WEST VIRGINIA DIVISION OF ENERGY

MEMORANDUM

To: President Jeff Kessler, Chair
Speaker Tim Miley, Chair
Joint Committee on Government and Finance

cc: Jason Pizatella, Deputy Chief of Staff
Keith Burdette, Cabinet Secretary, West Virginia Department of Commerce
Joshua Jarrell, Deputy Secretary/General Counsel, West Virginia Department of Commerce

From: Jeff Herholdt, Director
West Virginia Division of Energy

Date: July 9, 2013

Re: Quarterly Report Ending June 30, 2013
Legal Challenges Potentially Impacting the Energy Industry

As mandated by West Virginia Code §5B-2F-2(s), the following information presents legal challenges with the potential to impact the state's energy industry. This submission has been summarized by the West Virginia Chamber of Commerce's Energy Committee. Reports are submitted on a quarterly basis.

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REPORT ON LITIGATION RELATED TO

ENERGY AND NATURAL RESOURCES IN WEST VIRGINIA

SECOND QUARTER 2013

1. D.C. Circuit Court Upholds EPA Veto of CWA §404 Permit After Permit-Issuance

On April 23, 2013, the United States Court of Appeal for the District of Columbia upheld EPA's authority to retroactively veto Section 404 permits. The ruling comes as a disappointment to those in the coal industry seeking the certainty and finality in the CWA §404 permit context.

The permit in question was related to Mingo Logan Coal Company's U.S. Army Corps of Engineers Permit for the Spruce No. 1 Surface Mine in Logan County, WV. The permit was originally issued in January of 2007. EPA waited until January 13, 2011 to exercise its "veto" power pursuant to Section 404(c) of the CWA, which provides EPA the authority to "prohibit the specification (including the withdrawal of specification)" of waters of the U.S. as a disposal site for fill material "whenever [it] determines...that the discharge...will have an unacceptable effect...." In exercising its "veto" power, EPA claimed valley fills associated with the mine will have adverse impacts water quality, which will in turn cause unacceptable impacts on aquatic life. However, all discharges of water from the fill area are regulated by an NPDES permit. That permit was issued by WVDEP after EPA withdrew objections to it years ago. The veto marked only the 13th time since 1972 that EPA had used its Clean Water Act veto authority, and the first time EPA had ever vetoed a previously permitted mine.

Mingo Logan sued EPA in the U.S. District Court for the District of Columbia, arguing that EPA's "veto" was improper. On March 23, 2012, Judge Jackson of the D.C. District Court overturned EPA's retroactive veto. The Court applied the two-step analysis articulated in *Chevron U.S.A. v. NRDC*, 467 U.S. 837 (1984). The *Chevron* two-step test applies where a court reviews an agency's interpretation of the statute it administers. First, the court must determine whether Congress has spoken directly to the precise question at issue. If the intent of Congress is clear and unambiguous, then the court must give effect to the unambiguously expressed intent of Congress, and the inquiry is over. The second step applies where the language of the statute is found to be silent or ambiguous with respect to the specific question. If the statute is silent or ambiguous, the Court then determines whether the agency's interpretation of the statute is a permissible construction of the statute.

EPA took the position that Section 404(c) authorized it to exercise its veto at any time—even after permit issuance. Although Judge Jackson found the language of 404(c) to be ambiguous in isolation, she found that the statutory text as a whole and the legislative history of the statute ran counter to EPA's claim that it could "withdraw specification" after permit issuance. Thus, Judge Jackson ruled that EPA's interpretation failed the first step of *Chevron*. The Court went on to determine that, even if there were ambiguity to the language, EPA's position also failed under step two of the *Chevron* analysis. Here, the Court's analysis was complicated by the fact that the

Clean Water Act provides authority to both the Corps and EPA, and in such a case there is an argument that EPA is owed no deference. However, the Judge ruled that, even according EPA some deference, EPA's interpretation of its authority to allow it to exercise its 404(c) authority after the Corps had issued a permit was unreasonable. The Court used a variety of strong language in discussing EPA's interpretation, characterizing it as illogical and impractical, along with stating that EPA had resorted to "magical" thinking.

Of note, the Court pointed to the various amici briefs filed expressing concern with eliminating finality from the permitting process as additional grounds for finding EPA's interpretation to be unreasonable. It thus relied on the primary argument made by industry—certainty of a permit is a foundation of the permitting process. The Court's opinion is also notable for its strong language in places, making such statements as: EPA's "reading does not exactly leap off the page" and "[t]his is a stunning power for an agency to arrogate to itself when there is absolutely no mention of it in the statute."

On appeal, the Circuit Court of Appeals reversed the District Court, focusing on the plain language of the statute. The Appeals Court focused on the Oxford Dictionary definitions of two key statutory terms, "whenever" ("at whatever time, no matter when") and "withdrawal" ("[t]o take back or away something that has been given, granted, allowed, possessed, enjoyed, or experienced"), in ruling that the CWA "imposes no temporal limit on the [EPA] Administrator's authority to withdraw the Corps' specification '*whenever*' he makes a determination that the statutory 'unacceptable adverse effect' will occur." The Court stated that the statute's use of the expansive conjunction, "whenever," demonstrated Congress's "intent to grant the Administrator authority to prohibit/deny/restrict/withdraw a specification at *any* time."

Additionally, the Court found that the Corps "specifies" areas for fill in the final permit itself. Thus, the Court reasoned EPA's veto power can *only* be exercised post-issuance. The Court also noted that the Corps has consistently maintained its right to exercise a post-issuance veto for approximately thirty years. The Appeals Court rejected Mingo Logan's arguments that EPA's veto conflicted with: (1) the plain statutory language; (2) section 404 as a whole; and (3) the legislative history of section 404(c).

2. Fourth Circuit Affirms Issuance of Valley Fill Permit

For the fifth time, the United States Court of Appeals for the Fourth Circuit has turned back a challenge by anti-mining groups to the permits needed to conduct surface mining in Central Appalachia. On May 15, 2013, a unanimous three-judge panel affirmed an earlier determination by a West Virginia district court that the Corps of Engineers complied with both the Clean Water Act and NEPA in issuing a §404 "fill" permit to Highland Mining for a surface mine in southern West Virginia.

On appeal, the Sierra Club argued that the Corps had "misapprehended" the baseline water quality in waters draining the fill area at issue and, consequently, could not accurately assess the impact of the fill discharges. Additionally, it argued that the Corps had irrationally rejected claims that conductivity discharged by the permitted operation would cause cumulatively significant adverse effects to aquatic life. In both instances, the Court determined that the Corps

understood the baseline and adequately considered potential cumulative impacts. As noted by the Court, "[c]ontrary to the Environmental Coalition's contention that the Corps failed to take a hard look at conductivity and stream impairment, the record amply shows that the Corps grappled with the issue extensively." Ultimately, the Court noted that once it determined that the Corps had taken a "hard look" at the environmental consequences, the Appellants' position was "reduced to no more than a substantive disagreement with the Corps," and that the review of the courts is limited and may not be used to second-guess substantive decisions committed to agency discretion.

In a concurring opinion, Judge J. Harvie Wilkinson expressed concern that the Corps had approved a permit that would increase conductivity levels in a stream already on the State's list of biologically "impaired" waters. He observed the EPA had expressed "significant concerns" about compliance with water quality standards, but ultimately concluded that the courts are a poor substitute for candid review by federal agencies. He noted that if the Court had seized solely on EPA's expression of concerns, "I fear we would stifle the very agency candor and applicant responsiveness that is essential to the proper functioning of the administrative process and, ultimately, to the goal of natural resource protection."

3. Sierra Club Targets Landowners for Clean Water Act Claims at Reclaimed Surface Mines

In three new lawsuits, the Sierra Club and other anti-mining groups have filed Clean Water Act ("CWA") citizen suits against landowners for discharges of selenium. The lawsuits involve mine sites where the State has terminated jurisdiction under both the Surface Mining Act and the NPDES program.

The Sierra Club has many pending CWA citizen suits against mine operators for claimed violations of "effluent limitations or standards" in cases where the mine operator still holds an NPDES permit. In those cases, the Sierra Club has sought to enforce both actual numeric effluent limits as well as water quality standards which have not been reduced to a permit-specific limit. These latest complaints represent a break from those previously filed cases.

The new complaints target landowners—not the mine operators. In each case, the mine at issue has been reclaimed and, with approval from WVDEP, the sediment control structures covered by the operator's prior NPDES permit have been removed. WVDEP has terminated its authority under both the SMCRA and NPDES programs. Nonetheless, the Sierra Club alleges that valley fills, or the water leaving them, are "point sources" subject to the NPDES program of the CWA.

In particular, the Sierra Club has focused on selenium, claiming that valley fills at each of the sites are discharging selenium without an NPDES permit under the CWA. Surprisingly, at some of the sites, the sampling data cited by the Sierra Club shows detectable concentrations of selenium, but at concentrations below the water quality criterion of 5 parts per billion. In those circumstances, if the landowner sought and obtained an NPDES permit from WVDEP, the WVDEP could well determine that there was no "reasonable potential" for the water leaving the fill to violate the water quality criterion and thereby elect not to impose a selenium limit.

The cases raise important questions, such as whether valley fills, which are not accompanied by a pond or other conveyance through which drainage leaves the fill area, are "point sources" subject to the NPDES program or are non-point source waters subject to other CWA controls. Likewise, there are issues about the interplay of SMCRA and the CWA. In order to achieve SMCRA bond release and authority to remove sediment control structures, mine operators are first required to demonstrate that they are meeting their NPDES limits without treatment. The extent to which landowners or mine operators can ever extract themselves from the CWA is jeopardized by these actions.

4. Federal Court in Kentucky Rejects Motion to Introduce Expert Testimony in Challenge to Mine-Related §404 Permit

A federal court has rejected efforts of the Sierra Club and others to introduce evidence outside the record in a challenge to a Corps-issued 404 permit. By order of June 12, 2013, the U.S. District Court for the Western District of Kentucky denied the Sierra Club's motion to introduce expert testimony in a challenge to a Clean Water Act §404 "fill" permit issued by the Corps of Engineers to Leeco, Inc. for fills associated with a surface mine. *See Kentuckians for the Commonwealth, et al. v. U.S. Army Corps of Engineers*, No. 3:12-cv-00682 (W.D. Ky.)

The Sierra Club's challenges to the permit have been advanced under both the Clean Water Act and NEPA. Those claims include allegations that the Corps was obliged to consider the health effects of mining generally on area populations based on recent papers which correlate health statistics to residential proximity to mines. Additionally, the Sierra Club has claimed that the Corps failed to adequately consider the impacts of the fills on downstream water and that the mitigation protocols used to design and approve mitigation do not replace the lost stream "functions." As to the latter claim, the Sierra Club sought to introduce the expert testimony of Dr. Margaret Palmer, who testified previously in similar challenges to §404 permits in West Virginia. It also sought to challenge the in-lieu fee component of the mitigation protocol used in Kentucky by calling an expert "ecological economist" to challenge the manner in which the Corps has monetized ecological impacts and benefits.

The Court noted first that "record review" is generally the rule in cases that rely on the Administrative Procedure Act, but that a "reviewing court may consider materials supplementary to the administrative record in order to determine the adequacy of the government agency's decision, even when the court's scope of review is limited to the administrative record." Ultimately, though, the Court declined the invitation to hear the Sierra Club's experts, expressing concern that the extra-record expert testimony would convert the case to a trial *de novo* from a "record review" case:

> The Court finds it unnecessary to consider the evidence proposed by Plaintiffs. First, the proposed additional evidence is voluminous, consisting of over 400 pages of documentation and testimony from two experts. While it is true that consideration of evidence outside of the record does not automatically turn a record review into a trial *de novo*, the Court fears granting Plaintiffs' motion would do just that. The

> amount of extra-record evidence Plaintiffs seek to introduce is at odds with much of the case law they cite in support of their request.

The ruling by the Court was at odds with a prior ruling of a district court in West Virginia in a similar case, but consistent with the Fourth Circuit's subsequent admonition that "consideration of extra-record evidence in a NEPA case does not, however, give courts license to simply substitute the judgment of plaintiff's experts for that of the agency's experts." *OVEC v. Aracoma Coal Co.*, 556 F.3d 177, 201 (4th Cir. 2009).

The Court will now proceed to consider the merits of the case based on the existing administrative record.

5. U.S. Supreme Court Upholds State's Right to Water Within Its Borders

The U.S. Supreme Court in *Tarrant Regional Water District v. Herrmann et. al.* held that states have a right to restrict out-of-state diversions of water. 569 U.S. ___ (June 13, 2013). The unanimous decision delivered by Justice Sotomayor held "[t]he Red River Compact does not preempt Oklahoma's water statutes because the Compact creates no cross-border rights in its signatories for these statutes to infringe. Nor do Oklahoma's laws run afoul of the Commerce Clause." The Red River Compact, 94 Stat. 3305, allocates water rights between the States within the Red River Basin. These States include Texas, Oklahoma, Arkansas, and Louisiana. Tarrant Regional Water District, a Texas Agency, brought this suit in an effort to acquire water under the Red River Compact from within Oklahoma. The Red River Compact is silent as to cross-border rights. Tarrant Regional Water District alternatively argued that the Oklahoma statutes unconstitutionally restrict interstate commerce because; Oklahoma water statutes limit out-of-state water diversions. Both arguments were denied by the U.S. Supreme Court.

6. The West Virginia Supreme Court of Appeals Provides Certainty by Defining the Term "Surface" When Used in a Conveyance

In West Virginia, there has been some confusion regarding whether a conveyance of "surface only" could possibly include any rights, minerals or formations underlying the surface, particularly if there is not an express reservations of such rights, minerals or formations. The source of this confusion is attributed to the West Virginia Supreme Court of Appeals case *Ramage v. South Penn Oil Co.* In *Ramage*, the Court held that the "term 'surface,' when used as the subject of a conveyance, is not a definite one capable of a definition of universal application, but is susceptible of limitation according to the intention of the parties using it; and in determining its meaning regard may be had, not only to the language of the deed in which it occurs, but also to the situation of the parties, the business in which they were engaged, and to the substance of the transaction." As a consequence of this holding, any conveyance of "surface only" was left open to interpretation by extrinsic evidence at a later date.

On June 13, 2013, however, the West Virginia Supreme Court of Appeals handed down the decision *Faith United Methodist Church v. Morgan,* in which the Court reconsidered whether the term "surface" in a conveyance is presumed to be ambiguous and open to interpretation through the use of extrinsic evidence as held in *Ramage.* The Court held that the term "surface" is not

presumptively ambiguous; instead, the term "surface" has a definite and certain meaning, which the Court articulated: "[t]he word 'surface,' when used in an instrument of conveyance, generally means the exposed area of land, improvements on the land, and any part of the underground actually used by a surface owner as an adjunct to surface use (for example, medium for the roots of growing plants, groundwater, water wells, roads, basements, or construction footings)." The Court expressly overruled the earlier decision, stating that it "deviated from certainty and uniformity in our property law . . . [and] is outmoded and is unjust." The Court expressed its hope that the holding in *Faith United Methodist Church v. Morgan* would "prevent and eradicate" uncertainties in land titles.

7. West Virginia Circuit Court Upholds Issuance of Mining Permit

A West Virginia circuit court recently upheld a decision by the West Virginia Surface Mine Board affirming the issuance of a surface mining permit challenged by members of the Coal River Mountain Watch.

The Coal River Mountain Watch challenged a permit issued to Marfork Coal Company for its Collins Fork Surface Mine on the grounds that the West Virginia DEP waited too long to hold an informal conference on the permit. By law, such conferences are technically required to be held within three weeks of the public comment period. In this instance, the conference was delayed by more than three years so that changes could be made to reduce the size of the operation. The operation was not only reduced in size, but designed to eliminate an historic mining site that had been left unreclaimed. Members of the Coal River Mountain Watch attended the informal conference and expressed their views.

Both the West Virginia Surface Mine Board and the Circuit Court of Kanawha County rejected arguments by the Coal River Mountain Watch that the permit needed to be vacated for not complying with the three week deadline. In reaching its decision, the circuit court noted that there was a technical violation of the three week deadline, but found that the Coal River Mountain Watch was not harmed in any way by the delay. Indeed, the circuit court found that the delay operated to the benefit of the Coal River Mountain Watch by allowing them to comment on the most recent version of the permit application.

8. Industry Groups and States Seek U.S. Supreme Court Review of D.C. Circuit Decision Involving EPA's Suite of Greenhouse Gas Regulations

Industry groups and states (including the State of West Virginia) recently filed petitions in the U.S. Supreme Court, seeking review of the D.C. Circuit's June 26, 2012, decision in *Coalition for Responsible Regulations, Inc. et al. v. EPA*, 684 F.3d 102 (D.C. Cir. 2012). The decision addressed challenges to the following suite of EPA rules regulating greenhouse gases (GHGs) under the Clean Air Act: (1) the Endangerment Finding (74 Fed. Reg. 66,496; Dec. 15, 2009) and EPA's denial of reconsideration of that finding (75 Fed. Reg. 49,556; Aug. 13, 2010); (2) the Tailpipe Rule (75 Fed. Reg. 25,324; May 7, 2010); (3) the Timing Rule (75 Fed. Reg. 17,004; April 2, 2010); and (4) the Tailoring Rule (75 Fed. Reg. 31,514; June 3, 0210). EPA promulgated these GHG regulations following the U.S. Supreme Court's ruling in *Massachusetts v. EPA*, 549 U.S. 479 (2007), that the Act's general definition of "air pollutant" was broad

enough to encompass GHGs and that GHGs were an "air pollutant" that was potentially eligible for regulation under the *mobile source* provisions in Title II of the Act.

9. US Supreme Court Grants Cert on CSAPR Rule

On June 24, 2013 the U.S. Supreme Court granted EPA's and American Lung Association's cert petitions in the CSAPR (Cross State Air Pollution Rule) Litigation. The Court's order limits the review to the questions presented in EPA's petition, which are:

1. Whether the Court of Appeals lacked jurisdiction to consider the challenges on which it granted relief.

2. Whether States are excused from adopting SIPs prohibiting emissions that "contribute significantly" to air pollution problems in other states until after the EPA has adopted a rule quantifying each state's interstate pollution obligations.

3. Whether the EPA permissibly interpreted the statutory term "contribute significantly" so as to define each upwind state's "significant" interstate air pollution contributions in light of the cost-effective emission reductions it can make to improve air quality in polluted downwind areas, or whether the Act instead unambiguously requires the EPA to consider only each upwind State's physically proportionate responsibility for each downwind air quality problem.