Texas Environmental Update

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Texas Developments

TCEQ To Consider Rule Proposal Increasing Water Fees

On February 11, 2009, TCEQ is scheduled to consider proposed rules that would modify the consolidated water quality fee, the public health service fee, and the water use assessment fee to generate revenue sufficient to support water program activities in fiscal year 2010. The rule proposal would increase both the consolidated water quality fee and the public health service fee and eliminate the reduced fee rate for water rights that authorize amounts above a certain threshold.

The rule proposal is intended to address the depletion of the agency's Water Resource Management Account fund balances due to the decline in general revenue appropriated by the legislature and water-related fees that have remained unchanged for seven to ten years. Among other things, the rules are drafted to allow for the possibility that the existing statutory cap of $75,000 for wastewater permits may be amended by the legislature, and these are intended to incorporate any change to the statutory cap without further rule action. Additional information relating to this rule proposal may be found at http://www.tceq.state.tx.us/rules/pendprop.html.

Texas Governer Perry Again Cautions Against EPA Activism

On the heels of his aggressive response to EPA's proposed framework for regulating greenhouse gas ("GHG") emissions through the Federal Clean Air Act (see December 2008 Texas Environmental Update), Governer Perry used his January 27th "State of the State" speech to once again challenge EPA's regulation of industries important to the Texas economy. "Unfortunately, our strength in petrochemical production and refining makes us a big target on the radar of an increasingly activist EPA, whose one-size-fits-all approaches could severely harm our energy sector," said Governor Perry. He warned that EPA's potential to harm Texas with punitive actions will only increase in the months and years to come. His comments set the same tone as his response to EPA's proposed GHG regulatory framework, which, he said, would "punish innovation, cost jobs and drive investment out of Texas and oversees."

During his speech, Governor Perry promoted several environmental initiatives, including a proposal to give residents in Clean Air Act non-attainment areas a $5,000 incentive towards a purchase of plug-in hybrid electric vehicles and stronger support for Texas' diverse energy portfolio. He noted the state's opportunity in bio-fuels based on its energy expertise, while cautioning against the nation's use of food crops for energy. He encouraged the production of nuclear power in Texas, noting that six potential new reactors are in the planning stages. He also touted Texas' status as the nations leading wind energy producer, but emphasized the need to "build out the transmission and distribution lines, streamline the regulations, and cut the red tape, so we can move this power to where it's needed." The course of these initiatives will be determined, in large part, by the actions of the 81st Texas Legislature.

The Governor's speech can be found at http://governor.state.tx.us/news/speech/11852/

81st Texas Legislative Session Underway

The 81st Texas Legislative Session is now underway and will run until adjournment on June 1, 2009. Bills of interest filed since the December edition of Texas Environmental Update are identified in the attached chart, available at http://www.bdlaw.com/assets/attachments/81st_Legislative_Session_-_Environmental_Bills_of_Interest.pdf.

EPA Approves State Implementation Plan Revision for El Paso County

On January 15, 2009, EPA published approval of a Texas State Implementation Plan ("SIP") revision. The revision consists of a maintenance plan for El Paso County developed to ensure continued attainment of the 1997 eight-hour ozone National Ambient Air Quality Standard ("NAAQS") through the year 2014. The primary purpose of a maintenance plan is to demonstrate how an area will remain compliant with the 1997 ozone standard for the ten-year period following the effective date of designation as unclassifiable/attainment. Since the effective date of El Paso County's attainment designation was June 15, 2004, the plan must demonstrate attainment through 2014. The plan provides for the continued operation of an ozone monitoring network and contingency measures that would be triggered to address any violation of the 1997 ozone NAAQS. Specific contingency measures that would be triggered include vent gas control; control of emissions from degassing or cleaning of stationary, marine and transport vehicles; and control of emissions from petroleum dry cleaning systems.

EPA published the rule without prior proposal as a non-controversial amendment. The rule will be effective on March 16, 2009 without further notice unless EPA receives adverse comment by February 17, 2009. If adverse comments are submitted, EPA will publish a withdrawal informing the public that the rule will not take effect. The Federal Register publication of this action is available on EPA's website at http://www.epa.gov/EPA-AIR/2009/January/Day-15/a708.htm.

Upcoming TCEQ Workshops

TCEQ will be holding emissions inventory and Texas Emissions Reduction Plan ("TERP") program workshops in February. The workshops include the following:

February 10, 2009 -- Emissions Inventory Workshop in Austin to provide guidance for preparing and improving emissions inventory submittals, including discussion of common challenges and demonstrations of the new electronic filing process. Please see TCEQ's website at http://www.tceq.state.tx.us/assistance/events/emissions_inventory.html for additional details.

February 3, 5, 9 and 11, 2009 -- TERP Grant Application Workshops in Austin, Marshall, New Caney and Weatherford. These workshops are sponsored by the Texas Department of Agriculture to encourage participation from the agricultural sector, but anyone interested in the TERP program may attend. Please see TCEQ's website at http://www.tceq.state.tx.us/implementation/air/terp/terp_mtgs.html for more details.

Texas Rules Updates

See TCEQ website at http://www.tceq.state.tx.us/rules/whatsnew.html for information on new rule developments.

National Developments

Obama Directs Environmental Protection Agency To Reconsider Bush Administration Denial Of California Clean Air Act Waiver Request

In his first significant action on global warming, President Barack Obama yesterday issued two executive orders aimed at improving the fuel efficiency of passenger vehicles. The first directed the Environmental Protection Agency (EPA) to reconsider his predecessor's

denial of California's application for a preemption waiver from the Clean Air Act (CAA) to enable the state to set strict automobile emission and fuel efficiency standards. The second directed the U.S. Department of Transportation (DOT) to finalize this Spring its rulemaking to implement 2007 legislation to develop tighter corporate average fuel economy (CAFE) standards for 2011. The second order also directed DOT to undertake a separate rulemaking process in later years that will consider other legal, scientific and technological issues related to climate change.

Obama's directive to EPA quickly fulfilled a major campaign pledge. Last March, after not acting on California's waiver request for several years, former EPA Administrator Stephen Johnson denied the request, concluding that Section 209(b)(1)(B) of the CAA was not intended to allow individual states to set vehicle emission standards to address global climate change. California quickly filed a legal challenge to that decision which is now pending in the U.S. Court of Appeals for the District of Columbia (*California v. E.P.A.*, appeal docketed, No. 08-1178 (D.C. Cir., May 5, 2008). The day after President Obama was inaugurated, California Governor Arnold Schwarzenegger asked the Obama administration to reconsider the EPA's decision denying the waiver. A copy of the Governor's letter can be accessed at http://gov.ca.gov/index.php?/press-release/8596/. California's tailpipe emission regulations themselves are the subject of another lawsuit brought by the auto industry against the state in a U.S. district court in California (*Central Valley Chrysler-Jeep v. Witherspoon*, 2007 WL 135688 (E.D. Cal. 2007)).

EPA's denial of the waiver has prevented California from implementing its 2002 legislation requiring a 30 percent reduction in greenhouse gas (GHG) emissions from passenger cars and light-duty trucks by 2016. As GHG emissions from cars and trucks account for some 40% of the state's total GHG emissions, the so-called "tailpipe emission standards" are a key component of the state's effort to reduce its GHG emissions to 1990 levels by 2020, as required under the California Global Warming Solutions Act of 2006 (AB 32). The California Air Resources Board (CARB), the state agency implementing AB 32, has estimated that the new rules would cut GHG emissions from passenger vehicles 18 percent by 2020, and 27 percent by 2030.

At least 13 other states plan to implement California's tailpipe emission standards if the waiver is granted. The 13 states that have adopted California's standards but, like California, cannot enforce them absent an EPA waiver are Arizona, Connecticut, Maine, Maryland, Massachusetts New Jersey, New Mexico, New York, Oregon, Pennsylvania, Rhode Island, Vermont and Washington. Other states, including Florida, Iowa, North Carolina and Utah, are considering adoption of the standards.

To be clear, **Obama's executive order does not require EPA to grant California's waiver request**. Rather, it requires EPA to undertake a legal process to reconsider the denial of the waiver. This raises several legal issues.

First, while policies change with administrations, it's a little more difficult for legal analyses to change. For EPA to reverse its prior decision to deny the waiver request, it will have to develop a legal rationale that explains if not accommodates such a 180 degree shift. The politics have grabbed most of the attention, but there are substantive legal issues involved. Most notably, Section 209(b)(1) of the CAA provides that the waiver must be denied if EPA finds that the State doesn't need separate standards in order "to meet compelling and extraordinary conditions." While climate change is a compelling and extraordinary condition, it is difficult to contend that global warming is unique to California. This issue will have to be resolved, especially if the other states that wish to adopt California's tailpipe emission standards are to be able to do so if EPA reverses course and grants California its waiver.

Second, California's pending lawsuit challenging the waiver denial cannot be ignored. The case has been briefed, and as a matter of jurisdiction, the decision to dismiss or remand it to the EPA at this point lies with the Court of Appeals. Even if the EPA and the State were to decide to withdraw the case, they are not the only parties to the action, as the auto industry has been granted intervenor party status and will be heard on this issue as well.

Third, the public cannot be shut-out of EPA's reconsideration process. Concurrent with

Governor Schwarzenegger's letter to Obama, CARB Chair Mary Nichols sent a letter to the new EPA Administrator, Lisa Jackson, suggesting EPA skip a public hearing because the issue was already extensively noticed and heard, and conduct only a "short supplemental comment period" before granting the state's waiver request. (A copy of CARB's letter can be accessed at http://www.arb.ca.gov/newsrel/arbwaiverrequest.pdf. However, EPA may lack the authority to do that, as Section 209(b)(1) of the CAA requires "notice and opportunity for public *hearing*." There will be opportunities to participate in EPA's reconsideration process, though it is yet not clear what they will be.

One of the issues that is sure to be addressed in the public comments is the contention that it is improper under the CAA as well as unsound economic and environmental policy to allow a "patchwork" of differing state emission standards, and that instead there should be a single federal standard. As noted above, this was one of the primary bases for the EPA's decision to deny the waiver, citing the 2007 federal law to update the CAFE standards setting national fleet average emission requirements. President Obama's second executive order appears to have been aimed at addressing that argument. It directed the DOT to accelerate work in drafting more stringent federal fuel efficiency standards, as required by the 2007 law. The fuel efficiency standard is expected to be finalized by this spring and will require more stringent fleet efficiency standards by 2011 (impacting the industry beginning with the 2012 auto models), and meet the 2007 law's requirement that fleets average 35 mpg by 2020. Last year DOT proposed a rule that would phase-in this goal by requiring a 25% increase in the CAFE standards to an average of 31.6 mpg by 2015.

President Obama's two orders set the stage for a major policy debate at the federal level. The two strands of this policy debate — which will be played-out first in the comments on California's CAA waiver request — are first, the neo-federalism issues that arise when states address climate change differently and whether there needs to a national standard instead; and second, what those national CAFE standards should be. Both involve significant legal and scientific issues as well as economic and environmental policy questions.

Many environmentalists point to the 2007 U.S. Supreme Court decision in *Massachusetts v. EPA*, 549 U.S. 497, which affirmed EPA's power to regulate global warming pollution from motor vehicles, and urge that these issues be resolved by EPA promulgating uniform national emission standards that match California's. In one of her first acts on the job, EPA Administrator Lisa Jackson sent an email to all EPA employees last Friday, January 23, in which she outlined her five major priorities. "Reducing greenhouse gas emissions" was a the top of the list, and she stated that her EPA "will move ahead to comply with the Supreme Court's decision recognizing EPA's obligation to address climate change under the Clean Air Act." It bears mention that thus far the courts that have addressed this issue have concluded that *Massachusetts v. EPA* does support the efforts by individual states to adopt tailpipe emission standards to address climate change — including the California court considering the auto industry's challenge to California's 2002 law. In *Central Valley Chrysler-Jeep v. Witherspoon*, 2007 WL 135688 (E.D. Cal. 2007), the California court upheld California's 2002 tailpipe regulations and disregarded the plaintiff automakers' preemption arguments.

If EPA grants the state's request for an abbreviated comment period and then quickly grants the waiver, CARB has indicated that California's standards could be implemented as soon as this spring. AB 32 establishes an aggressive implementation schedule, and thus CARB is eager to implement the tailpipe emission standards. There is political momentum both to grant California's waiver request and to increase the CAFE standards soon. However, the outcome is not certain. The only conclusion to be drawn at this point is that all concerned should monitor developments closely in the months ahead, and be ready to participate in the upcoming comment period and/or public hearing on EPA's reconsideration of California's waiver request.

For more information, please contact Nico van Aelstyn at nvanaelstyn@bdlaw.com.

OSHA Issues Revised Field Operations Manual

Earlier this month, OSHA issued a revised Field Operations Manual, which entirely replaces

and substantially revises the 1994 existing Field Inspection Reference Manual (FIRM). Based on the OSHA Press Release, the Manual was developed to assist compliance officers conduct inspections and was part of "OSHA's continuing commitment to make its standards and enforcement activities transparent and understandable to all parties." This is the first revision of the original Manual, which was supplemented and modified by numerous additional directives, memoranda and interpretations over the past fifteen years. According to industry news sources, its issuance may have caught not only industry by surprise, but also OSHA inspectors, some of whom criticized the Manual for lacking adequately descriptions of the substance of the numerous changes that were made and complained they were not given advance notice of its development or publication. See, e.g., BNA Occupational Safety and Health Reporter, "OSHA Revised Field Operations Manual to Give Guidance to Compliance Officers" (January 22, 2008). Among the significant changes are a completely new chapter on inspections procedures as well as expanded guidance on violations assessments, including those related violations of the general duty clause. A copy of the manual is available at http://www.osha.gov/OshDoc/Directive_pdf/CPL_02-00-148.pdf.

Fifth Circuit Affirms Royalty Relief for Offshore Oil and Gas Leases

In a major victory for the oil and gas industry, the U.S. Court of Appeals for the Fifth Circuit ruled that the U.S. Department of the Interior's Minerals Management Service ("MMS") cannot require the payment of royalties from certain production on deepwater oil and gas leases issued between 1996 and 2000 in the Gulf of Mexico. *See Kerr-McGee Oil and Gas Corp. v. Allred*, Slip. Op. No. 08-30069 (5th Cir. Jan. 12, 2009).

The Outer Continental Shelf Deep Water Royalty Relief Act of 1995 ("DWRRA") incentivized the development of oil and gas from deepwater leases on the Outer Continental Shelf ("OCS") through relief from paying royalties, *i.e.*, a percentage of revenue, to MMS. Under Section 304 of the DWRRA, certain Gulf of Mexico lessees are entitled to royalty relief up to statutorily-prescribed production volumes of between 17.5 and 87.5 million barrels of oil equivalent per lease, varying by water depth. The DWRRA has been a remarkable success. With the passage of the DWRRA, Congress achieved its goals of spurred development, generated jobs, economic growth, and income for the government, while increasing domestic energy supply.

MMS sought to limit the statutory royalty relief by including a so-called "price threshold" in the leases, such that if commodity prices exceeded certain levels set by MMS, the royalty relief would be terminated. When oil and gas prices increased beyond the threshold, MMS demanded royalty payments on the royalty relief volumes from a number of Section 304 leases. Kerr-McGee sued, claiming that the statutorily-prescribed royalty relief volumes could not be conditioned by the agency and no royalty was owed. The Court agreed with Kerr-McGee and rejected MMS's attempts to collect royalties, holding that the DWRRA granted MMS no authority to limit Congress' clearly established volume-based royalty relief in favor of administratively established price thresholds. The Court analogized the case to *Sante Fe Snyder v. Norton*, 385 F.3d 884 (5th Cir. 2004), where it similarly held that Interior could not restrict Section 304's royalty relief by limiting relief to leases located in fields without existing production or by calculating relief by field rather than by individual leases.

While the decision directly concerns the eight leases obtained by Kerr-McGee, it also affects dozens of other deepwater leases issued to other companies between 1996 and 2000. The Federal Government has offered several different assessments of potentially foregone royalties under the DWRRA; these estimates, ranging from approximately $15 to $53 billion, also tend to rely on projected production that MMS has since deemed optimistic as well as oil and gas prices much higher than used today for Federal budgeting purposes. The Congress already had been engaged in efforts to "recoup" some of the foregone DWRRA royalties as a result of MMS having omitted any price thresholds in the DWRRA leases issued in 1998 and 1999. In an effort to compel those lessees to "renegotiate" their leases and include a price threshold that effectively would have limited the royalty relief, the House passed a measure in early 2007 that would have imposed monetary penalties or barred those lessees from participating in future OCS lease sales. The Senate also considered measures imposing taxes on the affected companies to regain some revenues. The debate in Congress centered on the contractual, constitutional and other legal issues that such

legislation presented. None of these proposed measures has been passed by Congress.

Now that the *Kerr-McGee* decision has expanded the debate to all five years of leases issued under the DWRRA, and in light of Congress' continuing oversight of many Interior programs, it is expected that the new Congress may again focus attention on this issue.

For further information on royalties and related oil and gas issues, please contact Fred Wagner (202) 789-6041, Bill Sinclair (410) 230-1354, or James Auslander (202) 789-6009.

To read the full court opinion, visit www.bdlaw.com/assets/attachments/Kerr-McGee_Decision.pdf.

EPA Finalizes Aggregation Policies under NSR Program

EPA issued a rule that finalizes its proposed policy on "aggregation" under the NSR Program. 74 Fed. Reg 2376 (January 15, 2009). Until now, even by the Agency's own observations, aggregation policies were piecemealed across scores of regulatory interpretations and guidance. EPA did not alter the text of the regulations that currently govern aggregation, but rather interpreted the text of the existing rules.

Aggregation issues come into play primarily as part of the first step of NSR's applicability test to determine whether a change will constitute a major modification. That step involves an analysis of whether the increased emissions of a particular proposed change are significant. 40 C.F.R § 52.21(b)(2)(i). The thrust of the aggregation policy is to ensure that sources include multiple interrelated changes when calculating a change in emissions for NSR purposes, thereby preventing sources from circumventing NSR permitting requirements by dividing up interrelated projects and evaluating each change individually.

Under the policy, facilities are required to group together the emissions resulting from multiple "nominally-separate" activities that are "substantially related" from an economic or technical standpoint. 74 Fed. Reg. at 2377. Activities are "substantially related" if there is "an apparent interconnection—either technically or economically—between the physical and/or operational changes, or a complementary relationship where a change at a plant may exist and operate independently, however its benefit is significantly reduced without the other activity." 74 Fed. Reg. 2378. The Agency rejected the use of the terms 'dependence' and 'viability' to create "regulatory 'bright lines,'" but noted that whether the viability of a physical or operational change is dependent upon another is a "relevant factor" in determining whether projects should be aggregated. *Id*. Although EPA had proposed definitions of "technical" and "economic" dependence in the draft rule, 71 Fed. Reg. at 54,245, 54,246, in the final rule the Agency chose not to adopt the definitions in favor of the case-specific interpretation described here.

The final policy also set forth the Agency's approach to timing. While EPA agreed that that timing alone is insufficient to make findings on aggregation of emissions, the Agency established a rebuttable presumption that assumes that construction activities are not "substantially related" if they have occurred three or more years apart. 74 Fed. Reg. 2380 (January 15, 2009). The Agency stated clearly, however, that it was not also establishing the converse presumption, *i.e.*, that construction activities that occur within three years are necessarily interrelated, although as a matter of practice, it may be difficult to avoid an implicit presumption during NSR review and that look-backs will necessarily need to be at least three years.

EPA withdrew its proposed rule on debottlenecking and took no action on the proposed rule for project netting, both of which were proposed together with the aggregation policies. 74 Fed. Reg. 2460.

The Kid-Safe Chemicals Act: A Significant Potential Change to the Toxic Substances Control Act

The Kid-Safe Chemicals Act ("KSCA"), which was first introduced to Congress in 2005 and reintroduced largely unchanged in 2008, is a likely vehicle for efforts to reform the Toxic

Substances Control Act ("TSCA") and to change United States chemicals policy in the 111th Congress.

This article examines the key provisions of the KSCA and highlights the major proposed changes and their impact on chemical manufacturers. First, the article looks at the background surrounding the development of the KSCA, including three Government Accountability Office ("GAO") reports requested by Senators Frank Lautenberg, James Jeffords and Patrick Leahy. A more detailed, bullet point analysis of all three GAO Reports has been annexed to this report. Following this brief examination of the background, the article examines the KSCA proposed amendments in detail. It concludes with a critical analysis of the proposed amendments and a look to the future Congressional debate on TSCA.

To read the full analysis, please visit http://www.bdlaw.com/assets/attachments/KID-SAFE_CHEMICALS_ACT_ANALYSIS.pdf.

Bisphenol A Developments in 2008: The Year in Review

The potential health effects of bisphenol A ("BPA") have sparked scientific controversy for years, but in 2008 that controversy grabbed the attention of regulators, legislators, litigators, non-governmental organizations, and the general public as never before. The attached article reviews the highlights of the 2008 BPA developments and provides some thoughts about developments expected in 2009.

BPA is a monomer used to manufacture polycarbonate, a hard plastic with many applications, but in 2008 it was best known for use in baby bottles and sports bottles. BPA also is used to manufacture epoxy resins, the protective linings on the inside of food cans. Under some conditions, low levels of BPA can leach out of polycarbonate and epoxy into the contents of the food container, resulting in human exposure.

The BPA controversy revolves around the significance of "low-dose" studies indicating that the chemical may cause adverse health effects at exposure levels orders of magnitude below levels determined to be safe using traditional toxicological methods. Until 2008, no national governmental agency had sufficient confidence in these low-dose studies to express concern about BPA exposures in people. That changed in 2008, and with that change the level of public concern about BPA skyrocketed. FDA became a particular center of attention. The new Congress and Administration may change the approach FDA took in 2008 with respect to BPA.

The full summary can be found at http://www.bdlaw.com/news-461.html.

Sixth Circuit Vacates EPA's Clean Water Act NPDES Permit Exemption for FIFRA-Compliant Pesticide Applications

On January 7, 2009, the Sixth Circuit vacated EPA's 2007 rule exempting certain pesticide applications that are compliant with the Federal Insecticide, Fungicide, and Rodenticide Act ("FIFRA") from the permitting requirements of the Clean Water Act ("CWA") (hereinafter "Final Rule"). *See National Cotton Council v. EPA*, Slip Op. No. 06-4630 (6th Cir. Jan. 7, 2009), available at www.bdlaw.com/assets/attachments/National_Cotton_Council_Opinion.pdf. The CWA prohibits the discharge of any "pollutant" into navigable waters from a "point source" without a National Pollutant Discharge Elimination System (NPDES) permit. 33 U.S.C. §§ 1311(a), 1342. EPA's Final Rule stated that the CWA was ambiguous with respect to pesticides and interpreted the terms "pollutant" and "point source" to support the pesticide exemptions. The Court found that the CWA directly and unambiguously "forecloses the EPA's Final Rule," as more fully discussed below. The result of the vacature, according to the Sixth Circuit, is that "dischargers of pesticide pollutants are subject to the NPDES permitting program" under the CWA. *National Cotton Council*, Slip Op. at 19. This result represents a significant departure from EPA policy and practice.

EPA's NPDES Pesticide Exemptions

EPA's Final Rule was a response to a series of cases, primarily in the Ninth Circuit, that used the CWA citizen suit provision to challenge a variety of pesticide application activities that resulted in some portion of the pesticides reaching water bodies. *See*, *e.g.*, *Headwaters, Inc. v. Talent Irrigation District*, 243 F.3d 526 (9th Cir. 2001) (finding that NPDES permits are required for discharges of residual pesticide remaining in water following application consistent with FIFRA). The Final Rule exempted two types of pesticide application activities from regulation under the CWA's NPDES permit program, as long as the applications were FIFRA-compliant: (1) pesticides applied directly to waters of the United States to control pests such as mosquito larvae and aquatic weeds, and (2) pesticides applied over or near waters of the United States where a portion of the pesticide is unavoidably deposited to such waters in order to target pests effectively. EPA explained its view that, as a general matter, pesticides applied in accordance with FIFRA are not "pollutants" for purposes of the CWA, defined in the CWA to include "chemical wastes" and "biological materials," and thus are not subject to wastewater discharge permitting requirements even if discharged to water bodies. According to EPA, pesticides are not "chemical wastes" because they are beneficial products registered for the purpose of controlling pests, and are designed, purchased, and applied to perform that purpose. Similarly, EPA declined to treat pesticides as "biological materials," because doing so would create an anomaly where biological pesticides would be deemed pollutants while chemical pesticides would not.

In the Final Rule, EPA nevertheless identified "pesticide residuals" as "excess" amounts of pesticide that remain in the water after application and completion of the intended pesticidal effect, and concluded that such residuals are "pollutants" for purposes of the CWA. However, EPA also concluded that such pesticide residuals only become CWA pollutants at some point in time following application, and therefore do not constitute a discharge of a pollutant from a point source at the time of application. As such, EPA determined that pesticide residuals should be treated as non-point source pollutants under the CWA that are exempt from NPDES permit requirements.

Challenges to EPA Final Rule

EPA published its Final Rule on November 27, 2007. Environmental organizations and industry groups immediately challenged the Final Rule by filing petitions for review in every federal Circuit Court of Appeals. Pursuant to an order of the Judicial Panel on Multidistrict Litigation, the petitions for review were consolidated in the Sixth Circuit. *National Cotton Council*, Slip. Op. at 7. The environmental petitioners claimed that EPA exceeded its authority under the CWA in promulgating the rule. Industry petitioners claimed the rule was arbitrary and capricious because it differentiated the treatment of pesticides for purposes of the CWA "pollutant" definition on the basis of whether or not the pesticides were applied in compliance with FIFRA. *Id*. at 9-10. Certain industry groups also filed a motion to intervene in support of the Final Rule.

Sixth Circuit: CWA Not Ambiguous, EPA's Exemptions Flawed

The Sixth Circuit reviewed the rule under the familiar test set forth in *Chevron v. Natural Resources Defense Council*, 467 U.S. 837 (1984), to determine whether the CWA spoke directly to the issues raised. The Court found that, contrary to EPA's position, the CWA was not ambiguous on any of the issues for which EPA had provided interpretations in its Final Rule. The court confined its analysis to a reading of the CWA, declining to analyze explicitly the relationship between the CWA and FIFRA.

"Chemical Waste:" In particular, the Court found that "the plain language of 'chemical waste' and 'biological materials' in [CWA] § 1362(b) to be unambiguous as to pesticides." *National Cotton Council*, Slip. Op. at 12. Focusing first on the "chemical waste" portion of the definition of "pollutant," the Court indicated that not all chemical pesticide uses would constitute "discarded," "superfluous," or "refuse or excess" chemicals, such that their discharge would require an NPDES permit. Instead, the Court concurred with the Ninth Circuit that "so long as the chemical pesticide 'is intentionally applied to the water [to perform a particular useful purpose] and leaves no excess portions after performing its intended purpose[] it is not a 'chemical waste,'" and does not require an NPDES permit." *Id*. at 13 (citing *Fairhurst v. Hagener*, 422 F.3d 1146, 1149 (9th Cir. 2005), which found an NPDES

permit was not required where the pesticide would leave no excess portion in the water after it had achieved its intended purpose of eliminating non-native fish). However, the court noted that "excess pesticide and pesticide residue meet the common definition of waste," as EPA had stated in the Final Rule, and would be considered "pollutants" under the CWA. *Id.* According to the Court, there are "at least" two pesticide application scenarios that fall into this category: (1) terrestrial and aerial applications of pesticides above or near waterways when residual or excess pesticide impacts the water and (2) residual or excess pesticide that remains after direct application to water and completion of the beneficial pesticidal purpose. *Id.*

"Biological Materials:" The court next found that the CWA's use of "biological materials" within the definition of "pollutant" includes all biological pesticides that are discharged to waters of the United States. Rejecting EPA's interpretation that to treat biological pesticides and chemical pesticides differently would be an anomaly, the Court instead found that by specifically using the word "biological materials" instead of "biological wastes" in the definition of "pollutant" under the CWA, Congress demonstrated an intent to treat biological and chemical pesticides differently. Therefore, under the court's analysis, all biological pesticides applied to waters of the United States, even those leaving no residue, are pollutants for which NPDES permits are required. *National Cotton Council*, Slip Op. at 14-16.

Pesticide Residuals: Finally, the court rejected the EPA's conclusion that pesticide residuals, while pollutants, do not require NPDES permits because they are not pollutants at the time of discharge. EPA's position was that the CWA requires permits "only for discharges that are 'both a pollutant, and from a point source' at the time of discharge." *Id.* at 11 (citations omitted). EPA had concluded in the Final Rule that pesticides are applied by point sources. The court found EPA's "[i]nject[ion] [of] a temporal requirement to the [CWA's] 'discharge of a pollutant' [language] not only unsupported by the Act, but [] also contrary to the purpose of the permitting program," which is 'to prevent harmful discharges into the Nation's waters." *Id*. at 17. Instead, the Court held that a "pesticide residue or excess pesticide—even if treated as distinct from pesticide—is a pollutant discharged from a point source" at the time it is discharged. *Id*. at 18.

In sum, according to *National Cotton Council*, NPDES permits are required for "at least" the two categories of pesticide application articulated in EPA's Final Rule, namely, direct and over/near water pesticide applications.

For further information about the Sixth Circuit's opinion and its implications, please contact Karen Hansen (khansen@bdlaw.com, (202) 789-6056), Richard Davis (rdavis@bdlaw.com, (202) 789-6025), Kathy Szmuszkovicz (kszmuszkovicz@bdlaw.com, (202) 789-6037), or Mike Neilson (mneilson@bdlaw.com, (202) 789-6061). This alert was prepared with the assistance of Graham St. Michel.

Renewable Fuel Standard Program Update: EPA Misses December 2008 Deadline, While EU Approves New Renewable Fuel Mandates with GHG Emissions Requirements

Amid continued reports of struggles at the U.S. Environmental Protection Agency (EPA) to develop a methodology for quantifying lifecycle greenhouse gas (GHG) emissions from renewable fuels, the Agency failed to meet a December 19, 2008 deadline set by the Energy Independence and Security Act of 2007 (EISA) for finalizing regulations to implement changes to the federal Renewable Fuel Standard program, known as "RFS2."

Meanwhile, on December 17 the European Union formally adopted its own climate change package, which includes a 20 percent overall renewable energy target by 2020, a specific renewable fuel target of 10 percent by 2020 for transportation fuels for each Member State, a complex lifecycle GHG emissions reduction formula for qualifying biofuels compared to fossil fuels, and GHG reduction targets for fossil fuels in many transportation fuels. In addition, by 2010, the European Commission must develop its own methodology to measure GHG emissions associated with indirect land use changes related to biofuels production. Companies importing fuels to the E.U. that wish to qualify for theses mandates will also need

to ensure compliance with the new requirements.

For more information about EPA's Renewable Fuel Standard Program or the EU's new fuels mandates, please contact David M. ("Max") Williamson at (202) 289-6084, dwilliamson@bdlaw.com, or Alan J. Sachs at (410) 230-1345, asachs@bdlaw.com.

A. EPA Fails to Promulgate Required RFS2 Changes in 2008

EPA is required by the 2007 EISA to establish mandatory levels of biofuels (such as ethanol) and biodiesel in the U.S. fuel supply as part of an overall national policy to promote renewable fuel sources as well as reductions in GHG emissions and energy independence (see Beveridge & Diamond, P.C. "Renewable Fuel Program Standard Update," available online at: http://www.bdlaw.com/news-news-270.html). The 2007 energy act substantially increased the volume of biofuels in the U.S. fuel supply over those levels required by the earlier 2005 Energy Policy Act, and also imposed a new greenhouse gas content requirement in response to allegations that some biofuels were less environmentally friendly than traditional fossil fuels.[1] EPA was required to finalize new regulations by December 19, 2008, but has not to date issued even a proposed rule. EPA announced in November that, given the delay, obligated parties will continue to be subject (with a few exceptions) to EPA's existing RFS regulations for the 2009 compliance period (see Beveridge & Diamond, P.C. "Renewable Fuel Program Standard Update: EPA Announces 2009 RFS Targets," available online at: http://www.bdlaw.com/news-news-414.html).

A primary cause for the regulatory delay is the Agency's struggle with the required GHG lifecycle analysis. The EISA requires renewable fuel from new facilities commencing construction after December 19, 2007 to achieve at least a 20 percent reduction in lifecycle GHG emissions compared to baseline (2005) lifecycle GHG emissions. Fuels that do not meet this target will not qualify as "renewable fuels" and cannot be sold into the renewable fuels trading market.[2] EISA defines the term "lifecycle greenhouse gas emissions" to mean EPA's determination of the "aggregate quantity of greenhouse gas emissions" – including both direct emissions and significant indirect emissions such as emissions from land use changes – related to "the full fuel lifecycle." Lifecycle GHG emissions expressly include all stages of fuel and feedstock production and distribution, from feedstock generation or extraction, through the distribution and delivery and use of the finished fuel by the ultimate consumer, where the mass values for all GHGs are adjusted to account for their relative global warming potential.

Industry representatives have reported that although EPA developed an analysis with estimates of lifecycle emissions, the White House Office of Management and Budget (OMB) and the U.S. Departments of Energy (DOE) and Agriculture (USDA) have voiced objections to the Agency's methodology. Concurrently, environmental groups have been pressing EPA to analyze indirect land-use changes that may result from an increase in biofuels production, particularly from land use changes abroad, such as clearing of Amazonian rainforest for feedstock production. Meanwhile, the biofuels industry is urging the Agency to proceed more cautiously, arguing that scientific evidence is not developed enough to draw conclusions or support analysis of indirect land-use changes at this time. Industry may also wish to re-evaluate the lifecycle emissions from traditional fossil fuels that provide the baseline for the GHG reductions required by EISA.

Should EPA fail to propose its RFS2 regulations before the close of the Bush Administration on January 20, it may take several additional months before the incoming Obama Administration is able to work through the issues implicated by the RFS mandate. Moreover, USDA recently established an Office of Ecosystem Services and Markets as required under the May 2008 Farm Bill, and the Obama Administration may instruct EPA and USDA to work together more closely on development of the RFS2 regulations.

B. EU Adopts Directive Requiring GHG Lifecycle Reduction for Biofuels and Fossil Fuels

Meanwhile, the EU Parliament approved on December 17 a new Renewable Energy Directive requiring that renewable energy make up at least 20 percent of the EU's total energy consumption by 2020. Each Member State must meet a renewable energy minimum

target, which varies by Member State. By contrast, with respect to transportation fuels for all forms of transport, the new Directive also requires each Member State to meet 10 percent of its transportation fuel needs for all forms of transport through biofuels, renewable electricity or hydrogen.

The EU Parliament declined to mandate a proposed renewable fuels interim target of 5 percent by 2015 or a proposed stipulation that at least 40 percent of renewable fuels come from "second-generation" biofuels (*i.e.*, fuels developed from waste, residues, or non-food cellulosic and ligno-cellulosic biomass), or electricity or hydrogen. However, the Directive does provide that second-generation biofuels will be double-credited for quota purposes, and renewable electricity consumed by electric cars will be counted at 2.5 times its input.

The new biofuels mandate will replace existing voluntary renewable fuel targets established in 2003 and implemented by individual Member States through a variety of policies. In 2005, biofuels accounted for only 1 percent of all transportation fuels consumed in the EU.

1. GHG Emissions Requirements for Biofuels

The new Directive requires that biofuels achieve at least a 35 percent lifecycle GHG emission reduction compared to fossil fuels in order to be taken into account for purposes of measuring compliance with the Directive's mandates or to be eligible for financial support for the consumption of biofuels. From 2017 onwards, the lifecycle GHG emissions of qualifying biofuels produced in existing production plants must be at least 50 percent lower than fossil fuels, while biofuels produced in new installations must achieve a lifecycle GHG reduction of at least 60 percent. The Directive includes methodologies for calculating GHG impacts of biofuels without currently taking into account any net carbon emissions from land use changes, while requiring that the EU develop a methodology by 2010 to measure the GHG emissions from indirect land use changes traceable to biofuel production.

The Directive also states that biofuels made from crops grown in an area with "recognised high biodiversity value" (*i.e.*, forest undisturbed by significant human activity, areas designated for nature protection purposes, or highly biodiverse grassland), or an area that was peatland in January 2008, should not count towards the transport target. The European Commission is also required to monitor the social impact of the EU's biofuel policy and if necessary propose corrective action, especially if increased biofuels production leads to rising food prices or does not comport with social sustainability criteria.

2. GHG Emissions Requirements for Fossil Fuels

In addition, the EU adopted amendments to the Fuel Quality Directive to require that all transport fuels for use by road vehicles and non-road mobile machinery -- including fossil fuels -- achieve a lifecycle GHG emissions reduction requirement of 6 percent below 2010 levels by 2020, including emissions attributable to a fuel's induced land-use changes, transport and distribution, extraction, processing and combustion. The Directive imposes a mandatory 6 percent reduction on fuel suppliers, with recommended intermediate targets of 2 percent by 2014 and 4 percent by 2017. It also provides for a review of that mandate in 2012, aimed at the possible expansion of the lifecycle GHG reductions to 10 percent below 2010 levels, with additional potential reductions contemplated through the use of electric vehicles or GHG-saving technologies such as carbon capture and storage, and through credits purchased under the Clean Development Mechanism. EU fuel suppliers, as well as foreign suppliers importing fuels into the EU, will need to ensure compliance with these GHG emissions reduction requirements, which Member States must begin implementing "as gradually as possible."

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[1] In 2009, the RFS is intended to result in the use of 11.1 billion gallons of renewable fuel. The RFS is designed to escalate each year until culminating in a total requirement of 36 billion gallons of renewable fuel by 2022.

[2] EISA establishes specific quotas and GHG reduction mandates for various other subcategories of renewable fuels, including:

- "Conventional biofuel," which means renewable fuel that is ethanol derived from corn starch is subject to the 20% lifecycle GHG emission reduction;
- "Advanced biofuel" which means a renewable fuel, other than ethanol derived from corn starch, that has lifecycle GHG emissions that are at least 50% less than baseline lifecycle GHG emissions;
- "Biomass-based diesel," which means renewable fuel that is biodiesel that has lifecycle GHG emissions that are at least 50% less than baseline lifecycle GHG emissions; and
- "Cellulosic biofuel," which means renewable fuel derived from any cellulose, hemicellulose or lignin that is derived from renewable biomass that has lifecycle GHG emissions that are at least 60% less than the baseline lifecycle GHG emissions.

Firm News & Events

B&D: Proud Sponsor of Two Inaugural Balls

Beveridge & Diamond, P.C. served as an official sponsor of the National Bar Association Inaugural Ball, held at the J.W. Marriott Hotel on Sunday, January 18 and the Green Inaugural Ball, which took place at the National Portrait Gallery on Monday evening, January 19th.

The firm was happy to invite clients to share in the festivities surrounding the inauguration of President Barack Obama. The Green Inaugural Ball was an opportunity for members of the firm and clients to meet with the incoming EPA Administrator and officials from past and present Administrations with environmental responsibilities, as well as with members of the environmental community.

The blog link below features Beveridge & Diamond Managing Principal, Ben Wilson, at the NBA Inaugural addressing the attendees and reminding them that "Come Wednesday, we have a lot of work to do to enact change in this country,"

http://legaltimes.typepad.com/blt/2009/01/national-bar-association-ball-heavy-on-the-excitement.html

B&D Elects New Principals

Beveridge & Diamond, P.C. is pleased to announce that **Katherine T. Gates**, Washington, D.C. office, and **K. Russell LaMotte**, Washington, D.C. office, have been elected as Principals and Shareholders of the Firm.

Katherine Gates' practice is devoted primarily to federal and state trial and appellate litigation in the environmental and toxic tort areas. She litigates matters under the Comprehensive Environmental Response, Compensation and Liability Act, similar state statutes and common law tort claims regarding alleged hazardous substance contamination at facilities and sites.

Russ LaMotte advises and represents clients in matters relating to international environmental and oceans-related regulatory regimes. He serves as co-chair of the firm's Climate Change practice group, advising clients on both the emerging U.S. climate change regimes and the evolving international climate change framework. Before joining Beveridge & Diamond, he was an international lawyer at the U.S. Department of State, where he served as Deputy Assistant Legal Adviser designing, negotiating or implementing major environmental and oceans agreements and initiatives.

Previous Issues of Texas Environmental Update

To view all previous issues of the Texas Environmental Update, please go to http://www.bdlaw.com/publications-93.html.

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