



November 6, 2009

## IMPACT OF RECENT LITIGATION ON THE CLIMATE CHANGE DEBATE

## ENERGY/ENVIRONMENTAL ALERT

Two decisions issued in the past several weeks by the U.S. Courts of Appeal for the Second and Fifth Circuits have confirmed the gathering momentum of common law initiatives by environmental advocates to assess liability against Greenhouse Gas (GHG) emitters. This trend is, of course, important in predicting the course of case law development and that effect has been extensively discussed elsewhere. Equally important, however, is the trend's effect in complicating the already complex landscape of the climate change debate taking place in the Congress and before regulatory bodies. The potential of common law liability presents a number of issues which should be taken into account in formulating legislation and regulations. This memorandum discusses the need for such consideration and identifies some of the issues which legislators, regulators and GHG emitters should take into account.

## I.

The Second Circuit's decision in *Connecticut v. American Electric Power Co.*, No. 05-5104 CV, was handed down on September 21, 2009. Several states, New York City and several environmentally-oriented land trusts sued a number of major GHG emitters seeking an injunction that would cap emissions from these companies and require a steady reduction in that cap. The case was dismissed by the District Court on the grounds that the claims represented a "non-justiciable political question," and the plaintiffs appealed.

The Appeals Court reversed the District Court, finding that the political question doctrine was inapplicable. The Court noted that federal laws and regulations may preempt the federal common law of nuisance, which is the basis for Plaintiffs' claims, but federal laws or regulations are not adequate at this time to cause such preemption.

Less than a month later, the Fifth Circuit held that private property owners could pursue claims for damages against major GHG emitters on the grounds of public and private nuisance, trespass and negligence. *Comer v. Murphy Oil Co.*, No. 07-60756, October 16, 2009. This case is a proposed class action involving thousands of people who allege that damage to their Mississippi coastal properties from Hurricane Katrina would not have been as destructive absent GHG emissions from the Defendants, who are large GHG emitters.<sup>1</sup>

Both appellate decisions rejected dismissals of claims on summary judgment, setting a rather low bar for adequately pleading a cause of action. It likely will be more difficult for plaintiffs to prove their respective cases than to plead them, and the plaintiffs may find it difficult either to prove causation or to quantify the Defendants' appropriate share of any damages shown. Nevertheless, the ability to bring and prosecute damage claims is an important power and, given the magnitude of the damages involved and the abundance of available deep pockets, it seems likely that the plaintiff's bar will increasingly find ways to bring credible actions, and that legislative or regulatory actions can have a significant impact on such actions' potential for success.

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<sup>1</sup> Between the dates of these two decisions, the U.S. District Court for the Northern District of California dismissed a very similar lawsuit. *Native Village of Kivalina v. ExxonMobil Corp.*, No. C 08-1138, September 30, 2009. Plaintiffs have announced their intention to appeal this decision to the Ninth Circuit; it is noteworthy that the two appellant decisions discussed above reversed dismissals by a District Court.

## II.

In order to adequately assess impacts on the legislative/regulatory debates, we need to understand their specific elements.

What might be termed the “modern era of the climate change policy debate” began with the Supreme Court’s decision in *Massachusetts v. EPA*, 549 U.S. 497 (2007). In that case, the Supreme Court, in addition to enhancing advocacy groups’ ability to litigate by enunciating a relatively low bar for establishing standing, ruled that GHG is a “pollutant” under the Clean Air Act (CAA) and that the Environmental Protection Agency (EPA) is authorized to regulate GHG emissions from new motor vehicles if it determines that such emissions endanger the health and welfare of the American public.

The *Massachusetts v. EPA* decision set in motion a cascade of regulatory actions, many of which have substantial potential impact on emitters’ common law liability exposure. Pursuant to the authority of the CAA, EPA has:

- Finalized a rule requiring major emitters of GHGs -- those emitting more than 25,000 tons per year -- to report to EPA on their emissions. 74 Federal Register 56260 (October 30, 2009). This rule covers carbon dioxide (CO<sub>2</sub>) and five other greenhouse gases, and raises a number of questions in the litigation context, such as: Can the information reported by emitters be used as evidence against them in common law litigation? Can the database be used to compute liability shares? Does the exemption of small emitters mean that they are not contributors to GHG problems and therefore should escape liability? Etc.
- Proposed an “endangerment finding.” 74 Federal Register 18885 (April 24, 2009). If finalized, this proposed rule would determine that GHG emissions endanger the public health and welfare, which triggers regulation of these emissions under the CAA. Will the endangerment finding render GHG emissions nuisance per se or extremely hazardous activity? Is continued emission of GHG negligence per se or reckless endangerment? Etc.
- EPA and the Department of Transportation have proposed a joint rule governing GHG emissions from light duty vehicles and establishing fuel economy standards. 74 Federal Register 49454 (September 28, 2009). Will previously manufactured vehicles remain a source of liability? What are implications for warranties and fitness for use? Will old high emission vehicles be treated similarly to asbestos or lead-based paint?
- Finally, EPA has proposed a “tailoring” rule for GHG emissions from stationary sources. 74 Federal Register 55142 (October 27, 2009). This proposed rule attempts to limit the scope of the regulation of GHG emissions to stationary sources emitting 25,000 TPY or more of GHG. Whether this effort will succeed given that the CAA imposes a 100/250 TPY threshold for regulation remains to be seen. In any event, a final version of this rule will require Best Available Control Technology (“BACT”) for new and modified sources if they meet the emissions threshold. In addition, Title V permits will be required for affected sources, although many such sources already have such permits. Does this mean that low emitters are excused from liability and do the large emitters pick up this “orphan share”?

Congress has also been busy. It is aggressively considering major climate change legislation. This summer, the House passed the Waxman-Markey bill, and the Senate Environment and Public Works Committee and other Senate committees are drafting their own version or portions thereof of climate change legislation. The basic feature of this legislation is a program that would cap GHG emissions, a cap which would decline over time. In order to emit GHGs above a set limit, a “covered entity” would be required to

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<sup>2</sup> Law 360 Newswire, November 3, 2009, “GHG Appellate Rulings Could Incite Insurance Brawls.”

acquire “allowances” or cut emissions. Most allowances will initially be given away for free. But over time, they will have to be purchased as free allowances are phased out. Facilities that emit less and have excess allocations can sell or trade those allocations to higher emitting sources. Although the Congress would seem to be an appropriate, and perhaps the most appropriate, governmental actor to resolve questions of the sort outlined above, we have not as yet seen any meaningful Congressional consideration of these issues or of the more general issues of preemption or displacement. The absence of such consideration could have long term adverse effects.

### III.

There are a number of possible developments in the judicial context which could affect the impact of the *AEP* and *Comer* decisions. First, the Defendants may seek a rehearing *en banc* by the respective circuit courts or they may seek a writ of certiorari from the Supreme Court. In either event, any impact would await further decision, and would obviously depend on the ultimate decision.

Second, the Second Circuit recognized in *AEP* that a comprehensive legislative or regulatory scheme could effectively preempt or displace the federal common law under which these cases were brought. As noted above, however, neither the regulatory agencies nor the Congress seem to be paying much attention to the relationship between statutes/regulations and the common law. We expect Congress to take an extended period before enacting climate change legislation, barring unexpected developments, and EPA is rumored to be moving quite slowly on finalizing its regulations despite publicly announcing that it is moving quickly. Most importantly, none of the bills before Congress, nor EPA’s proposed regulations, explicitly preempt the common law, on which the recent decisions rest, or clearly state their intended effect on common law liability. In the absence of clear guidance, the courts might or might not consider the statutory or regulatory approach to be sufficiently comprehensive to preempt, displace or otherwise supersede common law.

### IV.

In the absence of comprehensive federal legislation or regulation clearly enunciating its intended effect on common law liability, we would expect, at least in the short term, a continuing gathering of momentum for common law GHG cases and a resulting spate of litigation against large GHG emitters. With the pleading bar set so low, summary judgment is not likely; instead, protracted discovery and debate regarding establishing factual and scientific issues will be the norm. Since *Comer* explicitly found that private plaintiffs have standing to sue, the prospect of obtaining damages should tempt some people and entities to become plaintiffs. While any plaintiff’s chances of success appear problematic, the prospect of extensive discovery, including testimony of experts, plus potential class actions and the potential for truly major recoveries may tempt many defendants to settle quickly in order to avoid litigation costs and the possibility of a devastating verdict.

There is little doubt that the common law offers potential for devastating plaintiffs’ verdicts. By the same token, however, a comprehensive regulatory system likely will involve broader across-the-board impacts and costs. The question of whether emitters and insurers should support comprehensive regulation or take their chances with common law liability is debatable. The question of whether it might be preferable to have both would not seem to be debatable. The latter result appears possible or even likely unless attention is paid to these issues.

If Congress, or perhaps EPA, were to adopt legislation or regulations that preempted or displaced federal common law liability, such action could alleviate the common law litigation risks facing major GHG emitters (and their insurers). Slow progress in the legislative and regulatory arenas, the possibility that a legislative or regulatory solution will be deemed incomplete by the courts and lack of clarity regarding Congressional or agency intent could increase momentum for common law litigation, even in the presence of new legislation or regulations. Absent careful attention to this specific point on both the

administrative and legislative fronts, companies could wind up with both federal compliance obligations and federal common law liabilities. The litigation wave could continue to swell and break over affected entities.

If litigation does occur, it will bring one of the battlefields of environmental law – insurance coverage – to the fore once again. Prominent policyholder attorneys have already stated that there is clearly coverage of at least defense costs and, depending on the type of claim, indemnification for damages as well.<sup>2</sup>

However, the issue may not be that clear cut. Given that the Supreme Court has found GHG to be a “pollutant,” it would appear difficult to implicate policies that have the “sudden and accidental” or so-called absolute pollution exclusions. Insurers’ counsel quoted in a *Law 360* article emphasized their belief that pollution exclusions will preclude coverage for defense costs in GHG suits. Policies not containing these exclusions may be more likely to be implicated, although complex allocation issues may arise. In any event, the coverage determination will be quite factually intensive. Further, the emergence of this new area of environmental coverage disputes should give any company pause in agreeing to “policy buy-back” settlements in current coverage disputes.

The foregoing suggests that at least three steps are essential for any entity that is involved or has the potential of involvement in climate change litigation. First, insurance coverage, and the impact of prior environmental coverage litigation, should be carefully assessed. Second, a concerted effort to persuade EPA to clearly describe the anticipated effect of its regulations and, where appropriate, include preemption of federal common law language in its regulations should be made, while insured GHG emitters will want to guard against regulatory statements that may prejudice either liability or coverage issues. Insurers should have a wide range of coverage-related concerns but share a common interest with their insured in avoiding liability and preempting federal common law. Finally, a concerted effort should be made to persuade Congress to take the threat of common law liability into account in its legislative enactments and to include appropriate language regarding liability for both past and future conduct in whatever legislation is ultimately enacted.

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