

February 8, 2008

Climate Change Policy Update Week of February 4-8, 2008

Commentary: *Falling mercury usually signifies global cooling, but falling mercury regulations could signify a new twist in global warming legislation. This week, a Federal court vacated EPA's Clean Air Mercury Rule (CAMR), which would have established a cap-and-trade program for mercury emissions from power plants. The demise of the CAMR could revive interest in Congress in what had been called the "4-P" approach to regulating the power sector. Sen. Carper (D-DE) has been the leading proponent of this approach, calling for a program to establish coordinated caps for power plant emissions of mercury, sulfur dioxide, nitrogen oxides, and CO₂. Sen. Carper has further asserted that a power sector-only program would be an easier launching point for U.S. greenhouse gas regulation than an economy-wide program.*

Congress

- **Congress Receives Administration's 2009 Budget Request.** President Bush submitted his \$3 trillion Fiscal Year 2009 budget request to Congress on Monday. The proposal recommends \$25 billion for the Department of Energy (DOE), which is roughly \$500 million over the agency's FY 2008 budget allocation. The Administration calls for additional resources for clean coal technology and other clean technology programs. It also recommends significant cuts in certain popular programs, including a 27 percent decrease in funding for renewable energy and efficiency projects. The proposal recommends a combined \$241 million for the Administration's Clean Coal Power Initiative and a restructured FutureGen program; the Administration proposes to re-focus the FutureGen program on relatively smaller amounts of funding for several carbon capture and sequestration R&D projects. In all, the Administration seeks to fund the Office of Fossil Energy at \$1.1 billion in FY 2009, a 41 percent increase over current funding levels. The Administration is also seeking to extend the loan guarantee program for advanced coal, nuclear and renewable energy programs. DOE is specifically requesting a four-year extension for nuclear plant projects and three-year extensions for other loan guarantee-qualifying projects. In addition, a new international clean technology fund designed to enable the deployment of technology in developing countries would be funded at \$400 million in FY 2009 as the first installment of a three-year, \$2 billion commitment from the U.S.

If you have questions about topics covered in this Update, please contact Kyle Danish, head of the Climate Change and Emissions Trading Practice, at kwd@vnf.com

Administration

- **DOE to Issue Clean Energy Loan Guarantees in 2008.** Secretary of Energy Samuel Bodman told the Senate Energy and Natural Resources Committee this week that DOE expects to receive at least 16 applications in the next several months from firms seeking loan guarantees for clean energy and nuclear power projects. Secretary Bodman said that the agency could issue the loan guarantees by the end of the year. Firms are expected to submit applications for projects involving advanced technology for biomass, fossil energy, solar, industrial energy efficiency, electricity delivery and reliability, hydrogen, and alternative fuel vehicles. The loan guarantee program was authorized under the Energy Policy Act

February 8, 2008

of 2005 and Congress appropriated \$20 billion for the program in its FY 2008 Energy and Water Appropriations bill.

- **EPA Begins Rule to Establish Greenhouse Gas Registry; Will Draw Info From Existing Programs.** Director of the Environmental Protection Agency (EPA) Office of Transportation and Air Quality's Transportation and Climate Division, Sarah Dunham, said that the agency is taking initial steps toward establishing a greenhouse gas registry. The registry, which was required by language included in the FY 2008 omnibus appropriations bill (H.R.2764), will compile data on greenhouse gas (GHG) emissions from a broad range of U.S. industries. EPA is required to issue a proposed rule on the registry by September and final regulations nine months later. The Administration eliminated funding for the registry in its FY 2009 budget proposal. Ms. Dunham said that the agency will use some emissions data that it already collects from programs such as the Corporate Average Fuel Economy (CAFE) program.
- **Remaining Presidential Candidates Support Mandatory Climate Cap-and-Trade Program.** Former Massachusetts Governor Mitt Romney (R) dropped out of the presidential race, leaving Sen. John McCain (R-AZ) and former Arkansas Governor Mike Huckabee as the most likely remaining potential Republican candidates. Both candidates have publicly supported a mandatory federal cap-and-trade program to reduce GHG emissions, and Sen. McCain previously co-sponsored cap-and-trade legislation with Sen. Joseph Lieberman (I-CT). Of the leading Republican candidates, Mr. Romney was the only one who had not indicated whether he would support a federal climate program. Sen. Hillary Clinton (D-NY) and Sen. Barack Obama (D-IL), the major current Democratic presidential candidates, also support a cap-and-trade approach.
- **EPA Panel Rejects Permitting Challenge to Coal-Fired Power Plant.** The EPA Environmental Appeals Board (EAB), the final Agency decisionmaker on administrative appeals under all major environmental statutes administered by EPA, rejected on procedural grounds a challenge brought by the Sierra Club in which the environmental group argued that a Clean Air Act Title V operating permit for a coal-fired power plant in Illinois should contain limits on CO₂ emissions from the facility. The group had claimed that CO₂ is a regulated pollutant under the Clean Air Act (CAA) – the CAA triggering requirement for a permit limit – because the Acid Rain Program requires facilities to monitor and report their CO₂ emissions. On this basis, the group further argued that the Title V permit for the Illinois integrated gasification combined cycle (IGCC) coal-fired plant should require the use of “best available control technology” (BACT) to limit its emissions. In dismissing the Sierra Club challenge on procedural grounds, the EAB noted that while the issue was “reasonably ascertainable” during the comment period, the Sierra Club failed it to raise the issue for consideration while the issue was open for comments. The EAB decision does not prevent this issue from being raised in challenges to other permits, and other environmental advocacy groups have asserted similar arguments in the context of other permit challenges.
- **Court Vacates Clean Air Mercury Rule.** In a Clean Air Act development that could have indirect implications for federal cap-and-trade legislation, the Court of Appeals for the District of Columbia Circuit vacated EPA's Clean Air Mercury Rule (CAMR). The CAMR would have established a cap-and-trade program for electric power plant emissions of mercury. The decision could revive earlier proposals in Congress for comprehensive legislation that would address the power sector's emissions of mercury, sulfur dioxide, nitrogen oxides, and CO₂.

February 8, 2008

- **EPA Cites Concerns Over CO₂ Emissions for Nevada Power Plant.** EPA filed comments in response to a draft Environmental Impact Statement (EIS) for a proposed coal-fired power plant in southern Nevada. EPA has the authority under the National Environmental Policy Act (NEPA) to review and comment on the adequacy of any federal EIS. Under NEPA, the presence of a proposed plant on federal land becomes a “major federal action” requiring an EIS and triggering EPA’s responsibilities under the act. Chief among the agency’s concerns was whether CO₂ emissions from the plant had been adequately addressed. EPA recommended that the Bureau of Land Management (BLM), the agency that owns the land on which the proposed power plant would be constructed, provide additional information on CO₂ emissions, as well as analysis of alternatives to the power plant, including use of renewable energy, conservation measures to reduce electricity consumption, and not building the facility. EPA has raised similar concerns about other proposed coal-fired power plants in Nevada.
- **Department of Interior Proceeds with Alaskan Oil Lease Opposed by Environmental Advocates.** The Department of the Interior announced Wednesday that it drew \$2.6 billion in winning bids from companies seeking permits to drill for oil and gas in Alaska’s Chukchi Sea. Companies made over 667 bids for 448 tracts in the 29-million acre area. The lease-sale has been contested by environmental groups and members of Congress who argue that gas exploration would endanger polar bear populations in the area. The Fish and Wildlife Service missed a January deadline to decide whether it would list the polar bear as endangered under the Endangered Species Act due to habitat loss from melting arctic ice.
- **State Department Seeks Comments on Future of IPCC.** This week, the U.S. State Department published a solicitation for public comments on the future role of the Intergovernmental Panel on Climate Change (IPCC). Comments, which are due by February 29, will focus on the structure and content of IPCC reports and the panel’s drafting process. The next planning session of the IPCC will be held in Budapest, Hungary this April.

States and Cities

- **Massachusetts GHG Trust Offered as Model for National Cap-and-Trade Program.** Under the Commonwealth of Massachusetts’ proposed rules for regulating the CO₂ emissions efficiency of power plants (outside the RGGI process), the “GHG Expendable Trust” would allow regulated firms to pay into the trust to receive credit toward their compliance obligations under the regulations. The amount of the payments would be set annually by the Massachusetts Department of Environmental Protection and would be used to fund emissions offset projects. Supporters of the trust argue that the fund would expand the options for compliance and relieve allowance market uncertainty. Others claim that the trust would compromise the environmental integrity of the program by allowing regulated firms to comply by paying a set price rather than reducing emissions or funding specific offset projects. Observers note that Massachusetts faces a lack of available offsets for the CO₂ regulations stemming from the state’s failure to pre-qualify offset projects.
- **Pennsylvania Not Likely To Join RGGI Due to Fears Over Leakage.** Kathleen McGinty, Secretary of the Pennsylvania Department of Environmental Protection, stated that fears over “leakage” prevent the state from joining the regional GHG emissions cap-and-trade program. Ms. McGinty asserted that the RGGI design, which regulates power producers rather than energy consumers, allows power producers regulated by the cap to meet their compliance obligations by reducing their own generation and importing power from outside the RGGI states, which has the effect of offsetting any emission

February 8, 2008

reductions in the RGGI region with higher emissions outside the region – an effect referred to as “leakage.” She said that Pennsylvania instead is pursuing a consumption-based approach to regulating GHG emissions. While noting problems with some RGGI design decisions, Ms. McGinty said that RGGI and other regional cap-and-trade programs have been helpful in spurring Congress to pursue the creation of a national cap-and-trade program.

- **Los Angeles-Area Air District to Form Stakeholder Group to Advise on Development of Cap-and-trade Program Rules.** The South Coast Air Quality Management District (SCAQMD) will establish an advisory group to help develop a voluntary CO₂ cap-and-trade program for the district. The stakeholder technical advisory group will assist SCAQMD staff in drafting rules for implementing the cap-and-trade program. The program, to be called the “SoCal Climate Solutions Exchange,” will be based on SCAQMD’s Regional Clean Air Incentives Market (RECLAIM) program, a cap-and-trade program created in 1993 to reduce nitrogen oxides and sulfur dioxide emissions in the region.
- **Citizens’ Group Challenges Michigan Agency’s Failure to Regulate CO₂ Emissions From Coal-Fired Power Plants.** The group, Citizens for Environmental Quality, filed a suit against the Michigan Department of Environmental Quality (DEQ) to force the agency to regulate CO₂ emissions from coal-fired power plants. In filing the suit, the group said that the DEQ failed to adequately respond to the group’s previous request for rules governing CO₂ emissions. The group noted that five companies are seeking permits for new coal-fired power plants in the state, which would increase the state’s CO₂ emissions by millions of tons. A spokesman for the agency said that it is waiting for guidance from EPA before taking action on CO₂ emissions and expressed disagreement with the group’s contention that CO₂ is a regulated pollutant under the Michigan Environmental Protection Act.
- **Florida Joins Suit Challenging EPA Waiver Denial; D.C. Council Approves Adoption of California Vehicle Emission Standards.** Florida became the seventeenth state to join the suit by California appealing EPA’s denial of a waiver for California’s vehicle GHG emissions standards. Florida Gov. Charlie Crist (R) issued an executive order on July 13, 2007, directing the state Department of Environmental Protection to adopt the California standards, and the agency is in the process of developing rules adopting the standards. The Clean Air Act requires that California receive a waiver from EPA before California and other states can implement the motor vehicle emission standards. In other news related to the California waiver, the District of Columbia City Council voted for legislation adopting California’s emissions standards. The D.C. Council will vote on the issue again in March before sending the legislation to D.C. Mayor Adrian Fenty.

Industry

- **Three U.S. Banks Release Guidelines for Addressing Climate Change Risk in Financing Fossil Fuel Generation.** Citi, JPMorgan Chase, and Morgan Stanley released guidelines for an approach to evaluating climate change risks in the U.S. electric power sector, called the “Carbon Principles.” The Carbon Principles are intended to assist lenders and clients in assessing the regulatory and financial risks associated with GHG emissions “in an environmentally responsible and cost effective manner.” Under the Carbon Principles, fossil fuel generation will be assessed under an “Enhanced Diligence Process” that will evaluate the proposed financing under a range of future CO₂ emission costs and controls. The banks committed to: encourage clients to pursue cost-effective energy efficiency and no- or low-emission generation “taking into consideration the potential value of avoided CO₂ emissions;” apply the Enhanced Diligence Process to fossil fuel generation financing; and to educate industry participants about the diligence required for fossil fuel financing while encouraging regulatory and

February 8, 2008

legislative changes consistent with the Carbon Principles. The Carbon Principles were developed with input from leading power companies, including American Electric Power and Southern Company, and environmentalists.

- **Voluntary Carbon Registries to be Operational by Summer.** Developers of two different voluntary carbon offset standards, the Voluntary Carbon Standard and The Gold Standard, each announced that registries for projects developed in accordance with their standards will be operational in the near future. The Voluntary Carbon Standard expects to have registries for its approved projects operational by July, while The Gold Standard anticipates launching its registry in early March. Each program provides a set of standards for independent verification of emission reduction projects. The Gold Standard aims to provide a system for identifying projects that not only achieve reductions, but also various other environmental and social co-benefits. Having a registry for each program will help clarify which entities have title to reductions verified under each standard.
- **Joint Venture Between Bank of America and Climate Exchange Plc Cancelled.** The two companies announced that they are cancelling a joint venture proposed in July of 2007, under which Bank of America would have purchased 500,000 carbon credits over a three year period in return for an increased share of Climate Exchange Plc, the parent company of both the European Climate Exchange and the Chicago Climate Exchange.

Studies and Reports

- **Studies Find that Biofuels Increase GHG Emissions through Land Use Change.** Two reports published in the journal *Science* indicate that the production and use of biofuels results in increased GHG emissions relative to conventional transportation fuels when emissions from changes in land use are accounted for. One report focused on U.S. croplands and analyzed the effects of increased prices for biofuel feedstock on land use patterns. The report indicates that biofuels production results in clearing of additional land, either for biofuel growth on newly cleared land or additional land cleared for crop production that was displaced by biofuel crops. When land use is taken into account, the report found that production of corn-based ethanol nearly doubles GHG emissions over 30 years relative to the same amount of conventional fuel, while emissions from switchgrass grown on corn lands increases emissions by 50 percent. The other report similarly found that food-based biofuels create a “biofuel carbon debt” by releasing 17 to 420 times more CO₂ than the annual GHG reductions provided by these biofuels from fossil fuel displacement. Both reports recommend using agricultural waste or nonfood crops on abandoned agricultural land for biofuel production.

International

- **India Set to Adopt National Plan to Address Global Warming.** Indian Prime Minister Manmohan Singh announced that India will release a climate change plan this June. The Prime Minister said the plan will not include absolute emissions targets, but stated that the nation is prepared to limit its per-capita GHG emissions to the same levels as those in developed countries. India’s current per-capita emissions are approximately ten times lower than current U.S. per capita emissions. In addition to per-capita limits, the plan is also likely to include a venture capital fund for green technologies, measures to increase energy efficiency, and an adaptation program to mitigate the effects of climate change on the nation’s poor.

February 8, 2008

- **Australian Proposal Calls For Mandatory GHG Emissions Registry.** Australia's Climate Change and Water Minister Penny Wong released a proposal for a mandatory national GHG emissions registry and energy use regime. The report proposes creating reporting requirements at both the facility and corporate levels. The proposed registry would regulate all facilities that emit 25,000 tons or more of carbon dioxide equivalent (CO₂e) or that use greater than 100 terrajoules of energy. Corporations with aggregate emissions of greater than 125,000 tons CO₂e or that use 500 terrajoules of energy would also be required to report to the registry. In releasing the report, Minister Wong stated the national reporting system would provide the data necessary for creating a national emissions trading scheme. The proposed registry is currently open for public comment and will eventually be added to Australia's National Greenhouse and Energy Reporting Act of 2007.
- **Japanese Bill Promotes Use of Forest Carbon Sinks to Meet Kyoto Obligations.** The bill will promote use of forest carbon sinks by providing financial support to local governments to conduct forestry programs aimed at reducing national GHG emissions. Forest carbon sinks are included in the Kyoto Protocol as a mechanism for meeting national emission reduction goals. Japan's obligation under the Kyoto Protocol requires it to reduce national GHG emissions by 6 percent from 1990 levels by 2012. The Japanese plan to meet that obligation calls for achieving 3.8 percent of that 6 percent reduction through domestic carbon sink plantation projects. Japan currently manages 350,000 hectares of forest land and the national plan calls for adding 200,000 hectares over the next five years to meet its emission reduction goal.

The Climate Policy Update is intended as a general summary of major climate change-related policy developments that we judge to be of interest to a broad range of our clients and friends. We welcome your comments and suggestions. Coverage in, and selection of topics for, the Update is not intended to reflect the position or opinion of Van Ness Feldman or any of its clients on any issue. This document has been prepared by Van Ness Feldman for informational purposes only and is not a legal opinion, does not provide legal advice for any purpose, and neither creates nor constitutes evidence of an attorney-client relationship.

© 2008 Van Ness Feldman, P.C. All Rights Reserved.