

T O U R F R I E N D S A N D C L I E N T S

M e m o r a n d u m



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EPA Proposes Draft Rule Requiring Greenhouse Gas Emissions Monitoring and Reporting

On March 10, 2009, the US Environmental Protection Agency (“EPA”) released its long-awaited draft rule entitled “Mandatory Reporting of Greenhouse Gases” (the “Draft Rule”).¹ The Draft Rule requires a wide range of greenhouse gas (“GHG”)² emission sources, including fossil fuel manufacturers and suppliers, industrial facilities and utilities, to monitor and report their GHG emissions to EPA starting in 2010. If enacted, the Draft Rule will be the first federal, broadly applicable set of mandatory requirements relating to GHG emissions.

Background. The FY08 Consolidated Appropriations Act,³ signed into law on December 26, 2007, charged EPA with developing a rule pursuant to its existing authority under the Clean Air Act (the “CAA”) requiring mandatory GHG emissions monitoring and reporting “above appropriate thresholds in all sectors of the economy.” An accompanying “explanatory statement” directed EPA to include in its rule “upstream” sources that produce fuels or other products that result in GHG emissions as well as “downstream” emitters of GHGs. Although the law called for a draft rule within nine months of the law’s passage, it took 15 months – and the change in administration – for the Draft Rule to be released. The Draft Rule is currently subject to public comment.

The Draft Rule should be understood in the broader context of EPA’s evolving policies with respect to climate change. The preamble to the Draft Rule explains that one of its primary purposes is to help inform future climate change policy decisions. In addition, the Draft Rule is being released as EPA considers a number of significant GHG emissions policy issues, including: (i) an “endangerment” finding concerning CO₂ emissions under the CAA in response to the Supreme Court’s decision in *Massachusetts*

¹ The full text of the Draft Rule and EPA’s preamble are available at: <http://www.epa.gov/climatechange/emissions/ghgrulemaking.html>. The Draft Rule has not yet been published in the Federal Register.

² The GHGs subject to the reporting requirements are carbon dioxide (CO₂), methane (CH₄), nitrous oxide (N₂O), hydrofluorocarbons (HFC), perfluorocarbons (PFC), sulfur hexafluoride (SF₆), and other fluorinated gases including nitrogen trifluoride (NF₃) and hydrofluorinated ethers (HFE).

³ Pub. L. No.110-161, 121 Stat. 1844, 2128 (2008).

v. EPA,⁴ (ii) reconsideration of the EPA's decision that CO₂ is not a regulated pollutant under certain CAA permitting programs, and (iii) reconsideration of EPA's denial of California's request for a waiver of preemption of its regulation of GHG emissions from vehicles. Although the preamble gives no indication concerning EPA's ultimate position on these issues, the broad scope and ambitious timetable of the Draft Rule is consistent with widely held expectations that EPA is likely to favor more stringent GHG emissions policies.

Key Provisions of the Draft Rule. The key provisions are as follows:

- **Facilities and Businesses Covered by the Draft Rule.** The Draft Rule covers the following three categories of facilities and businesses:
 1. Most suppliers of fossil fuels or industrial GHGs and manufacturers of vehicles or engines.
 2. Facilities with certain categories of GHG emissions sources, such as electrical generation and manufacturing of chemicals, cement, aluminum and certain electronics.
 3. Facilities that emit 25,000 metric tons or more of carbon dioxide equivalent ("CO₂e") per year from either stationary fuel combustion or a wide variety of source categories, including food processing, industrial landfills, iron and steel production, and pulp and paper manufacturing. Facilities with emissions from stationary fuel combustion sources only (e.g., non-industrial facilities) are only required to report if their maximum rated heat input capacity is 30 million Btu/hour or more.

As a general rule, these three categories of facilities and businesses will be required to monitor and report the GHGs they emit to EPA on an annual basis. The facilities and businesses included in the first category listed above are considered "upstream" reporters, and will also be required to report the estimated amount of GHG emissions by the ultimate "downstream" users of the products they supply.

- **"Facility" Broadly Defined.** Because the Draft Rule (with limited exceptions) requires monitoring and reporting of GHG emissions on the facility level, the definition of the term "facility" is critical. The Draft Rule defines the term facility to include contiguous and adjacent units under common ownership or control. This definition would appear to include within its scope sites that may not independently meet any of the reporting categories described above but are part of a group of sites under common ownership. For example, industrial parks or large commercial complexes owned by a single entity would appear to be subject to the Draft Rule if the combined emissions of the development as a whole exceed the threshold, even if each unit within the development is operated by independent, unrelated businesses.

⁴ 127 S.Ct. 1438 (2007).

- **Implementation Timeline.** Monitoring and reporting requirements under the Draft Rule would start on January 1, 2010, and a report on GHG emissions for calendar year 2010 would be due by March 31, 2011. Vehicle and engine manufacturers would begin reporting for model year 2011. However, EPA acknowledges that it may not be able to issue its final rule in time for the effective date proposed in the Draft Rule, in which case 2010 emissions could be reported using the best available data or the effective date could be delayed until 2011.
- **Monitoring and Recordkeeping Requirements.** The Draft Rule provides for direct or indirect GHG emissions monitoring depending on the emissions monitoring system in place at a facility on the effective date. Facilities that do not have an existing continuous emissions monitoring system (“CEMS”) will not be required to install such systems and instead may employ indirect monitoring methods described in the Draft Rule. Facilities with CEMS in place will generally be required to use, or if necessary upgrade, their existing CEMS to monitor GHG emissions. There are also substantial recordkeeping requirements, including retaining a wide variety of records relating to the calculation of emissions for five years.
- **Cost of Compliance.** According to EPA estimates, approximately 13,205 facilities will be required to report under the Draft Rule with aggregate estimated costs of \$160 million in the first year of implementation and \$127 million annually thereafter. Compliance costs are likely to vary among facilities depending on factors including the quantity of GHG emissions and whether emissions monitoring needs to be initiated or expanded.
- **“Indirect” Emissions Generally Not Covered.** Aside from suppliers of fossil fuels or industrial GHGs and manufacturers of vehicles or engines, the Draft Rule only requires reporting of emissions directly emitted by a reporter’s operations. Emissions resulting indirectly from the operation of a facility, such as power plant emissions associated with the electricity used by the facility, are not required to be reported and are not considered when determining if the 25,000 ton reporting threshold is calculated. In contrast, some currently existing voluntary reporting regimes focus on a facility’s total “carbon footprint,” which includes all GHG emissions that directly or indirectly result from a facility’s operations.
- **Penalties for Non-Compliance.** Violations of the Draft Rule are subject to the penalty and enforcement provisions set forth in §§ 113 and 203-205 of the CAA, which provide for civil and criminal penalties and injunctive relief to compel compliance.

Public Comment Period. The Draft Rule is subject to public comment for 60 days following publication in the Federal Register (which has not occurred yet). The EPA is seeking comments on specific aspects of the Draft Rule, including (i) the emissions reporting threshold, (ii) the effective date, frequency and duration of reporting, (iii) whether vehicle fleet operators should be subject to reporting requirements, and (iv) whether facilities should be required to quantify and report their electricity purchases.

Impact and Significance of the Draft Rule. If implemented, many businesses will need initially to determine whether their operations fall into one of the reporting categories set forth above in the Draft Rule. For some categories of businesses, this determination will be straightforward. For other categories of businesses, this determination may require a preliminary assessment of their annual GHG emissions.

If a business determines that it is likely subject to the Draft Rule, it will need to ensure that appropriate systems and resources are in place to calculate its GHG emissions in accordance with the terms of the Draft Rule. Businesses that already report GHG emissions information under other mandatory or voluntary programs should consider that the Draft Rule will establish a reporting standard that may fundamentally differ from other GHG reporting programs. Businesses that disclose GHG emissions information pursuant to these other programs on their website, securities filings, sustainability reports or other public documents will need to explain or reconcile any discrepancies with GHG emissions information reported under the Draft Rule.

If a facility determines that it is not subject to the Draft Rule because it does not meet the GHG emissions reporting threshold, it will be advisable to document how the determination was made in case it ever becomes the focus of regulatory scrutiny. In addition, facilities below the reporting threshold should periodically reassess their emissions, particularly if there are any changes in the nature of their operations or production levels.

Finally, mandated reporting is a natural first step towards a federal GHG emissions cap and trade system that is widely anticipated under the Obama Administration. The emissions data reported under the Draft Rule will no doubt provide policy makers, reporting businesses, investors and the general public with valuable information about the likely impact such a system may have.

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