so, GHGs are not currently regulated.

Petitioners, in turn, have pointed to other EPA regulations that call for monitoring GHGs to argue that the Agency currently is regulating GHGs, and thus must impose GHG controls.

A finding by the EAB that GHGs are regulated pollutants today could have dramatic ramifications across all sources.

In addition to bolstering their argument that new permits must include GHG limits, environmental groups undoubtedly would argue that such a finding would flow into other provisions of the Clean Air Act for both mobile and stationary sources, potentially accelerating EPA regulation under multiple Clean Air Act provisions and bringing delays to pending permits for new facilities.

Groups also could argue that such a determination would trigger the PSD requirements described above, bringing as many as a million new sources under EPA's permitting authority.

Courts also are considering several other issues, including the timing of when EPA is required to issue an endangerment finding, California's authority to establish GHG standards for cars and trucks, whether EPA is currently required to set GHG standards in creating "New Source Performance Standards" for stationary sources under Clean Air Act Section 111, and whether the Department of the Interior properly limited the ramifications of the Endangered Species Act on climate change in listing the polar bear as a threatened species.

Finally, various citizen groups have brought four separate nuisance cases against GHG emitters for alleged harm due to climate change impacts. These cases, most of which have been dismissed at the district court level, are in various stages of litigation.

Other Roles To Watch

This article focuses on the upcoming roles of regulators and courts since both are moving forward on GHG controls regardless of decisions by politicians and third parties. Other important parties to watch include:

Congress, which will continue to debate comprehensive climate legislation and may feel greater urgency to act depending on how some of the issues identified above are resolved by EPA and the courts;

state and local governments who in many instances are pursuing aggressive climate controls at the regional level;

environmental groups, who already have signaled an intent to continue to pursue aggressive action in the courts regardless of the action or inaction by the next Administration;

international negotiators developing the United States' role in a post-2012 international framework for addressing GHGs;

Wall Street and insurance companies which, at least prior to the financial crisis, had been turning increasing attention on assessing the risks to companies of climate change controls and impacts;

and companies who are not considered traditional emitters of GHGs but will have downstream impacts from the higher fuel and energy costs associated with GHG controls.

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