EDWARDS ANGELL PALMER & DODGE

Guidance Note

The impact of climate change

Effective 1 January 2008 Kendall Freeman merged with Edwards Angell Palmer & Dodge LLP

Contents

Introduction

After much debate, plenty of inconvenient truths and perhaps as many convenient untruths, there finally seems to be a general consensus that climate change exists and that humans are contributing to it, probably causing its acceleration. In the last 12 months, from the Stern Review in the UK to the UN's Intergovernmental Panel on Climate Change (IPCC), there has been a significant shift towards governmental acceptance of the existence of climate change and of the potential consequences it brings with it.

The immediate effects of climate change are already well known and it is widely accepted that the earth has already started to experience some of these effects, such as the melting of glaciers and ice caps, the associated rise in water levels, and the greater frequency of extreme weather. However, less is known about the impact of climate change on businesses, from the burden of increased regulation to the financial threat of bad publicity and litigation.

At a time when environmental issues are climbing both the political agenda and the courts' daily Cause List, this Guidance Note will review some of the most recent worldwide developments and consider the potential legal issues, and the potential consequences, that may arise for almost every business.

Reviews and Regulations

The UN's Intergovernmental Panel on Climate Change

The recent assessment report from the IPCC[1] (its fourth since 1990), which was a culmination of three years' work reviewing of hundreds of studies, directly linked climate change to human activity which it said was '*very likely*' to have been the main cause of global warming since the 1950s.

The report outlined the following consequences of global warming:

1. a rise in sea levels of between 8 and 31 inches this century, as opposed to between 6 and 9 inches in the past century
2. the likely warming of the global climate of between 3.6 and 6.3 degrees Celsius in the next 100 years
3. the Arctic Sea to lose its year-round ice cover by the end of the century
4. a continued upward trend towards hot extremes and heat waves.

Particular significance has been given to this report because it was signed by 130 countries and, as a result of having to achieve consensus, is a conservative estimate of what might happen. Achim Steiner, Executive Director of the United Nations Environment Programme which established the IPCC, emphasised that: "*the implications of global warming over the coming decades for our industrial economy, water supplies, agriculture,*

1 IPCC Forum Assessment Report "Climate Change 2007: The Physical Science Basis." The Panel said they were 90% confident of this, as opposed to being between 66% and 90% confident in 2002. The IPCC reported in 1990 that "*the unequivocal detection of the enhanced greenhouse effect from observations is not likely for a decade or more*"', and indeed the current report states that the existence of climate change is now '*unequivocal*'.

biological diversity and even geopolitics are massive. Momentum for action is building; this new report should spur policymakers to get off the fence and put strong and effective policies in place to tackle greenhouse gas emissions"[2] and it was perhaps with this in mind that the Stern Review was commissioned.

The Stern Review Report on the Economics of Climate Change

The Stern Review, commissioned by the UK Government, concluded that the benefits of strong, early, coordinated action against climate change far outweigh the economic costs of doing nothing. It estimated that the cost of *not* taking action could be equivalent to losing between 5% and 20% of annual global GDP, whereas the costs of taking action now could be limited to around 1% of annual global GDP, if the world pursues the optimum policies.

The report said that global temperatures had already risen by half a degree because of climate change and that taking no action would most likely lead to a further rise of 2 to 3 degrees over the next 50 years. The estimated economic impact of such increases was a 10% reduction in global economic output.

However, the report was not generally pessimistic, suggesting that a reduction in demand for heavy polluting goods, greater efficiency, and a growth in the production and use of cleaner energy could help to stabilise climate change. Not all of the suggested methods for tackling climate change were entirely convincing, such as the rather vague ideas of promoting sustainable forestry in South America and creating a fund to help poorer countries invest in green technology, which seem like wishful

2 United Nations Environment Programme – Press Release, 2 February 2007.

thoughts never likely to struggle beyond bureaucratic tangles. However, there were many more practical suggestions. On a global basis, Stern proposed the creation of a global market for carbon pricing and the extension of the European Union Emission Trading Scheme (EU ETS) to the US, India and China, with specific targets for the scheme to reduce carbon emissions by 30% by 2020 and by 60% by 2050. Focussing on the UK, Stern urged the Government to make carbon reduction targets statutory and to create a new independent body to monitor the Government's progress in meeting these targets.

The European Union Emission Trading Scheme

The EU ETS was introduced across Europe to help fulfill its Kyoto Protocol commitments to reduce carbon dioxide emissions[3]. It chose to do so in a market friendly way, using a 'cap and trade' basis, which puts a price system in place that essentially allows companies to regulate themselves but provides a cost incentive to reduce emissions. Phase 1 of the EU ETS began in January 2005 and will run until the end of 2007, and Phase 2 will run from 2008 to 2012.

The 'cap' requires Member State governments to set emission limits for all installations in their country covered by the scheme, these include power stations, refineries, iron and steel and most of the energy intensive industries, overall covering about 40% of the EU's total carbon dioxide emissions. Each installation is then allocated allowances determining how much carbon dioxide they can emit for the particular phase in question, as set by the National Allocation Plan.

The 'trade' part of the scheme allows companies that exceed their

3 The EU ETS was established by Directive 2003/87/EC.

allowances to buy unused allowances ('permits') from companies which have cut their emissions, but those without permits are fined €40 per excess tonne of carbon dioxide. The problem with Phase 1 of the scheme was that Member States, under heavy lobbying from industry, issued more permits than required which resulted in carbon prices falling as low as €8 per tonne, and thus it has been cheaper to buy spare permits than pay the €40 fine or take steps to reduce emissions.

EU Environment Commissioner Stavros Dimas has pledged to reduce the number of permits granted in Phase 2 saying that the EU has to prove to other more sceptical nations that carbon trading schemes can work. However, negotiations are currently taking place and it remains to be seen whether lessons have been learned from the first phase or whether the Member States will once again bow to the demands of industry.

The EU ETS is soon being extended to aviation because, although the sector accounts for only 3% of the EU's Greenhouse Gases (GHGs), its emissions have increased by 87% since 1990, faster than any other sector and largely due to the advent of cheap air travel. Under the proposals, the EU ETS will cover commercial flights within the EU from 2011, and all flights to and from the EU from 2012.[4] The Commission says it expects any increase in ticket costs to be limited.

The effectiveness of the EU ETS, even in an extended form, will be difficult to judge in the short term, but many critics have suggested that without a global scheme international companies will only move emissions to countries without emission restrictions. However, as shown below, cap and trade schemes are the most popular method for curbing GHG emissions, both with legislators and the business community.

4 Domestic flights are already subject to national limits set by the Kyoto Protocol.

Road Transport

Road transport was not included within the scope of the EU ETS because the scheme is based on direct emissions and it was considered far too costly to administer for individual drivers. It may well be extended in the future, potentially through car manufacturers[5].

However, because road transport is the second largest GHG emitting sector in the EU, the European Commission's recent communications on fuel efficiency for cars confirmed their intention to introduce mandatory targets[6]. In June 2006 the European Council unanimously stated that "*in line with the EU strategy on carbon dioxide emissions... the average new car fleet should achieve emissions of 140g/km (2008/09) and 120g/km (2012)*", and the European Parliament has called for this to be reduced further to 80-100g/km through emissions trading between car manufacturers[7]. The Commission has also proposed the increased use of bio-fuels as another approach to reduce carbon dioxide emissions from road vehicles and it has said it will propose a legislative framework to carry out the initiatives by mid 2008.

5 Changes to the EU ETS, other than inclusion of aviation, can only take effect from 2013. This ensures stability for those already involved in the market, as well as sufficient time for the legislative adjustments.

6 Communication from the Commission to the Council and the European Parliament: Results of the Review of the Community Strategy to Reduce Carbon Dioxide Emissions from Passenger Cars and Light Commercial Vehicles - Brussels, 7 February 2002 COM(2007) 19 final.

7 The average in 2005 was 162g/CO_2/Km.

The Environmental Liability Directive

The Environmental Liability Directive (ELD)[8], which Member States were required to transpose into their national law by April 2007[9], is aimed at preventing future environmental damage and remedying any damage already caused. It covers water damage[10], land damage[11] and damage to the biodiversity from specifically regulated activities[12].

The ELD is not retroactive but, when implemented, will be in force as if from April 2007. It does not provide an action for economic loss, personal injury or property damage, and is instead based on the 'polluter pays' principle which provides that a polluter must remedy any damage they have already caused and/or prevent any potential damage they might cause in the future.

However, only certain activities attract strict liability (such as waste management, the disposal of substances into water supplies, and the manufacture and transportation of certain dangerous pollutants). Liability is fault-based for damage caused by any other activity, including fishing, farming and land development. This limited application of strict liability, together with the wide exemption for damages caused by acts of armed

8 Directive 2004/35/CE.

9 Only Latvia, Italy and Lithuania have done so.

10 Defined as any damage that significantly adversely affects the status or ecological potential of a water body as defined under the Water Framework Directive (Directive 2000/60/EC).

11 Defined as land contamination that creates a significant risk of human health being adversely affected as a result of introduction in, on or under land of substances, preparations, organisms or micro-organisms.

12 This includes protected species and natural habitats listed in the Birds and Habitats Directives, and other species and habitats added at the discretion of Member States.

conflict, natural phenomena, acts that were authorised at the time they occurred, or by emissions which at the time were not considered to be harmful[13], indicate that enforcement of the spirit of the ELD could prove difficult.

Local authorities or the Environmental Agency (EA) will be responsible for enforcing the ELD. NGOs and individuals who are directly affected by polluters can request that a local authority or the EA take action, and they can seek judicial review of any action already taken. There is also a 'fail all' provision which holds a Member State responsible for remedying any damage for which the polluter cannot be held liable.

13 "*According to the best available scientific and technical knowledge*".

UK Legislation

The UK Government has passed both direct and indirect legislation which tackles global warming. The signing of the Kyoto Protocol was the most direct of these, and it binds the UK to reduce six GHG emissions, by 12.5% to below 1990 levels, by 2012. The Government's plan to meet this commitment, and to go beyond it, were outlined in the recent Climate Change Bill and the Energy White Paper. The White Paper sets out a long term plan of action to address these challenges at home and abroad, whereas the Climate Change Bill sets out a specific framework and identifies new legal requirements that are aimed at meeting the Government's objectives.

The draft Climate Change Bill published in March 2007 sets out a framework for transforming the UK to a low-carbon economy. The key points of the draft bill are:

1. clear and legally binding targets for reducing carbon dioxide emissions, including a 60% reduction by 2050 and a 26% to 32% reduction by 2020

2. a system of “carbon budgets” covering a five year period. This will be set at least 15 years ahead, to provide some certainty to the businesses and individuals that need to invest in low-carbon technologies

3. the creation of the Committee on Climate Change, to provide independent expert advice to the Government on meeting its targets and staying within its carbon budgets, and to produce an annual progress report to Parliament, to which the Government must respond

4. the Government to report at least every five years on the current and predicted impacts of climate change and must produce proposals for adapting their policy as a result.

In May 2007 the Government published the Energy White Paper which outlines the Government's international and domestic energy strategy. The four key goals in the report were:

1. to cut carbon dioxide emissions by 60% by 2050, with real progress by 2020
2. to maintain the reliability of energy supplies
3. to promote competitive markets in the UK and beyond
4. to ensure that every home is adequately and affordably heated.

The White Paper introduces a mandatory emissions cap and trade scheme, called the Carbon Reduction Commitment (CRC), which it predicts can make significant savings for 'non-energy intensive' organisations such as hotel chains, supermarkets, banks, central government and the larger local governments. Enforcement of such requirements will be monitored through smart meters and an Energy Performance Certificate with energy ratings, which all business premises will be required to have when built, sold or rented out. There are also proposals to ensure that from 2016 all new homes are carbon neutral, and to ban inefficient light bulbs.

In addition to the CRC will be the Carbon Emission Reduction Target (CERT) which is aimed at forcing energy suppliers to reduce their carbon emissions by doubling the previous targets set by the Energy Efficiency Commitment, which required that electricity and gas suppliers with more than 15,000 domestic customers achieve certain energy savings by assisting their customers to take energy-efficiency measures in their homes; of particular importance was that suppliers had to achieve at least half of their energy savings in households on income-related benefits and tax credits.

The White Paper also urges the EU to include not only aviation but also surface transport in the EU ETS. It expresses hope that a more effective EU

ETS, with a realistic carbon price, will ensure companies investing in new power stations take account of the cost of carbon, and thus, as originally intended, the EU ETS would provide an incentive for investment in low carbon energy generation. Indeed the White Paper stresses that "*companies will need to make substantial new investments over the next 20 years as many coal and nuclear power stations close*".

One of the controversies touched upon in the White Paper is the much debated (and litigated) nuclear question[14]. It points out that nuclear power provides only about a fifth of the UK's energy, whereas gas and coal provide about one third each, with renewable sources providing a relatively paltry 4%. The Government says that a new consultation will be launched considering whether new nuclear power stations should be an option for reducing GHG emissions, pointing out that without the current nuclear plants the UK's emissions would already be 5% to 12% higher. However, with most current plants due to close in the next 15 years, the Paper points out that the UK will struggle to meet its targets and it adds that the failure to build new nuclear plants would endanger the security of energy supply by cutting down on the number of options available.

With regards to legislation that will tackle global warming, one of the most important examples is the Companies Act 2006. The Act came into force on 1 October 2007, and it provides at least one significant change to corporate governance by requiring that in his duty to promote the success of the

14 In January this year Greenpeace succeeded in delaying the Government's nuclear plans by challenging the consultation process which Mr Justice Sullivan decided had been "*misleading*", "*seriously flawed*" and "*procedurally unfair*" because it had contained no actual proposals and the only information given to those consulted was described by the Judge as "*wholly insufficient for them to make an intelligent response*". In particular the information given on nuclear waste, probably the issue of greatest concern, was said to be "*not merely inadequate but also misleading*". The result was that the Judge granted what he called a "*quashing order*" which stalled the Government's plans for the new nuclear power stations and forced the consultation process to begin again.

company, a director must have regard to a number of factors, including: "*the impact of the company's operations on the community and the environment*"[15]. As such, failure to reduce GHG emissions could be sufficient ground on which to base an action for breach of duty.

Moreover, at section 417, the Act provides that the directors of quoted companies must provide a business review which specifically includes the same environmental disclosure if considered relevant to the "trends and factors likely to affect the future development, performance and position of the company's business". This might indicate that provided directors can show they have considered the relevant factors (eg haulage companies considering environmentally friendly fuels), it is unlikely they will be in breach of the new duty, even if they do not ultimately decide to take the most environmentally friendly approach. However, very serious consideration should be given where a company refuses to take an approach which would reduce emissions.

The significance of these provisions was outlined by Alistair Darling, then the Secretary of State for Trade and Industry, who pointed out that the Act was evidence of a shift in thinking: "*the Bill …enshrines in statute what the law review called "enlightened shareholder value". It recognises that directors will be more likely to achieve long term sustainable success for the benefit of their shareholders if their companies pay attention to a wider range of matters… to promote the success of the company in the collective best interest of the shareholders, but in doing so they will have to have regard to a wider range of factors, including the interests of employees and the environment*"[16]. This certainly seems to sum up part of the reason that climate change has now become such a focal point for governments because it is essentially a movement driven by the general public, and this pressure, together with litigation initiated by public interest groups, has prompted the current wave of regulation.

15 Companies Act 2006, (Section 172(1)(d))

16 Alistair Darling, Commons Second Reading, 6 June 2006.

US Legislation

US State Regulation

The US has been much maligned for its apparently slow recognition of climate change although it should be noted that, in the absence of federal legislation, the states themselves have begun to grasp the nettle. California is leading the way with the recent enactment of the Global Warming Solutions Act 2006, which requires the California Air Resources Board (CARB) to implement a state-wide annual cap on GHG emissions from certain sectors. It is anticipated that this will reduce emissions by 25% to 30%, to 1990 levels. The scheme begins in 2012 and the cap will be incrementally reduced to reach the target by 2020.

It is the CARB's responsibility to develop a plan by 2009 to meet the target, using "*direct emission reduction measures, alternative compliance mechanisms, market mechanisms, and potential monetary and non-monetary incentives*". By 2011 the CARB must have analysed the appropriate sectors and the appropriate caps, and must have adopted a framework for implementation. The California Public Utilities Commission (CPUC), which must be consulted by CARB, has indicated that the requirements will be imposed on the load-serving entities which deliver power to end users, rather than generators, thus addressing the significant imports of coal-based energy into California. CPUC is also encouraging a cap and trade system.

The Regional Greenhouse Gas Initiative (RGGI) is an agreement by nine Northeastern and Mid-Atlantic states aimed at developing multi-state carbon dioxide regulation in the electric power sector (eventually it intends to include other GHGs). Under the RGGI a non-binding 'model rule' was published in August 2006 which proposed a cap and trade system, similar

to Phase 1 of the EU model, in which states would individually place annual per tonne limits on total state-wide emissions from power plants. The initial budget would be similar to current emissions and states would be given the discretion to decide how and to whom their allowances were allocated, except that 25% of their allowances would have to be dedicated to '*consumer benefit or strategic energy*' purposes. Various 'offsets',[17] and safety valves,[18] have been included to try to maintain a stable market. The Governors of participating states have agreed to propose similar rules to their state legislatures before the end of 2008, with the system scheduled to begin in 2009.

US Federal Regulation

At a federal level the fall of Congress into democratic hands in November 2006 has seen a dramatic flurry of climate change bills[19]. The following five bills were introduced before the end of February 2007, all based on the principle of cap and trade:

1. In January 2007, Senators Obama, McCain and Lieberman re-introduced the Climate Stewardship Act, a bill that would introduce a cap and trade system for GHG emissions from power plants, industry and oil refineries. Sectors not covered would be able to register any reductions they made and sell them to industries which were involved in the scheme. Credit would also be given for early action and past reductions. The goal would be to reduce GHG emissions to 2004 levels by 2012 and to 1990 levels by 2020.

17 The limit for offsets can be extended to 5% of an emission source's total emissions if the price of allowances surpasses $7, increasing to 10% if allowances go beyond $10.

18 Allowances for taking actions that reduce carbon dioxide loading in a way that is '*real, additional, verifiable, enforceable, and permanent*'.

19 The previous Senate chairman of the Environment Committee was James Inhofe, who described climate change as: "*the greatest hoax ever perpetrated on the American people*".

2. Also in January 2007, the Feinstein-Carper Bill, endorsed by PG&E, Calpine, Entergy, Exelon, FPL, and PSEG, proposed a reduction in electricity emissions to 25% below what they are expected to be by 2020. This sets the cap at 2006 levels in 2011, 2001 levels by 2015 and would then reduce the cap by 1% each year from 2016 to 2020. The Environmental Protection Agency (EPA) would then have the discretion to introduce increased reductions from 2020. Allowances would be auctioned in the same way as other cap and trade schemes.

3. The most stringent of the bills proposed was the Global Warming Pollution Reduction Act of 2007, which requires the reduction of GHG emissions to 1990 levels by 2020, and then reducing them incrementally to 80%, to below 1990 levels, by 2050.

4. In December 2006, Senators Harry Reid and Barbara Boxer, the new Chairwoman of the Senate Environmental Committee, introduced the National Energy and Environment Security Act of 2007 which requires GHG emission stabilization at 2013 levels by 2020, increased biofuel production, a commitment to energy efficiency measures and the promotion of alternative forms of energy, such as wind and solar. It also proposed rolling back incentives that sponsor the oil industry.

5. In February, Senators Kerry and Snowe reintroduced the Global Warming Reduction Act intended to cut GHGs by 60% below 1990 levels by 2050, starting at 1.5% for the first decade. The bill covers the entire economy and includes a national renewable energy standard of 20%.

As in the UK, there is also indirect legislation in the US, similar to the Companies Act requirements in the UK. The Securities and Exchange Commission (SEC) specifically requires public companies to consider environmental issues, imposing a duty on companies to disclose the material effects that compliance with environmental regulations will have on a company's finances. It also requires that consideration must be given for

any estimated expenditure in the future as a result of such legislation[20]. This undoubtedly places companies in a difficult position, forcing them to predict what regulations may be imposed upon them.

Another provision at Item 303(a)(i) of the Securities Act, imposes an obligation to "*Identify any known trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way*."[21] This is another vague obligation on US businesses, which will inevitably be looking for clarification.

20 Standard Instructions for filing forms under the Securities Act of 1933, Securities Exchange Act of 1934 and Energy Policy and Conservation Act of 1975—Regulation S-K §229.101 (Item 101)[(c)(l)] - Description of business (xii) "*Appropriate disclosure also shall be made as to the material effects that compliance with Federal, State and local provisions which have been enacted or adopted regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, may have upon the capital expenditures, earnings and competitive position of the registrant and its subsidiaries. The registrant shall disclose any material estimated capital expenditures for environmental control facilities for the remainder of its current fiscal year and its succeeding fiscal year and for such further periods as the registrant may deem material*."

21 Securities Act 1933, (Item 303(a)(l), liquidity 229.303).

US Litigation

What is evident over the past 12 months is the increasing propensity of the courts to apportion blame, much as they have done in the Big Tobacco litigation in the US, and in asbestos litigation, by bending the rules of causation. The success of such litigation may threaten to burst the flood gates because the blame for global warming can potentially be laid at the door of every energy using company. The US Courts have seen the majority of important cases so far, probably because the current US administration is perceived as having failed to consider the climate change problem.

One of the most recent cases in the US, and certainly one of the most significant, was *Massachusetts et al v Environmental Protection Agency et al* (EPA)[22]. The action was brought after the EPA rejected a petition by public interest groups and a dozen states to regulate automobile emissions, on the grounds that it lacked sufficient statutory authority to do so and that, in any case, the causal link between such emissions and global warming was not strong enough to warrant restrictive regulation[23].

The legal issue before the court was whether automobile GHGs fell within the Clean Air Act's (CAA) definition of an 'air pollutant', thus placing a duty on the EPA to regulate them[24]. The preliminary question determined by the court was whether the claimants had sufficient standing to bring the action,

22 Case Number 03-1361.

23 Interestingly, the EPA also said that the regulation of automobiles might conflict with the President's overarching approach to tackling climate change. The claimants said this was a policy consideration not within s202(a)(i) of the Clean Air Act Amendments of 1990.

24 Section 202(a)(1) of the Clean Air Act, 42 U.S.C. § 7521(a)(1), requires the administrator of the Environmental Protection Agency to set emission standards for "*any air pollutant*" from motor vehicles or motor vehicle engines "*which in his judgment cause, or contribute to, air pollution which may reasonably be anticipated to endanger public health or welfare.*"

in other words, whether they could satisfy the constitutional requirement of having a '*concrete and particularized injury*' that is '*fairly traceable to the defendant*'. In addressing this question the court made a significant and potentially groundbreaking statement when it noted that "*the harms associated with climate change are serious and well recognized*[25]". The court then held that the damage associated with climate change, such as flooding and coastal erosion, constituted an injury capable of supporting standing to bring a claim. However, the court did limit this standing to Massachusetts, which it said was entitled to protect its constituents, acting in its 'quasi-sovereign' capacity.

With regard to the substance of the decision, the Court said that the EPA had evaded the "*clear statutory command*" of the CAA by failing to determine if GHG emissions were 'pollutants' under the Act. The Court said that such pollutants fell well within the CAA's definition and said that the only way the EPA could refuse to regulate such emissions would be if it determined that there was insufficient scientific consensus on whether GHGs contributed to global warming. However, the court said it would be "dubious" of any such decision by the EPA, and noted that "*the risk of catastrophic harm, though remote, is nevertheless real*".

The Court also made a significant statement when it rejected the EPA's argument that a reduction in US emissions was pointless because increased emissions from other countries would easily absorb those reductions. The court said that "*a reduction in domestic emissions would slow the pace of global emissions increases, no matter what happens elsewhere*".

It is difficult to predict with absolute confidence what the effect of the ruling will be, but the potential effects are wide ranging. In the immediate future, similar actions which had been stayed pending the decision are now more

25 Justice Stevens, giving the majority judgment.

likely to be decided in favour of the environmentalists. These include an action brought by Coke Oven Environmental Task Force and 10 Northeastern states, challenging an EPA decision to refuse to regulate carbon dioxide emissions, on this occasion from power plants[26]; and also a challenge by the automobile industry to a Californian law limiting carbon dioxide emissions from new motor vehicles[27].

The Supreme Court may well have triggered a change in the US approach from voluntary reductions to mandatory caps, either through the CAA or through one of the bills being considered by congress. As indicated above, industry itself may well prefer federal legislation rather than an inconsistent patchwork of individual state legislation, an ironic consequence of which could be that far reaching state legislation is undermined by more moderate federal legislation[28].

The decision could also prompt a shift from the majority of cases being brought by public interest groups aimed at injunctive relief or judicial review, to cases brought by injured parties seeking damages, or government authorities seeking to plug budget shortfalls. There is already evidence of such cases in California, where a claim was issued in September 2006 against six of the world's largest automobile manufacturers and which alleges that the GHG emissions from their automobiles create a public nuisance[29]. California is not seeking to force the companies to cut their emissions but instead it wants compensation both for the current costs and for the potential future expenditure that may

26 *Coke Oven Environmental Task Force, et al v EPA*, No. 06-1131 (D.C. Cir. Apr.7, 2006).
27 *Central Valley Chrysler-Jeep Inc. v Witherspoon*, No. CV-F-04-6663 (E.D. Cal. 2006).
28 Under Article IV of the US Constitution, the 'supremacy clause', federal law trumps state law if any conflict arises.
29 *California v. General Motors Corp.*, No. 3:06-CV-05755-MJJ (N.D. Cal. filed Sept. 20, 2006).

be incurred by the state as a result of global warming. Such claims echo the way 'Big Tobacco' was sued in order to cover the medical cost to state health systems caused by smoking.

However, perhaps the most radical claim currently being considered is one brought by the owners of property damaged by Hurricane Katrina seeking compensation from dozens of oil and coal companies, and chemical manufacturers, alleging that the companies' GHG emissions contributed to global warming and thus led to the greatly intensified weather conditions that allowed the hurricane to form[30].

30 *Comer v. Murphy Oil C.A*, No. 1:05-CV-436-LTS-RHN (S.D. Miss. 2006). After a motion to dismiss from the Defendants, the Plaintiffs have been given leave to amend their claim.

Significant Litigation in the Rest of the World

Courts all over the world are now considering the issues of climate change, from developing countries such as Nigeria and Argentina to the developed world, such as Canada and Australia.

In November 2005 the Federal High Court of Nigeria considered a class action by communities in the Niger Delta who were suing the Government and five multinational oil companies for the environmental damage caused by the flaring of gas over a period of 40 years. The Court ordered that gas flaring must stop in the Niger Delta because it violated guaranteed constitutional rights to life and dignity.

The spectre of climate change also appeared in Argentina in the wake of the 2003 Sante Fe floods, after which Article 6 of the UN Framework Convention on Climate Change[31] was used to force the Government to disclose that they had failed to act on necessary infrastructure changes that they were recommended to take in order to adapt to climate change. Similarly, in Canada, the Government's response to climate change is being challenged in the Federal Court by Friends of the Earth, who allege that the Government has failed to meet its international commitments under the Kyoto Protocol.

Australia has also seen a significant amount of litigation in the past few years. In 2004 an Australian tribunal delivered a decision that a panel considering an application to extend a coal field must consider the environmental impacts of the GHG emissions generated by the field[32].

31 Art. 6 UNFCCC requires countries to '*promote and facilitate… public access to information on climate change and its effects*'.

32 *Re Australian Conservation Foundation and Ors v Latrobe City Council and Minister for Planning* [2004] 140 LGERA 100.

Similarly in 2006 the Australian NSW Land and Environment Court delivered a decision ruling that the impacts on climate change had to be considered in an environmental assessment of a proposed coal mine[33]. This case is important not just because of its potential impact on any similar development in Australia that requires an environmental assessment but also because this was one of the first rulings where the court said that downstream emissions had to be considered. However, the floodgates were restrained as Justice Pain noted that in this case there was a sufficient proximate link between the mining and climate change because of the scale of the project and because the downstream sales were solely to power stations using the coal for fuel.

In contrast is the decision in *Re Xstrata Coal*[34]. The Queensland Conservation Council (QCC) challenged Xstrata Coal's plans to enlarge one of its mines in central Queensland. The QCC sought to have GHG emissions considered in the decision to grant the lease, and to force the company to avoid, reduce or offset the future carbon dioxide emissions that would result from the expanded site, over the next 15 years. On this occasion the Tribunal ruled that there was no causal link between the GHGs from the mine and the harm caused by global warming, and that in any case the volume of emissions was negligible. Although this decision seems to buck the recent trend, it should be noted that in making his decision the President of the Tribunal controversially questioned both the validity of the IPCC's findings and of the Stern Review.

On the whole, recent international court decisions show a significant trend in favour of the recognition of climate change and the surrounding repercussions as legitimate grounds on which to base litigation[35]. In fact, some judges have even cited 'intergenerational equity' as a factor in their decision, and there is no reason to believe there will not be an upward trend in similar claims.

33 *Gray v The Minister for Planning* [2006] NSWLEC 720.

34 *Re Xstrata Coal Queensland Pty. Ltd. & Others* [2007] QLRT 33.

35 The very existence of Environmental Courts, such as that in New Zealand, is evidence of the same.

Conclusions

Clearly with the increasing amount of existing and proposed legislation, all directors should begin to think very seriously about the impact of climate change on their businesses. The breadth of recent developments has meant that almost every business may be affected, from developers who will have to consider the carbon cost of any new projects (and perhaps the litigation costs of former projects), to directors who will have to consider their personal liability for any lack of disclosure under legislation such as the Companies Act or the Securities Act. Directors will also have to consider whether they will be able to insure themselves against that risk.

Inevitably there will be a battle at some point between the insurers and the insured because while most policies generally exclude claims related to pollution[36], it is unclear whether such exclusions include all issues relating to climate change, or whether such exclusions will simply be disapplied by the courts. Undoubtedly, decisions like *Massachusetts v EPA* will encourage further claims and the width of the pollution exclusions will begin to become clear if companies are forced to start paying damages. The question will then be when, and from whom, the insurers and reinsurers start to seek redress.

Class actions, such as the Hurricane Katrina case, will no doubt cause even greater consternation amongst businesses with high emissions but, while this may be a problem in the US, such cases are less likely in the EU because of the limited availability of contingency fee arrangements and the paucity of US-sized jury awarded damages. Such litigation is also less likely in the EU because of the public perception, unlike in the US, that

36 With the exception of some policies available in the Bermudan market.

governments are starting to tackle climate change, and also because of the existence of legislation which makes it more likely that enforcement actions will be brought against infringers by the state, or by environmental action groups challenging a state's decision not to act.

The possibility of class action lawyers entering the fray should also be a further prompt for federal regulation in the US to clarify the uncertainty of the Securities Act and to forestall further broad interpretation of older legislation and the development of a confusing patchwork of state regulation. Indeed, the power industry is increasingly calling for federal action or endorsing specific policies, particularly cap and trade. This is a result of their increasing legal obligations and their need to know and cover their risk, but also because there may be money to be made.

Indeed, the coming regulations will bring numerous business opportunities in developing technology, in energy efficient products, and in emissions trading, and companies are positioning themselves to take advantage of these opportunities, either by promoting certain legislation in order to shape policy in their favour or by strengthening their public image.

As such, whilst the recent developments on climate change indicate there will be a price to be paid, companies worldwide are aware that there will also be a buck to be made.

January 2008

This publication is for general guidance only and is not intended to be a substitute for specific legal advice. If you would like any further information please contact:

James Maton tel: +44 (0)20 7556 4547 *jmaton@eapdlaw.com*

EDWARDS ANGELL PALMER & DODGE UK LLP

One Fetter Lane, London EC4A 1JB United Kingdom
tel: +44 (0)20 7583 4055 fax: +44 (0)20 7353 7377

eapdlaw.com