

HOUSE OF REPRESENTATIVES PASSES CLIMATE CHANGE AND CLEAN ENERGY BILL; SENATE IS NEXT HURDLE

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To Our Clients and Friends:

On June 26, 2009, the United States House of Representatives narrowly passed a climate change and clean energy bill, H.R. 2454, known as the American Clean Energy and Security Act of 2009 (“ACES”). Introduced by Energy and Commerce Committee Chairman Henry Waxman (D-Calif.) and Chairman of the Subcommittee on Energy and Environment Edward Markey (D-Mass.), the approximately 1,500-page bill is the first piece of legislation approved by either body of Congress curbing greenhouse gas (“GHG”) emissions. The bill institutes a cap on GHG emissions and establishes a program to trade emissions allowances. The bill also supports the growth of clean energy technologies by, among other things, implementing a federal renewable energy credit system, encouraging energy efficiency and investing in “smart grid” technologies.

HIGHLIGHTS OF THE LEGISLATION

Cap-and-Trade

ACES establishes a nationwide cap-and-trade program covering approximately 85% of the nation’s GHG emissions. The cap generally applies to emitters of more than 25,000 tons of GHGs annually, though a number of businesses are covered regardless of their emissions. Covered entities must obtain emissions allowances for their GHG emissions. The bill aims to reduce GHG emissions to 17% below 2005 levels by 2020 and to 83% below 2005 levels by 2050. The emissions reduction requirement begins in 2012, when the bill mandates a 3% reduction from 2005 levels.

The following are highlights of the cap-and-trade portion of the bill:

Implementation in Phases. The cap-and-trade program is to be phased in over the next five years. Beginning in 2012, producers and importers of petroleum and coal-based liquid fuels will need to obtain emissions allowances for the carbon content of their fuels. Additionally, electric utilities will be required to obtain allowances for their GHG emissions. Industrial emitters of more than 25,000 tons of GHGs annually and other emitters of GHGs will be regulated under the cap-and-trade program beginning in 2014, while natural gas distributors will be regulated in 2016.

Offsets. Regulated entities can achieve compliance through the purchase of offsets. Offsets are GHG reductions achieved by a source that is not regulated under the federal cap-and-trade program. The bill allows for a large amount of offsets, the use of which would annually allow up to two billion tons of additional emissions.

USDA and EPA to Share Regulation of Offsets. The Department of Agriculture will be responsible for overseeing domestic offsets in the agriculture and forestry sectors. Landowners can generate offsets for activities that reduce GHG emissions or sequester carbon in the soil, such as sustainable forest management, reforestation, cover cropping agricultural lands or no till cultivation methods. Offsets in other sectors will be administered by the Environmental Protection Agency (“EPA”).

Trading, Banking and Borrowing Allowances. Companies will be able to trade and “bank” allowances for future use, and in certain circumstances, borrow against future allowances. These transactions would be regulated primarily by the Federal Energy Regulatory Commission (“FERC”) in conjunction with the Commodity Futures Trading Commission, which would regulate the market for allowance derivatives.

Protection for Energy-Intensive Industries. Beginning in 2020, the bill imposes a border adjustment charge on energy-intensive goods imported from countries that do not have comparable emissions regulations.

Reporting Requirements. The bill requires the EPA to draft regulations establishing a GHG registry. It mandates that all covered entities, as well as all entities emitting more than 10,000 tons of GHGs annually, submit data to the EPA on their GHG emissions and their production or importation of fuels that will lead to GHG emissions. The provision gives the EPA broad discretion to require any other entity to report on their GHG emissions if such reporting will further the purposes of the bill to reduce GHG emissions.

Emissions Allowances. Initially, 85% of emissions allowances are to be freely allocated to electric and natural gas utilities, home heating suppliers and energy-intensive industries and distributed to promote energy efficiency and renewable energy investments. The remaining 15% of allowances are to be auctioned. The above allocations will change as an annually increasing percentage of allowances will be auctioned instead of freely allocated, with 70% of allowances auctioned by 2031.

Removal of EPA Authority to Regulate CO₂ as an Air Pollutant. The bill contains a provision preventing the EPA from regulating carbon dioxide emitted from stationary sources except through the cap-and-trade program.

Clean Energy Provisions

The bill contains a number of provisions intended to accelerate the transition to renewable energy and a modern electricity grid, including the following:

Renewable Energy Credits. The bill initiates a federal renewable electricity standard and creates federal renewable energy credits (“Federal RECs”) for electricity generated by renewable resources. These Federal RECs can be sold, exchanged, traded or banked for up to three years. Starting in 2012, retail electric utilities will be required to obtain Federal RECs in amounts representing 6% of the electricity each supplies annually and increasing to 20% by 2020. In some circumstances, a portion of this requirement may be satisfied instead through measures intended to increase energy efficiency.

Smart Grid. The bill encourages expansion of the “smart grid,” which the bill broadly defines to include electricity infrastructure that may have digital information and controls for improving the reliability, efficiency and security of the grid, “smart” appliances and consumer devices that contain features enabling communication with the grid, advanced electricity storage and “peak-shaving” technologies, including plug-in electric and hybrid electric vehicles.

Electrical Load Management. The states, together with FERC, the North American Electric Reliability Corporation (“NERC”) and individual and regional load serving entities are required to work together to manage peak demand and lower overall demand through energy efficiency, distributed generation, demand response or “smart grid” technologies.

Siting Electric Transmission Lines. The bill mandates coordinated regional and national planning for transmission overseen by FERC. While the bill empowers FERC to override state roadblocks to transmission lines from renewable sources in western states, it stops well short of granting FERC siting authority for transmission lines. Rather, FERC is instructed to study whether federal siting authority is necessary, and to report back to Congress in three years.

Encouraging Energy Efficiency. The bill introduces and expands various energy efficiency programs for new and existing commercial buildings and residences, industrial equipment and lighting. Efficiency may also satisfy a portion of the Federal REC requirements.

Developing Carbon Capture and Sequestration. The bill supports a carbon capture and sequestration (“CCS”) demonstration program for coal-fired power plants. New coal-fired power plants permitted after 2020 must use CCS, and coal-fired plants permitted between 2009 and 2019 must use CCS by 2025. In addition, electricity generated by fossil fuel generating units that use CCS technology generally will not be subject to the Federal REC requirements.

Next Steps

The United States Senate now takes center stage as it begins to consider this bill. Senate Environment and Public Works Committee Chairwoman Barbara Boxer (D-Calif.) has pledged to have a climate bill, based on ACES, passed out of committee by the end of August. Additionally, Senate Majority Leader Harry Reid (D-Nev.) has set a September 18 deadline for the various Senate committees to produce their climate bill provisions. Full Senate consideration of the climate bill is expected to begin in the Fall. Given this timeline, the Senate may vote on a climate bill before the end of the year.

The Senate has already made progress regarding clean energy legislation. The Energy and Natural Resources Committee recently approved its own energy bill, the American Clean Energy Leadership Act, which among other provisions, requires electric utilities to obtain 15% of their electricity from renewable sources by 2021 (compared to the 20% by 2020 required by ACES) and would open additional offshore areas for oil and gas production.

Over the next few months, the debate concerning the merits of clean energy and climate change legislation, and resulting costs to U.S. businesses, will intensify. We will continue to monitor developments on climate change and clean energy legislation.

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