Section of Environment, Energy, and Resources
AMERICAN BAR ASSOCIATION

# In-House Counsel Committee Newsletter

**Vol. 15, No. 1** **April 2014**

## MESSAGE FROM THE CHAIR

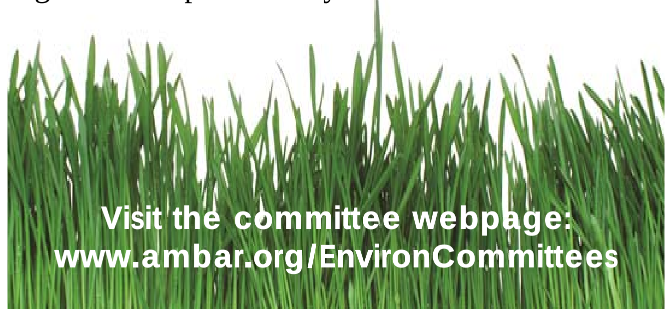
Holli Feichko

I would like to thank our contributing authors and vice chairs, Deonne Cunningham and Seth Jaffe, whose diligent work has produced yet another excellent and timely newsletter. This issue covers a wide variety of topics ranging from current domestic and international environmental issues (such as an update on EPA's audit policy, next generation compliance, and budgetary implications; the expanding reach of the Endangered Species Act; and China's response to the 2013 UN Climate Change Conference in Warsaw) to practical guidance on common and emerging issues (such as the use of the primary jurisdiction doctrine to defend litigation involving contaminated sites; how manufacturers may respond to shareholder sustainability proposals under SEC Rule 14a-8; and retail electric supply agreement basics and negotiations tips. My continued hope is that In-House Counsel Committee members will find our newsletters interesting and useful.

I would also like to thank the panelists and committee members Peter Wright, Sheila Deely, and Paula Schauwecker for their excellent work on the "How to Get Hired by In-House Counsel" panel at the 2013 SEER Fall Conference in Baltimore, Md. For those who may have missed the conference, the panel illustrated the outside counsel selection process based on competing pitches from outside counsel teams (composed of representatives from a hypothetical big firm and a hypothetical boutique firm) to take on a hypothetical litigation matter for an imaginary corporation. During the panel, the in-house counsel panelists offered tips for getting hired by in-house counsel, including best practices and frequent mistakes to avoid. The materials for the panel also included tips from outside counsel on marketing techniques. The program materials are available under "Related Resources" on the In-House Counsel Committee website: http://apps.americanbar.org/dch/committee.cfm?com=NR506000.

I also hope you will join us for an upcoming roundtable discussion on how to succeed as in-house counsel. Details on this program will be available soon on our website.

On behalf of the committee's leadership, I encourage and welcome your ideas for additional articles, programs, and other mechanisms to engage on issues critical to in-house counsel. I also invite you to join us at upcoming SEER conferences, such as the Fall Conference in Miami, Florida, October 8–11. http://www.americanbar.org/calendar/2014/10/22nd-fall-conference.html. I also hope that you will enjoy the programming, particularly those organized or sponsored by the committee.



**In-Housel Counsel Committee Newsletter**
**Vol. 15, No. 1, April 2014**
***Deonne Cunningham and Seth Jaffe, Editors***

**In this issue:**





AMERICAN BAR ASSOCIATION
## SECTION OF ENVIRONMENT, ENERGY, AND RESOURCES

## CALENDAR OF SECTION EVENTS

May 2, 2014
**State of the Practice Symposium**
Vanderbilt University Law School
Nashville, TN

May 2-4, 2014
**Spring Council Meeting**
The Hutton Hotel
Nashville, TN

May 29, 2014
Key Environmental Issues in US EPA Region 2
Primary Sponsor: New York State Bar Association
Columbia Law School
New York, NY

June 4-6, 2014
**32nd Annual Water Law Conference**
The Red Rock Resort, Casino and Spa
Las Vegas, NV

August 8-10, 2014
**ABA Annual Meeting**
Sheraton Boston Hotel
Boston, MA

October 8-11, 2014
**22nd Fall Conference**
Trump National Doral Miami
Miami, FL

**For full details, please visit www.ambar.org/EnvironCalendar**

## THE SEC'S ENCOURAGEMENT OF "SUSTAINABILITY" PROPOSALS UNDER RULE 14A-8: HOW MANUFACTURERS CAN ADAPT

Patrick Daugherty and Daniel Pieringer

As concern about the environmental impact of manufacturing grows, the long-term success of a manufacturer may depend, in part, on its strategies for sustainability. But these strategies are not created and perpetuated in a vacuum. Increased shareholder activism regarding sustainability has the potential to affect any public company's approach, and recent changes in how the SEC looks at shareholder sustainability proposals are giving shareholder activists a bigger voice. Manufacturers need to consider taking appropriate steps to adapt to the new environment.

### Rule 14a-8

Public companies answer to their shareholders in numerous ways. One way in which shareholders may request company action is by making proposals in accordance with what is known as Rule 14a-8, adopted under the Securities Exchange Act of 1934. *See* 17 C.F.R. 240.14A-8, *available at* http://www.ecfr.gov/cgi-bin/text-idx?c=ecfr&rgn=div5&view=text&node=17:3.0.1.1.1&idno=17#17:3.0.1.1.1.2.87.226. Under Rule 14a-8, a shareholder that otherwise satisfies the rule's prerequisites may submit a "recommendation or requirement that the company and/or its board of directors take action" for inclusion in the company's proxy materials.

Not every proposal, however, results in a shareholder vote. By objecting to the SEC, companies may exclude proposals on one or more of the grounds stated in Rule 14a-8. For example, companies may exclude recommendations that are "vague and indefinite," or that arise from "personal grievance[s]." The most common ground for exclusion allows a company to keep a proposal out of its proxy materials if the proposal "deals with a matter relating to the company's ordinary business operations."

### Sustainability Proposals

Shareholder proposals cover a broad scope of topics, ranging from diversity to poison pills to voting processes. Increasingly, these proposals address "sustainability," which generally encourages acting responsibly and adhering to environmental, social, and economic policies so as to create a sustainable future. In 2012, shareholder proposal submissions grew by more than 6 percent over the year earlier, and the trend is continuing. Gibson, Dunn & Crutcher LLP, *Shareholder Proposal Developments During the 2013 Proxy Season, available at* http://www.gibsondunn.com/publications/Documents/Shareholder-Proposal-Developments-2013-Proxy-Season.pdf. According to an Ernst & Young report, environmental and social policy proposals were the largest category, representing almost 40 percent of all proposals. Ernst & Young, *Taking Flight: Environmental Sustainability Proposals Gain More Attention* (2013), *available at* http://www.ey.com/Publication/vwLUAssets/Environmental_sustainability_proposals_gain_more_attention/$FILE/EnvironmentalSustainabilityGainAttention.pdf. The same report indicates that 35 percent of these environmental and social policy proposals sought enhanced disclosure and other company actions regarding environmental sustainability. Furthermore, sustainability proposals are getting increased voting support among shareholders. Environmental and social policy proposals received about 20 percent support from shareholders in the 2013 proxy season, twice the level of support in 2005, according to the report.

Historically, companies were able to exclude most of these types of proposals from their proxy materials by asserting that the proposals dealt with the company's ordinary business operations. SEC Staff (the Staff), who review company requests for exclusion under Rule 14a-8, granted requests to exclude a proposal whenever the company could show that the proposal called for an "evaluation of risk." According to the then-operative Staff analysis, an evaluation of risk amounted to ordinary business operations. SEC Staff Legal Bulletin No. 14E (Oct. 27, 2009), *available at* http://www.sec.gov/interps/legal/cfslb14e.htm. While the Staff clarified in a 1976 release that proposals dealing with significant policy issues could not be excluded, "evaluation of risk" proposals did not fall in that category.

Those days, however, are over. In 2009, the Staff changed its analysis. A Staff legal bulletin issued that year stated that the Staff's position before 2009 resulted in "the unwarranted exclusion" of proposals that in some way relate to evaluation of risk, but that also focus on significant policy issues. SEC Staff Legal Bulletin No. 14E (Oct. 27, 2009), *available at* http://www.sec.gov/interps/legal/cfslb14e.htm. Instead, the Staff would look at the subject matter of the risk and whether that subject matter involves a matter of ordinary business to the company, rather than the mere fact that the proposal involved an evaluation of risk.

The pre-2009 analysis allowing companies to exclude proposals calling for risk assessment made it easy to exclude sustainability proposals because, as the Staff noted, "most corporate decisions involve some evaluation of risk." The new analysis raised the bar significantly. If the subject matter "transcends day-to-day business matters and raises policy issues so significant that it would be appropriate for a shareholder vote," then it generally will not be excluded under Rule 14a-8, provided there is a "sufficient nexus" between the nature of the proposal and the company's operations.

As a result, more shareholder sustainability proposals are making it into proxy statements. In a 2010 no-action letter (a Staff letter allowing a shareholder proposal), the Staff rejected a request from PPG Industries, Inc., which manufactures paints, coatings, glass and optical products, to exclude a proposal requesting a report on "how the company ensures that it responsibly discloses its environmental impacts in all of the communities in which it operates." PPG Industries, Inc., SEC No-Action Letter (Jan. 15, 2010), *available at* http://www.sec.gov/divisions/corpfin/cf-noaction/2010_14a-8.shtml. Later that year, Chesapeake Energy Corporation, the second-largest producer of natural gas, was required to include in its proxy materials a proposal requesting a sustainability report. Chesapeake Energy Corp., SEC No-Action Letter (Apr. 2, 2010), *available at* http://www.sec.gov/divisions/corpfin/cf-noaction/2010_14a-8.shtml. Similarly, in 2012, the Staff denied Cleco Corporation's request to exclude a proposal requesting a sustainability report from the energy services company. That proposal narrowly missed adoption, with 45.6 percent of the shareholder vote favoring the proposal. Cleco Corp., SEC No-Action Letter (Jan. 26, 2012), *available at* http://www.sec.gov/divisions/corpfin/cf-noaction/2012_14a-8.shtml.

Proponents of shareholder proposals requesting disclosure about matters relating to climate change have been particularly successful in avoiding exclusion. Earlier this year, PNC Financial Services Group was unable to exclude a proposal requesting the company's "assessment of the greenhouse gas emissions resulting from its lending portfolio and its exposure to climate change risk in its lending, investing, and financing activities." PNC Financial Services Group, Inc., SEC No-Action Letter (Feb. 13, 2013), *available at* http://www.sec.gov/divisions/corpfin/cf-noaction/2013_14a-8.shtml. Although PNC is not itself a manufacturer, this decision and the other recent ones like it mark a significant shift—one that will continue to have an impact on manufacturers.

Despite the apparent SEC transition toward requiring that more shareholder proposals be put to vote, the SEC still has exercised its authority to exclude some proposals dealing more generally with sustainability. For instance, the Staff allowed FLIR Systems, Inc., a thermal imaging systems manufacturer, to exclude a proposal requesting a report on the company's strategies on energy use management because the proposal focused not on sustainability but rather on "FLIR's strategies for managing its energy expenses." FLIR Systems, Inc., SEC No-Action Letter (Feb. 6, 2013), *available at* http://www.sec.gov/divisions/corpfin/cf-noaction/2013_14a-8.shtml. This decision indicates that, while sustainability is considered a significant policy issue by the Staff, cost reduction remains a matter within the company's ordinary business operations under Rule 14a-8. Similarly, a proposal requesting a report on an energy utility's use of renewable energy was excluded due to its relation to the company's "choice of technologies," and another proposal requesting a summary of plans to eliminate the release of mercury from a global manufacturer's industrial and consumer products was excluded due to its focus on "product development." FirstEnergy Corp., SEC No-Action Letter (Mar. 8, 2013); Danaher Corp., SEC No-Action Letter (Mar. 8, 2013), both *available at* http://www.sec.gov/divisions/corpfin/cf-noaction/2013_14a-8.shtml.

## Adapting to the Current Environment

Given the current landscape, manufacturers face more, and more expensive, demands from activist shareholders than they faced before. However, management is not without recourse.

One way to respond to the new likelihood of receiving proposals in the area of sustainability is to address shareholder concerns proactively. While traditionally the "ordinary business operations" rationale has been the most common ground for exclusion, a company also can exclude a proposal on the basis that it has "substantially implemented" the proposal's objectives. SEC Rule 14a-8(i)(10), *available at* 7 C.F.R. 240.14A-8, *available at* http://www.ecfr.gov/cgi-bin/text-idx?c=ecfr&rgn=div5&view=text&node=17:3.0.1.1.1&idno=17#17:3.0.1.1.1.2.87.226.

"A determination that the company has substantially implemented the proposal depends upon whether [the company's] particular policies, practices and procedures compare favorably with the guidelines of the proposal." Starbucks Corporation, SEC No-Action Letter (December 1, 2011), *available at* http://www.sec.gov/divisions/corpfin/cf-noaction/2011_14a-8.shtml. If shareholders want something a company reasonably can provide, then the company might prudently get out in front of the official requests, satisfying the shareholders and implementing the requests in a manner that best saves the company time and money.

Relative to this approach, one option is to open a dialogue with shareholders before they make formal proposals. If a company receives a letter expressing concern about environmental sustainability from a shareholder or an advocacy group such as "As You Sow" or the "Rainforest Action Network," the company should consider meeting with the proponent. When companies open a dialogue about the issues that matter to shareholders, the ensuing process can result in a mutually agreeable resolution before a formal shareholder proposal is submitted.

Finally, if a company does receive a formal shareholder proposal, the company should consider the following two courses of action. First, a company can explore procedural grounds on which to exclude the proposal. Sometimes a proposal fails simply because the shareholder that made the proposal does not own enough stock, or has not owned the stock for the requisite period of time to qualify for the shareholder rights provided by Rule 14a-8. *See* Bank of America Corp., SEC No-Action Letter (Jan. 16, 2013), *available at* http://www.sec.gov/divisions/corpfin/cf-noaction/2013_14a-8.shtml. In such a case, the company can ask the Staff to exclude the proposal, and at least postpone the issue.

If the proposal cannot be excluded on procedural grounds, or if the shareholder cures the procedural problem, there remains the option to negotiate. Engaging in a dialogue with the shareholder after a formal proposal has been received can be better than adding the proposal to the company's proxy materials, because the decision can be made, more or less, on consensual terms, without turning shareholders into adversaries by filing an exclusion request with the SEC.

Negotiating to an agreed-upon result, and thereby mooting the proposal, is a common result in this particular area of shareholder activism. An increasing number of proposals are being withdrawn after successful negotiation. In fact, environmental and social policy proposals have the highest percentage of proposals withdrawn in connection with direct dialogues between the company and its shareholders, according to the Ernst & Young report.

## Conclusion

As companies realize that there is market value in transparency, they are becoming more willing to provide disclosure on sustainability matters. This is a realization that can benefit manufacturers in the near term as shareholder activism continues to increase and the SEC continues to favor inclusion of sustainability shareholder proposals. Companies should be ready to meet the movement head-on. By being aware of these developments and being open to dialogue about shareholder sustainability concerns, manufacturers can save time and money, maintain strong relationships with their shareholders, and position themselves well for long-term, sustainable success.

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# USE OF THE PRIMARY JURISDICTION DOCTRINE TO DEFEND LITIGATION INVOLVING CONTAMINATED SITES

Gary P. Gengel, Kegan A. Brown, and Robert J. Denicola

## I. Introduction

Private litigation seeking to require defendants to investigate or remediate contamination, or reimburse past and future cleanup costs is often expensive and lengthy. Such cases present highly technical issues relating to the source, nature, and extent of contamination, how best to address the contamination, and which party or parties should pay for the remediation. When contaminated site litigation occurs at a site already involved in the regulatory process, the potential exists that the plaintiff will obtain a court ruling or remedy that is inconsistent with what would be required or determined by the administrative agency overseeing the process. As discussed below, in these types of cases, defendants may be able to invoke what is known as the "primary jurisdiction doctrine" to stay or dismiss private claims that would undermine an ongoing regulatory process.

## II. Primary Jurisdiction Doctrine

The doctrine of primary jurisdiction is designed to preserve a proper working relationship between courts and administrative agencies. Primary jurisdiction is a discretionary doctrine that a court may invoke to stay or dismiss a party's claims. While there is no "fixed formula" governing application of the doctrine, in general, the factors that courts evaluate include (1) whether the issue is a question within an agency's particular field of expertise, (2) whether the issue is particularly within the agency's discretion, (3) whether there is a substantial risk of inconsistent rulings, and (4) whether a prior application to the appropriate agency has been made. *See, e.g., U.S. v. W. Pac. R.R. Co.*, 352 U.S. 59, 62–63 (1956); *Raritan Baykeeper v. NL Indus., Inc.*, 660 F.3d 686, 691 (3d Cir. 2011); *Town of New Windsor v. Avery*

*Dennison Corp.*, No. 10 CV 8611, 2012 WL 67791 at *8 (S.D.N.Y. Mar. 1, 2012).

## III. Relevant Environmental Laws

Litigation involving contaminated sites often involves claims under the Resource Conservation and Recovery Act (RCRA) or the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) (or their state analogs). A brief summary of the pertinent portions of these federal statutes is discussed below.

### A. RCRA

RCRA allows private parties to commence a civil action against any person "who has contributed or who is contributing to the past or present handling, storage, treatment, transportation, or disposal of any solid or hazardous waste which may present an imminent and substantial endangerment to health or the environment." 42 U.S.C. § 6972(a)(1)(B), *available at* http://www.gpo.gov/fdsys/pkg/USCODE-2009-title42/html/USCODE-2009-title42-chap82.htm. Under this provision, a court may order the removal of all contamination that poses an imminent and substantial endangerment to human health or the environment. Although RCRA does not allow a private party to recover costs incurred to investigate and remediate a contaminated site, a private party who prevails in obtaining an abatement order may be awarded its attorney and expert fees. 42 U.S.C. § 6972(e), *available at* http://www.gpo.gov/fdsys/pkg/USCODE-2009-title42/html/USCODE-2009-title42-chap82.htm.

### B. CERCLA

Under CERCLA, four categories of parties—collectively referred to as potentially responsible parties (PRPs)—may be held responsible for the costs to investigate and remediate contaminated sites: (1) current owners and operators; (2) former owners and operators at the time of disposal of the hazardous substance; (3) any party who arranged for the disposal, treatment, or transportation of a hazardous substance to the site; or (4) any party who transported a hazardous substance to the site. 42 U.S.C. § 9607(a), *available at* http://www.gpo.gov/fdsys/pkg/USCODE-2009-title42/html/USCODE-2009-title42-chap103.htm. Although not expressly stated in the statute, courts have held that CERCLA liability is joint and several unless a reasonable basis for apportioning liability exists. *Burlington N. & Santa Fe Ry. v. United States*, 556 U.S. 599, 614 (2009). Private parties may assert CERCLA claims against PRPs to (1) recover past investigation and remediation costs, and (2) obtain a declaratory judgment for the reimbursement of all or a portion of future response costs. 42 U.S.C. §§ 9607, 9113(f), (g)(2), *available at* http://www.gpo.gov/fdsys/pkg/USCODE-2009-title42/html/USCODE-2009-title42-chap103.htm.

## IV. Recent Primary Jurisdiction Cases

### A. RCRA

In recent years, primary jurisdiction arguments have been raised against RCRA claims seeking a court order to abate contamination. Intuitively, primary jurisdiction has some appeal for claims seeking a court order to abate contamination if the site is also subject to an administrative order or other regulatory regime to achieve the same objective. As a starting point, courts differ on whether RCRA claims present technical issues best resolved by administrative agencies or whether the existence of the citizen suit provision itself demonstrates Congress's intent to have courts adjudicate such claims. *Compare, e.g.*, *PennEnvironment v. PPG Indus., Inc.*, No. 12-342, 2013 WL 4045794, at *19 (W.D. Pa. Aug. 8, 2013) *with McCormick v. Halliburton Co.*, No. CIV-11-1272-M, 2012 WL 1119493, at *2 (W.D. Okla. Apr. 3, 2012). Given the judicial division, recent RCRA decisions appear to focus on the degree of the regulatory agency's involvement. Where the agency is meaningfully involved, the invocation of primary jurisdiction appears more palatable. *See, e.g.*, *Stratford Holding LLC v. Foot Locker Retail, Inc.*, No. CIV-12-0772-HE, 2013 WL 5550461, at *5–6 (W.D. Okla. Oct. 8, 2013); *McCormick v. Halliburton Co.*, No. CIV-11-1272, 2012 WL 1119493, at *3 (W.D. Okla. Apr. 3, 2012). This result is not surprising, as one would expect courts to be hesitant to invoke primary jurisdiction where agency involvement is either lacking or the court is concerned about the progress of the remediation.

## B. CERCLA

By contrast, at first glance, primary jurisdiction might appear less applicable in CERCLA cases, where the plaintiff is seeking reimbursement of past response costs and a declaration regarding the defendant's share of future response costs—as opposed to the RCRA cases discussed, where plaintiffs sought an affirmative order to investigate and remediate the contamination. Two recent cases, however, demonstrate that the primary jurisdiction doctrine may be successfully invoked to defeat cost recovery and contribution claims for cleanup costs.

In *Asarco v. NL Industries*, Asarco asserted a CERCLA contribution claim against several defendants for their alleged share of response costs and natural resource damages (NRDs) with respect to the so-called Tri-States sites in southwest Missouri, southeast Kansas, and northeast Oklahoma. No. 11-00138, 2013 U.S. Dist. LEXIS 43013, at *3–6 (W.D. Mo. Mar. 18, 2013). In evaluating the defendants' primary jurisdiction argument, the court explained that the Environmental Protection Agency (EPA) had not yet completed its investigation of the sites and determined a final remedy. Therefore, "the amount of total liabilities, a prerequisite to a contribution right," was not known. Given that Congress intended EPA to determine the nature and scope of to remediate contamination under CERCLA, the court held that adjudicating Asarco's CERCLA contribution claim would "waste the parties' and this Court's resources," and "could lead to inconsistent judgments." As a result, the court invoked the primary jurisdiction doctrine to stay Asarco's contribution claim until, among other things, EPA completed its investigation, determined a final remedy, and calculated NRDs.

Another court employed similar reasoning in *Magic Petroleum Corp. v. Exxon Mobil*, a New Jersey state case where the plaintiff sought contribution under the Spill Compensation and Control Act (Spill Act), New Jersey's analog to CERCLA. No. A-1218-10T1, 2011 N.J. Super. Unpub. LEXIS 2021 (N.J. Super. App. Div. July 26, 2011). Although the court acknowledged that the plaintiff had a statutory right to contribution under the Spill Act, it dismissed the contribution claim under the primary jurisdiction doctrine because "[p]rior to adjudicating the possible liability of the parties, the scope and nature of that liability must be determined" and "only the [N.J. Department of Environmental Protection] can define the contaminants, determine the extent of the discharge, identify the authorized forms of investigative testing, and the permissive methodology of cleanup." Simply put, the court held that "until the DEP agrees the investigation properly identifies the scope of the cleanup and approves the methodology for proper remediation, the court cannot properly determine contribution," without exposing the defendant to inconsistent rulings and possibly interfering with the agency's regulatory process.

## V. Takeaways

Investigating and remediating a contaminated site often is a complex process that takes years or decades to complete. Where parties have agreed to undertake that process with agency oversight, the prospect of having the regulatory regime upset by private litigation is, to say the least, troubling. In light of EPA's well-publicized decision to drastically cut enforcement over the next four years, there may be an increase in private litigation involving contaminated sites.

Importantly, companies defending RCRA and CERCLA claims involving contaminated sites may be able to invoke primary jurisdiction to stay or dismiss the plaintiff's claims. If successful, concurrent costs to defend the litigation and complete the regulatory process would be avoided. While primary jurisdiction is a discretionary doctrine and will inherently depend on the unique facts at issue, recent case law suggests that the chances of successfully invoking the doctrine are increased if any of the following factors are present: (1) the agency is actively involved in the investigation or remediation of the site; (2) a final remedy has not been selected for the site; or (3) the nature and extent of contamination is not fully delineated.

To avoid exposure to private litigation, companies should consider what strategic steps, if any, can be taken at their site to lay the groundwork for potential application of the primary jurisdiction doctrine, including documenting (1) that the company has been working closely with the regulatory agency; (2) that the company has complied with agency requests and direction; (3) that the company and agency have agreed on a conceptual framework and remedial approach to address site impacts (e.g., source removal followed by monitored natural attenuation); and (4) that the litigation may result in delays and potentially an inconsistent remedy or irreconcilable liability determinations at the site. While establishing any specific set of facts does not guarantee that a court will agree to invoke primary jurisdiction, the chances of success likely increase if the court finds that the regulatory process is moving forward with a schedule and purpose.

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## RETAIL ELECTRIC SUPPLY AGREEMENT BASICS AND NEGOTIATION TIPS

Sameer A. Ghaznavi and Kyle Hermanson

### I. Introduction

If you have lived in the United States over the past 40 years, you have probably heard countless discussions of deregulation in the power industry. Deregulation generally refers to the removal of government control over price setting and entry and exit rules in an industry. It has been a hotly discussed political topic for decades as the federal government and various states have debated which industries, if any, should be deregulated. As a result of these debates, 15 states and the District of Columbia decided to deregulate their electricity markets, according to the Energy Information Administration. *See* Map, *available at* http://www.eia.gov/electricity/policies/restructuring/restructure_elect.html. This article is intended to serve as a brief introduction for in-house counsel about the value of retail electric supply to a corporation and the basics of negotiating a retail electric supply agreement in deregulated markets.

### II. The Demonstrable Value of Retail Electric Supply Agreements

Retail electric supply agreements provide a way for in-house lawyers to get entrenched in their company's business and help add value by creating profits or realizing tangible savings. As in-house counsel, we can be asked to provide advice on everything: marketing materials, contracts, leases, employment issues, disputes, and more. Our value largely stems from our ability to foresee risks and help our company avoid them. However, the value of avoided costs is often under-appreciated and overlooked, even when our assistance averts catastrophic damage to the company's bottom line. Ultimately, when it comes to performance reviews and review of the annual "Legal" budget, it can be difficult to prove the true monetary value of our counsel. If your company has offices in one of the 15 U.S. deregulated states or the District of Columbia, one way you can show commitment to the bottom line is to facilitate an internal discussion about the possibility of switching from a default utility electricity supply to a contracted rate with a competitive retail electric supplier.

Retail electricity suppliers are companies that purchase electricity in bulk quantities from the wholesale market and then resell that electricity to consumers at the retail level. Based on the amount of electricity used at your company's sites, the difference in rates between your default electricity supplier and a retail electric supplier can mean significant savings for your company that you, in turn, can use to demonstrate the Legal Department's positive impact on the company's bottom line.

## III. Helpful Tips for Finding and Selecting a Retail Energy Supplier

Due to market conditions, competition between retail energy suppliers has stiffened recently, so you should begin the process by requesting that your procurement or supply chain group research the market in your area and facilitate an RFP (request for proposal) process. There are multiple retail suppliers in every deregulated market, making the procurement process similar to that for most other services. Suppliers offer a variety of power products (see section IV for a discussion of a few of the most popular) and the best product for your company may be different for each site, depending on the type of facility and the site's power usage patterns. The length of a typical electric supply agreement ranges from a one-year to four-year term. Therefore, it is important to find a credible, creditworthy supplier who will not encounter any difficulties in purchasing and delivering power for the entire duration of the term. Recent history suggests that it is probably safe to assume that power prices are likely to be higher in the future, so if your supplier fails to deliver, you may be forced to recontract with a new supplier at a much higher rate, losing some the value you generated in the initial contract.

## IV. Common Types of Retail Electric Supply Agreements

Retail electric supply agreements can take several different forms. Below are brief summaries of a few of the most popular types:

- Fixed rate: Fixed-rate contracts give both consumers and retailers the stability they desire. The downside is that they open either party to losing money if the market creates more favorable rates than the fixed rate, leaving one party short of its projected savings or profits. Customers can bargain for a fixed price "all in" agreement (includes all distribution and capacity charges) or fixed price with pass-through pricing for distribution and capacity. For fixed price with pass-through pricing contracts, customers should take care to ensure that the supplier does not add a markup or margin to the distribution and capacity charges, as these are usually passed through at cost.
- Variable rate: Variable rate contracts allow consumers to take advantage of market lows; however, they do not protect against market highs. The price is based on an index price plus a fixed "adder" that is negotiated between the supplier and the customer. Often, this adder will be higher if you price the agreement through a broker because you will pay for the broker's commission.
- Block and index: Block and index contracts are a combination of fixed rate and variable rate contracts. Based on the consumer's usage, the consumer will pick a "block" of energy that will be sold at a fixed price. Any additional usage by the customer will be priced at a variable rate (with adder). This form of contract allows consumers with control over their usage to take advantage of market conditions by increasing usage when the market is low and using the block as a floor to power baseline operations.

## V. Negotiating a Retail Electric Supply Agreement

When you and your supply chain group have picked the most suitable product and found a supplier, you will need to review and negotiate your retail electric supply agreement. Here is a list of terms and conditions that are commonly negotiated and tips and tricks for negotiating a favorable agreement:

- Auto-Renew and Holdover: Retail contracts usually contain auto-renew and holdover language. The auto-renew provision will result in contract renewal at the end of term, but at a new (usually higher) rate. The holdover clause determines the price you will pay if you continue on a month-to-month basis with the supplier rather than renew. A holdover occurs when you opt out of renewal and fail to switch to a new supplier upon expiration of your current retail electric supply agreement. Rather than negotiate the notice period or holdover rates, it is fairly standard for customers to delete the auto-renew and holdover sections. This deletion will generally be accepted by suppliers since all it means is that the customer and the supplier will renegotiate a renewal prior to the end of the term. However, counsel should note that in certain service areas it may be beneficial for the customer to retain the holdover language. Without a holdover clause, in these service areas, if the customer fails to sign with a new retail supplier before the expiration of its current retail electric supply agreement, the customer could be dropped back to the default supplier (the local utility company) and forced to stay with that utility for a minimum period of time (usually several months) before being permitted to switch to another supplier. This can mean significant lost savings for the customer, since utility prices are generally higher than retail suppliers' prices.
- Force Majeure: Regulations governing the supply of power are constantly evolving. While a change in law provision is usually included in retail supply agreements, it often favors the supplier. It is an industry standard to allow suppliers to pass through any additional costs incurred as a result of a change in law, since these costs would be passed on to the customer irrespective of the customer's supplier. However, counsel should ensure that their contract is clear on what is included in the contract rate and should try to negotiate a term such that a change in law will not subject those elements to change. While it can be difficult to get the supplier to agree to a mutual change in law provision (industry standard could possibly be a one-way street, you can (and should) ensure that the contract terms are clear on what is included in the contract price, irrespective of whom the utility or electric distribution company chooses to bill.
- Interest Rates on Late Payments: Interest rates on late and disputed payments can vary from 6 percent to 20 percent. Be careful of lower interest rates that are coupled with a clause including language such as "higher of [the percentage] or maximum permitted under applicable law." Industry standard is to accept the "lower of" 6 percent to 10 percent per annum or maximum permitted under applicable law.
- Ability to Dispute Correctness of Invoices: Often, retail supply agreements will include language limiting the period within which you can dispute an invoice. Here, there are two considerations to balance: (1) withholding payment of disputed amounts; and (2) extending the period within which you can dispute an invoice to a reasonable time for your business counterparts to adequately review and respond. Industry standard is to receive between 60 and 90 days to dispute an invoice, provided that you can withhold on [on?]net disputed payments from amounts owed.

- Usage Variance: For fixed-price contracts, retailers base price on expected usage (how much power you will use during the year), consumption patterns (how your usage varies from hour to hour, day to day, and season to season), and current market conditions. Retailers expect that your usage and consumption will not change materially over the term of the agreement. Of course, businesses grow and evolve and along with growth and evolution, usage and consumption may change. You can negotiate usage and consumption variance language that will allow your usage or consumption patterns to change without an increase in the contract rate. Industry standard is to allow for a usage variance of 10 percent to 20 percent for commercial customers. However, suppliers are often unwilling to agree to provide a consumption variance band because if the change in consumption is permanent, this can result in significant increases to the cost of delivering power.
- Termination: As with any commodities agreement, in a retail electricity supply agreement, a defaulting party typically must pay liquidated damages to the other party. Where retail electric supply agreements differ from other commodity agreements, however, is that in addition to the usual mark-to-market (contract price subtracted from market price) calculation for the remainder of the expected usage during the term of the agreement, retail suppliers also include "margin" in their calculation of liquidated damages. Margin (a seller's fixed costs and overhead for providing supply) is calculated by the supplier and added to the wholesale market price, the sum of which forms the contract rate. Suppliers add margin to liquidated damages because, unlike similar commodity transactions at the wholesale level, absent a termination of the agreement, the supplier is guaranteed to collect its margin through the term of the agreement. The retail electricity is pre-purchased for the customer at the time of contract formation and the supplier's margins are not subject to change as a result of any changes in the market. Wholesale commodity agreements differ in that market fluctuations at the time of delivery can affect earnings for both parties. Lastly, liquidated damages in retail electric supply agreements will also typically include collection costs. A customer's liquidated damages for a supplier default are typically based on a mark-to-market calculation for the remainder of the customer's expected usage through the term of the agreement plus collection costs such as attorneys' fees. You may ask why mitigation efforts (for example, if the supplier finds another customer to take your electricity) do not factor in to help reduce your liquidated damages. Most suppliers will not agree to such provisions, since their business model is based on continuously finding new customers irrespective of a customer default, but it can be a useful part of the negotiation.
- Representations and Warranties: Along with the typical reps and warranties in any commercial agreement, the supplier should represent and warrant that it is a certified and licensed retail electric service provider in the service area.
- Indemnity: Unlike the typical indemnity in a commercial agreement, agreements for the supply of a commodity will usually have indemnities that shift responsibility and liability at the point of delivery; the supplier will retain liability to point of delivery and the customer will have liability afterwards. The supplier will usually not indemnify the customer from the point of delivery because it is actually the utility or electric distribution company (EDC) that is responsible for the delivery of electricity to the site.
- Limitation of Liability: It is standard for liability to be limited in retail supply agreements, usually to the amount of the total bills (or estimated based on expected usage

and contract price) over the term of agreement.

## VI. Conclusion

Retail electric supply agreements are not without risks, but they provide opportunity for legal-initiated cost savings for companies in deregulated states. The unique characteristics of retail electric agreements and the variety of available products make it important that in-house counsel understand the implications of otherwise “standard” terms and conditions.

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## ENDANGERED SPECIES: COMING SOON TO A PROJECT NEAR YOU

W. Parker Moore and Sara L. Vink

The Endangered Species Act (ESA) may not be at the top of the environmental law news cycle these days, but recent developments suggest that maybe it should be. While the ESA and its implementing regulations continue to provide the same strict regulatory framework they always have, the statute’s reach is expanding dramatically. Because of recent settlement agreements between the federal government and environmental groups, hundreds of new species likely will be classified as threatened or endangered over the next few years. The result? ESA restrictions will spread into areas of the country the statute previously has not reached and heightened restrictions will further limit activities in areas that it has. For these reasons, it is critical for project proponents and stakeholders in all industries to be aware of these developments and to identify strategies for handling the stampede of new threatened and endangered species listings that are coming.

### Background: The Endangered Species Act

Congress passed the ESA in 1973 to protect and recover imperiled species and the habitats on which they depend. The statute works to achieve those goals in several ways beginning with a federal listing of a species as threatened or endangered.

When defined criteria are met, the U.S. Fish & Wildlife Service (FWS or the “Service”), which administers the ESA on land areas of the United States, must list a species as threatened or endangered. The species listing process is the foundation of the ESA because the statute’s key protections apply only to listed species. The overall goal of the ESA, of course, is to prevent species from going extinct. Thus, the ESA requires FWS to list a species as “endangered” if it is “in danger of extinction throughout all or a significant portion of its range.” 16 U.S.C. § 1532(6), *available at* http://

www.fws.gov/endangered/laws-policies/section-3.html. On the other hand, the Service must list a species as "threatened" if it is "likely to become an endangered species within the foreseeable future throughout all or a significant portion of its range." 16 U.S.C. § 1532(20), *available at* http://www.fws.gov/endangered/laws-policies/section-3.html.

FWS must list a species as threatened or endangered based on the best available science and does not have discretion in making the determination. The listing triggers a number of important protections for the species under the ESA. For example, whenever FWS lists a species, it also must designate critical habitat for the species. Critical habitat is defined as "specific areas within the geographical area occupied by the species . . . essential to the conservation of the species and . . . which may require special management considerations or protection." 16 U.S.C. § 1532(5), *available at* http://www.fws.gov/endangered/laws-policies/section-3.html. When designated, critical habitat is protected through federal agency permitting and authorization processes from development or modification that would jeopardize a listed species.

The listing of a species also triggers the ESA's strict prohibition on any person "taking" the species without authorization. The ESA defines "take" broadly as "to harass, harm, pursue, hunt, shoot, wound, kill, trap, capture or collect, or attempt to engage in any such activity." 16 U.S.C. § 1532(19), *available at* http://www.fws.gov/endangered/laws-policies/section-3.html. The take prohibition is even broader when the regulatory definitions of "harm" and "harass" are considered. FWS defines "harm" to mean any act "which actually kills or injures wildlife," including "significant habitat modification or degradation." 50 C.F.R. § 17.3, *available at* http://www.gpo.gov/fdsys/pkg/CFR-2002-title50-vol1/pdf/CFR-2002-title50-vol1-sec17-3.pdf. The regulations define "harass" broader still to mean an "intentional or negligent act or omission which creates the likelihood of injury to wildlife by annoying it to such an extent as to significantly impair normal behavioral patterns including breeding, feeding or sheltering." Accordingly, the take prohibition bans any person not only from taking action that kills or harms a listed species directly or indirectly, including through impacts to its habitat, but even makes it illegal to annoy one too!

The breadth of the take prohibition is significant because the ESA's enforcement provisions have extremely sharp teeth. Depending on the type of violation and the species involved, an unlawful taking may result in civil penalties, criminal penalties, and even jail time. In addition, the federal government may seize any vehicles and equipment used in the activity that caused the taking and revoke federal operating permits, licenses, and leases related to the activity. As a result, it is crucial to be aware of any listed species that occur in your area of operation or future development and to be able to avoid unauthorized takes of those species and the ESA enforcement actions that accompany them.

## The Gathering Stampede of Listed Species

The ESA's listing process and take prohibition have been in effect for 40 years, but many industries have never been significantly affected by the statute during that time. In most cases, that is because no listed species live in any habitat where those industries operate. That is about to change.

In 2011, FWS entered into broad settlement agreements with the Center for Biological Diversity and WildEarth Guardians to resolve a litany of lawsuits that the environmental groups had brought over the Service's alleged failure to timely address hundreds of petitions to list species as threatened or endangered. Under the settlements, FWS agreed to make listing decisions by 2018 for all species subject to the listing petitions involved in the litigation. As a result, over the next four years, FWS must decide whether to list more than 750 different species. The Service has neither the budget, nor time to do that work properly, with the level of analysis required. Furthermore, it knows that the environmental groups likely will challenge any decisions not to list a species. Therefore, FWS, likely will list the great majority of those species as threatened or endangered.

On account of the settlement agreements, the ESA is entering a period of activity the likes of which have never been seen before. Industry now faces the effects of both a significant increase in the number of species listed and a previously unimaginable increase in the listing rate. In fiscal year 2013 alone, the first year under the settlement agreements, FWS listed 81 new species—12 times more than the total number of species listed throughout the two administrations of President George W. Bush. And that is just the beginning.

Between now and 2018, FWS will consider listing at least three species in every state. But that is the minimum. Some states, such as Florida and Tennessee, are home to well over 100 species for which the Service will be making listing decisions during that time. Other states such as Virginia (75 species), Kentucky (55 species), Nevada (54 species), and California (52 species) fall somewhere in the middle. *See* FWS, ESA Listing Workplan, *available at* http://www.fws.gov/endangered/improving_esa/listing_workplan.html. What's more, unlike the majority of federal agencies for whom Congress imposed significant budget cuts in fiscal year 2014, FWS's budget increased significantly, with $22 million earmarked exclusively to fund the Service's growing ESA species listing efforts.

The bottom line is that the list of protected species under the ESA will balloon in size over the next four years, expanding the statute's reach into areas that previously have not felt its effects. Each new listing will complicate existing business activities conducted in those areas because they will be subject to the ESA's strict regulatory program, and will delay the permitting and authorization process for any activities requiring federal permits or approvals or that rely on federal funds. As a result, when FWS lists a new species in your area, there is a high probability that it will take longer and cost more to do your work.

## Protecting Your Activities from the ESA

Although the spate of listing decisions expected over the coming years has serious implications, you have several options for ensuring compliance with the ESA and minimizing the impact. You should stay informed, participate in the public comment process to help shape accurate listing decisions, take preventive steps to insulate your activities from the effects of future species listings, obtain authorizations to take listed species that occur in your area when appropriate, and establish and maintain excellent contacts within the state and federal regulatory agencies.

### 1. Stay Informed and Participate

As with any regulatory program affecting your work, it is imperative to stay informed of developments arising under the ESA and then to take steps to address expected impacts. One of the best ways to do this is to monitor the *Federal Register* regularly for proposed listing decisions affecting your area so that you are not blindsided by a new species listing.

When you identify a proposal to list a species in your area, take advantage of the opportunity to comment on the proposed listing during the public comment period. While it is important to voice your general position on a proposed listing decision, the most effective comments will demonstrate to FWS a scientific basis why its proposal does not meet the legal and scientific listing criteria of the ESA. Submitting additional biological data about the species that supports your position will make those comments even stronger by building the administrative record that is before the agency and ensuring that FWS has the best available information when making its decision. Helping to build the record is crucial during the species listing process because you can be sure that the groups that support the listing of the species will submit ample comments and data that support the listing. It is important to vet the information they provide, as it can be inaccurate, incorrect, or irrelevant. Without submissions by interested stakeholders to counter such misinformation, however, you run the chance that the Service will improperly factor it into its listing decision. In other words, don't assume FWS will do its homework.

The same rationale applies in those all-too-infrequent instances when FWS receives a petition to list a species under the ESA, but makes an initial determination that the species does not warrant listing. There again, it is crucial for stakeholders to submit comments—but this time supporting the agency's decision. Those pushing FWS to list the species will bombard the agency with information to call into question the proposed "not warranted" decision and urge FWS to change its mind. As a result, if you agree with the Service that the species should not be listed, you should support the agency with comments and data to try to neutralize the information that listing proponents submit. Doing so significantly increases the likelihood that FWS will stand by its proposed "not warranted" determination and create an administrative record that puts the agency in a better position to defend its decision in court when environmental groups challenge it.

### 2. Prepare for the Listing

If it appears likely that FWS will list a species in your area, you may prepare to insulate your activities from the effects of the ESA when the species is listed. The most common strategy is to develop a candidate conservation agreement (CCA). CCAs provide incentives for landowners to conserve species before they are listed by offering assurances that their activities may continue if the species is listed later. Those wishing to enroll in a CCA must develop a plan for carrying out their activities subject to certain restrictions intended to conserve the species at issue. The idea is that with this CCA in place, the species may never need to be listed. But if FWS later decides to list the species as threatened or endangered, CCA enrollees will receive a permit authorizing take of the species incidental to carrying out any activities covered by the agreement (an "incidental take permit").

A more novel, but equally effective, approach is to develop species avoidance protocols that can be incorporated into your project design or into the activities that you conduct. This approach typically is carried out by studying the species and its habitat and the factors affecting them, and then working with species experts and FWS to develop protocols that can be followed to avoid taking the species. Because following the protocols will help avoid impacting the species they are designed to cover, activities may then move forward even if the species is listed without first obtaining take permits or facing the risk of an enforcement action for unauthorized take of the listed species.

### 3. Obtain Incidental Take Permits

If a species is listed in your area before you have had a chance to pursue one of the above pre-listing strategies, you still can insulate your activities from the ESA by obtaining an incidental take permit. To obtain a permit, applicants must develop a habitat conservation plan (HCP) that identifies the impact of the take, steps to minimize and mitigate that impact, the available funding for the plan, alternatives to the proposed activity that will result in taking, and related information. The HCP is submitted to FWS for approval, and the Service must comply with the National Environmental Policy Act (NEPA) before issuing any permits. This option, therefore, requires a significant investment of time and money, but it is far better than facing ESA enforcement action for the unauthorized take of a listed species. In addition, the incidental take permit/HCP option offers another advantage—it provides flexibility to cover multiple listed species, and even unlisted species, under the same plan and permits. Typically, the HCP can later be revised to include other species. This strategy offers a measure of ESA certainty decades into the future.

### 4. Build and Maintain Agency Relationships

Finally, regardless of which of the above strategies you pursue, or even if you do not pursue any of them, you should establish and maintain excellent relationships with state and federal regulators with authority over protected species. Earning a level of trust and collegiality with wildlife regulators will increase the likelihood that they will keep you in the loop about important developments affecting your activities, go the extra mile to assist when you find yourself in a tight spot, and help you work through difficult regulatory and permitting issues. If you do not already have good working relationships with the federal and state wildlife officials in your area, you should take the time to cultivate those relationships, or team up with someone who already has.

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## CHINA'S RESPONSE AND COMMITMENT IN WARSAW

Shufan Sung

Days after Haiyan, the most powerful typhoon in history, tore through the Philippines, the UN Climate Change Conference was held in Warsaw with a hope to keep governments on track toward a global agreement in 2015. In Warsaw, participating governments reached an agreement requiring all nations to take certain preliminary steps to prepare for a broader global climate change agreement [au: agreement?] in 2015. *See* News Coverage of the deal, *available at* http://www.cop19.gov.pl/latest-news/items/un-climate-change-conference-in-warsaw-keeps-governments-on-a-track-towards-2015-climate-agreement. Though many observers criticized the Warsaw Conference for the failure to reach substantial commitments or agreements on concrete mechanisms, and for making it even less likely that the Paris Conference scheduled in 2015 will achieve global commitments for greenhouse gas (GHG) reduction, there was some sparkle in Warsaw. China's government published its first National Climate Change Adaptation Plan (Plan) during the Warsaw Conference, and that is a laudable step in the right direction. *See* the Plan, *available at* http://qhs.ndrc.gov.cn/gzdt/W020131213626583538862.pdf.

### The International Cooperation Under the Plan

China is the world's largest developing country, with the world's largest population and the second largest economy. China's rapid growth has not only made its own ecosystem more fragile, but has also helped push worldwide GHG emissions to a potential breaking point. The widely reported air pollution in most metropolitan areas like Beijing and Shanghai has raised mounting public concerns over health, safety, and the environment. Against this backdrop, nine departments of the Chinese government, including most leading departments in charge of climate change tasks, such as the National Development and Reform Commission (NDRC), Ministry of Finance, and Ministry of Agriculture, prepared the Plan for unveiling at Warsaw.

The publication of the Plan signifies the awareness of the importance of climate change tasks at the highest governmental level, and marks the first time China's government has advanced climate change tasks to such a national strategic position. This is a good sign. Now is the critical time for China's government to consider its international responsibility as the world's largest emitter of GHGs. The Plan reflects a governmental determination to tackle climate change and accelerate adaptation. First, China sets out in the Plan a request that developed countries carry out the duties provided under the United Nations Framework Convention on Climate Change (UNFCCC), and provide the necessary funds, technologies, and action development to developing countries for initiating adaptation plans. China also states that it will actively participate in funding mechanisms within or outside of the Kyoto Protocol framework structure, and sufficiently use funds for establishing its adaption plans through cooperation in projects with other international organizations.

Sui Wei, one of China's leading climate negotiators and director general of the Department of the Climate Change of the NDRC, went on the record after Warsaw to lament that international climate negotiations have not led to meaningful funding for developing nations. In 2013, industrialized countries did not provide any of the $100 billion per year committed under the UNFCCC. *See* News Coverage, *available at* http://www.theclimategroup.org/what-we-do/news-and-blogs/cop19-warsaw-means-of-implementation-is-a-critical-issue-for-china. Perhaps in response to these statements, in Warsaw developed countries agreed to prepare biennial submissions on their updated strategies and approaches for scaling up finance between 2014 and 2020.

Second, under the Plan, China will actively introduce core technologies from other countries to bolster international technology development and transfer mechanisms, and to stimulate its own technology improvement. These remain some of the most pressing issues in implementing adaptation plans. By first absorbing foreign technologies, China readies itself to cultivate its own critical technologies in the long term. China makes clear through the Plan that it believes developed countries should broadly share and transfer core technologies to help developing countries fulfill their obligations in reduction. As technologies are essential and the most needed resource for developing countries, China calls for a cooperative technology-sharing mechanism.

Third, via the "South-South Cooperation"—the experience exchange and technology transfer between developing countries—China will develop adaptation capacities and share knowledge with other developing countries. This "South-South" transfer of technologies will cover many disciplines, including: agriculture production, desertification management, water resources comprehensive management, meteorology and marine disasters prediction and monitoring system development, biodiversity protection, and coastal zone protection. Through the South-South Cooperation, leading developing countries like China, India, and Brazil can form a group to collectively further adaptation technologies.

Last, regarding the Plan's most important element, the call from China to obtain a concrete time schedule for funding, China's primary lead negotiator and the vice chairman of NDRC, Xie Zhenhua, stated that it was a huge disappointment that developed countries did not commit specifically "when, how, and how much" will be paid to developing countries.

### China's Response and Commitment in Warsaw

In Warsaw, China's government repeated its position that it will reduce GHGs on its own timetable, based on its special society and economic model. China's negotiators stated that the purpose of the Plan, and China's overall strategy, is for the country to engage in its own sustainable development for China's future. It appears China has now committed to do this even in the absence of an international agreement. Regardless of international climate negotiations, China will continue to move toward a lower-carbon society. *See* News Coverage, *available at* http://v.ifeng.com/news/opinion/201311/0114f07b-7ef0-4a1e-9075-6f05dfa1c972.shtml.

China's negotiators also pushed back against arguments in Warsaw that it should do more given the size of its economy—the world's second largest. China opposed the arguments by developed countries that it should commit to the same proportional share of GHGs reduction as most industrialized countries. In fact, China still considers itself a developing country and, based on its economic prediction, until 2020 or even 2050, it will remain a fast-growing developing country. Thus China deems it unreasonable to assume the same duties as developed countries; it will continue to resist such calls.

China has further committed that it will keep working on GHG reduction tasks, and increasing adaptation tasks to minimize loss and damage. At the same time, China will develop a disaster monitoring system, and increase both disaster response capacities and public awareness to the response of disasters. However, similar to other countries, China did not commit in Warsaw to "when, how, and how much" emissions reduction it would complete.

Looking back on Warsaw, it is not surprising to see that all countries passed the buck and tried to avoid making real commitments in GHG reduction. While the United States leads the world economy and China chases behind it, the world remains hopeful that an intimate cooperation between the United States and China will play a critical role in the next term of international climate negotiation. China's commitment to keep reducing GHGs and enhance energy efficiency, although not under the international agreement, is a good start. Although China chooses to work on its own way at this stage, it surely opens the gate and welcomes more sharing and transferring in core technologies to help it build its adaptation system. As a result, the technology transfer will continue to be an important area for international energy lawyers to follow.

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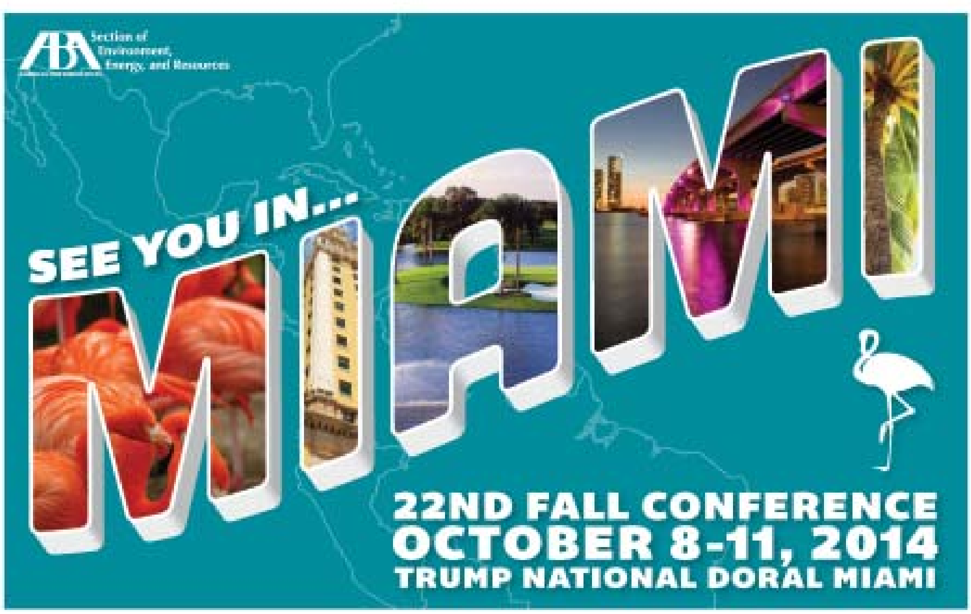

## WHERE ARE WE NOW? EPA'S AUDIT POLICY, NEXT GENERATION COMPLIANCE, AND BUDGETARY IMPLICATIONS

Mary Ellen Ternes

The Environmental Protection Agency (EPA) targeted its Audit Policy, "Incentives for Self-Policing: Discovery, Disclosure, Correction and Prevention of Violations" (*available at* EPA Audit Policy, http://www.epa.gov/compliance/resources/policies/incentives/auditing/) for abandonment in 2012. However, perhaps in response to resounding objections by industry and outside counsel, EPA has not yet dismantled this cherished avenue toward forgiveness.

For counsel productively using the Audit Policy, EPA's announcement that it intended to abandon the policy—particularly in the context of the agency's emphasis on Next Generation Compliance (http://www2.epa.gov/compliance/next-generation-compliance) and budgetary cutbacks in its "boots on the ground" inspections—created significant concern among industry that businesses would be caught in a communication and policy void that would lead to more punitive, yet unnecessary enforcement proceedings. While EPA has stated on its Audit Policy electronic disclosure Web site that it has now removed the possibility of e-reporting, the agency has maintained regulated entities' ability to directly report to regional Audit Policy staff. *See* EPA Audit Policy, http://www.epa.gov/compliance/incentives/auditing/. Hopefully, EPA will continue to recognize the many benefits resulting from its continued support of the Audit Policy, particularly in the context of more remote enforcement strategies, fewer "boots on the ground" inspections, and greater reliance on state enforcement resources.

### Audit Policy—History

In response to numerous states that passed audit privilege legislation, EPA developed an interim policy addressing the scope of "privilege" allowed for voluntary environmental audits and their findings. *See* 60 Fed. Reg. 66,709 (Mar. 31, 1995). S*ee also* State Audit Privilege and Immunity Laws & Self-Disclosure Laws and Policies, *available at* http://www.epa.gov/region05/enforcement/audit/stateaudit.html. Seeking to avoid litigation regarding the scope of privileged environmental audit findings, EPA's interim policy offered incentives to conduct voluntary audits where the audit's findings were disclosed and promptly corrected.

EPA issued its final Audit Policy in 1995, with the stated purpose of enhancing protection of public health and the environment by encouraging regulated entities to voluntarily discover, disclose, correct, and prevent violations of federal law. The benefits offered by EPA's 1995 final Audit Policy included reductions in the amount of civil penalties, possible elimination of gravity-based penalties, and a determination that the agency would not recommend criminal prosecution of disclosing entities. EPA's adoption of the 1995 Audit Policy followed five days of dialogue, hosted by ABA's Section of Environment, Energy, and Resources (SEER, then SONREEL) with representatives from regulated industry, states, and public interest organizations. The stakeholders identified options for strengthening the former interim Audit Policy and the final Audit Policy included changes reflecting insight gained through this ABA dialogue, more than 300 public comments, and EPA's practical experience in implementing the interim Audit Policy. Since adoption of the final Audit Policy, EPA has issued several guidance documents, including EPA's Audit Policy Interpretive Guidance (Jan. 1997); Audit Policy: Frequently Asked Questions (2007); and EPA's Audit Policy: Tailored Incentives for New Owners (Aug. 1, 2008) (all *available at* http://www.epa.gov/compliance/incentives/auditing/auditpolicy.html).

### Enforcement Budgetary Constraints

In the face of the fierce political opposition and severe budgetary cutbacks of recent years, EPA has issued public statements regarding areas where its resources would be cut back or eliminated. Specifically, on April 30, 2012, EPA's Office of Enforcement and Compliance Assurance (OECA) issued its "National Program Manager (NPM) Guidance" to EPA's regional offices proposing to spend no resources processing self-disclosures under the Audit Policy beginning with EPA's 2013 fiscal year. In the NPM Guidance, EPA stated that internal compliance reviews had become more widely adopted by the regulated community as part of good management and that most violations disclosed under the policy were not in the highest priority enforcement areas for protecting human health and the environment. EPA further explained that it could reduce its investment in the program to a limited national presence without undermining the incentives for regulated entities to conduct internal compliance reviews with potentially a modified Audit Policy that is self-implementing. *See* FY2013 OECA NPM Guidance, *available at* http://nepis.epa.gov/Exe/ZyPDF.cgi?Dockey=P100F6FG.PDF.

With the issuance of the NPM Guidance came a strong response by regulated entities. Members of the national environmental bar, including individual practitioners, the American College of Environmental Lawyers (ACOEL), and the Corporate Environmental Enforcement Council (CEEC), reached out to EPA and requested discussion, urging EPA to retain the Audit Policy. *See, e.g.*, related ACOEL blog postings, *available at* http://www.acoel.org/category/Audit-Privilege.aspx, and CEEC Letter to Cynthia Giles (Feb. 8, 2013), *available at* http://www.eli.org/sites/default/files/docs/seminars/04.16.13telecon/CEECAuditPolicyLtr.pdf?q=pdf/seminars/04.16.13telecon/CEECAuditPolicyLtr.pdf .

Some of the common arguments these attorneys made in defense of continued implementation of the Audit Policy include the fact that the Audit Policy serves as the basis for a continued culture of compliance even in landscape of dynamic changes to industry and regulation and that the Audit Policy has produced quantifiable benefits in achieving compliance, as well as serving as a consistent baseline for states adopting their own audit policies.

### EPA's Promotion of Next Generation Compliance

In 2012, EPA began promoting its Next Generation Compliance initiative. *See* Next Generation Compliance article, *available at* http://www2.epa.gov/compliance/next-generation-compliance. With the Next Generation Compliance initiative EPA is seeking to streamline federal enforcement oversight with regulations that adopt "built-in" compliance, advanced pollution monitoring, electronic reporting, increased transparency, and innovative enforcement strategies. One example of EPA's "built-in" compliance is initial certification of compliance with standards for mobile sources and air pollution control equipment by the manufacturer, rather than by post-installation field testing. Following installation, EPA's approach would use advanced pollution monitoring to evaluate compliance of operating air pollution control equipment. Advanced pollution monitoring would also include fence-line monitoring and remote sensing techniques including infrared cameras. Examples of electronic reporting include National Pollutant Discharge Elimination System (NPDES) electronic reporting. *See* NPDES Electronic Reporting Proposed Rule, *available at* http://www.gpo.gov/fdsys/pkg/FR-2013-07-30/pdf/2013-17551.pdf); EPA's Toxic Release Inventory electronic reporting data base TRI-MEweb, *available at* http://www2.epa.gov/toxics-release-inventory-tri-program. The greater electronic availability of data made possible by electronic reporting, in turn, allows greater transparency of reported data. Finally, innovative enforcement strategies build on advanced monitoring, electronic reporting, and third-party verification, coupled with industry sector approaches, including industry-wide recognition and notification of noncompliance, followed by set compliance deadlines and, if necessary, enforcement.

### EPA's Reduced Enforcement Goals for 2014–2018

On November 19, 2013, EPA published its Draft 2014–2018 Strategic Plan, with public comment ending on January 3, 2014 (*available at* http://www2.epa.gov/planandbudget/strategicplan). Comparing EPA's proposed 2014–2018 enforcement goals to its 2011–2015 enforcement goals shows that EPA intends to significantly cut back on the number of inspections as well as many other enforcement goals. Specifically, EPA is reducing its five-year cumulative inspection-and-evaluation goal from 105,000 inspections to 70,000 inspections. EPA expects to initiate fewer civil judicial and administrative enforcement cases, setting its initiation goal at 11,600 compared to an earlier 19,500, and conclude fewer cases, 10,000 compared to an earlier 19,000.

## Implications of Next Generation Compliance and Reduction in Inspections

EPA's Next Generation Compliance approaches, coupled with significantly reduced inspections, may seem like a relief to some. However, Next Generation Compliance emphasizes remote monitoring methods and automatic electronic reporting, which create the potential to present data without the necessary context required for a full compliance evaluation. Numbers alone do not allow a conclusive compliance determination. Reliance on mere data without the context achieved with an in-person inspection raises risks that enforcement actions, albeit reduced in number, may be allowed to proceed despite facts that militate against taking such action. Of course, this risk varies depending upon the regulatory program and may be less significant where delegated states maintain sufficient budgets for inspections. However, this concern remains magnified where, for example in the Clean Air Act context, qualitative data, such as fence-line monitoring and use of remote infrared cameras, may be relied upon to create a presumption of noncompliance, potentially collected in a manner that is divorced from actual quantitative point-source emission data and permitted parametric operating conditions that facilities rely on to demonstrate ongoing compliance. While regulated entities maintain documentation demonstrating ongoing compliance, the threat remains that such Next Generation Compliance techniques could mire entities in unnecessary enforcement actions where an in-person inspection could preempt such proceedings.

In this uncertain enforcement environment, regulated entities likely will want to continue to directly rely on the assurance provided by EPA's Audit Policy, as well as state audit policies adopted pursuant to, and maintained consistent with, EPA's Audit Policy and its policies and principles.

## Conclusion

As of January 2014, EPA continues to allow regulated entities to avail themselves of EPA's Audit Policy by reporting to named regional EPA Audit Policy staff. Hopefully, EPA's dismantling of its electronic Audit Policy reporting program constitutes sufficient savings to allow EPA's regional offices to continue accepting Audit Policy disclosures.

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