WEST VIRGINIA DIVISION OF ENERGY

MEMORANDUM

To: President Bill Cole, Chair
Speaker Tim Armstead, Chair
Joint Committee on Government and Finance

cc: Charlie Lorensen, 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: January 8, 2015

Re: Quarterly Report Ending, December 31, 2014
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 was prepared by David Flannery, Steptoe & Johnson PLLC. Reports are submitted on a quarterly basis.

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REPORT ON LITIGATION RELATED TO

ENERGY AND NATURAL RESOURCES IN WEST VIRGINIA

FOURTH QUARTER 2014

1. EPA Veto of Spruce Permit Upheld

By order entered September 30, 2014, the federal District Court for the District of Columbia, issued an order in which it upheld EPA's decision to prevent further work at the Spruce Mine of Mingo Logan Coal Company.

Mingo Logan had challenged EPA's action which vetoed the company's 404 permit. The company argued, in part, both that EPA could not act after the Corps had issued a permit and that EPA's decision was otherwise unlawful and unreasonable. In 2012, the district court ruled that EPA's action was untimely, and that the Clean Water Act prohibited EPA from using its 404(c) authority after the Corps had finally issued a permit. The D.C. Circuit Court, however, reversed that decision in 2013, ruling that the language granting EPA the right to act "whenever it determines" that a discharge will have an unacceptable impact is a grant of authority to act "at any time." The appeals court sent the case back to the district court to review the remaining challenges by Mingo Logan.

The September 30 decision rejects the remaining challenges by Mingo Logan to EPA's action. In doing so the Court ruled that despite comments in EPA's regulatory preamble that it should not use its 404 authority after a permit is issued unless there is new information not previously considered, there is no express requirement that EPA rely on new information. The Court also held that applying the high level of deference owed to EPA on factual issues, EPA's conclusion that there would be unacceptable impacts within the fill area itself is supported by the record. Finally, the Court held that EPA can rely on downstream water quality impacts in the exercise of its 404 authority even though those water quality impacts are the subject of an NPDES permit issued under Section 402 of the permit.

2. Federal Court Rules in Conductivity Case

On September 30, 2014, the federal District Court for the Southern District of West Virginia denied the motion of Fola Coal Company for a directed verdict in another Clean Water Act citizen suit alleging that discharges of conductivity by a mine operator are violating the State's narrative water quality standard. In these cases, the Plaintiffs rely heavily on the EPA Conductivity "Benchmark" as evidence that conductivity can cause adverse effects to aquatic insects.

At the end of the Plaintiffs' case tried in August, the mine operator moved for a directed verdict. It argued that Plaintiffs had not proven that the ionic mixture of Defendant's discharges was

sufficiently like that studied in the Benchmark to warrant the use the Benchmark as evidence of causation. It also argued that Plaintiffs must prove that the violation of the narrative water quality standard is caused by the discharge of a "pollutant," but that conductivity is only a characteristic of many pollutants and is not itself a pollutant that is causing impacts to aquatic life. The Court ruled that the waters are sufficiently like those used in the Benchmark to consider it as evidence. It also ruled that even though conductivity is not a "pollutant," it is a reasonable proxy for specific ions known to cause violations of the narrative water quality standard.

3.. EPA Amends CSAPR Compliance Dates and Allowance Allocations to Comply with Court Order

In response to the recent United States Court of Appeals for the District of Columbia Circuit's (D.C. Circuit or Court) order, the United States Environmental Protection Agency (EPA) issued an interim final rule on November 21, 2014 to amend the Cross-State Air Pollution Rule (CSAPR) compliance deadlines in 40 CFR parts 51, 52, and 97, which will be effective upon publication of the notice in the *Federal Register*, and a Notice of Data Availability (NODA) concerning emission allowance allocations for certain electricity generating units (EGUs).

Both documents are designed to be consistent with the United States Court of Appeals for the District of Columbia Circuit's (D.C. Circuit or Court) order on October 23, 2014 in *EME Homer City Generation, L.P. v. EPA* lifting the stay and tolling the compliance deadlines for three years of the heavily litigated CSAPR. However, CSAPR is still subject to on-going litigation, set for oral argument on February 25, 2015 before D.C. Circuit Judges Rogers, Griffith, and Kavanaugh. CSAPR was originally filed in 2011 and amended three times, by the Supplemental Rule, the First Revisions Rule, and the Second Revisions rule respectively.

The interim final rule provides that compliance with CSAPR's Phase 1 emissions budgets will now be required in 2015 and 2016 (instead of 2012 and 2013) and compliance with CSAPR's Phase 2 emissions budgets and assurance provisions will now be required in 2017 and beyond (instead of 2014 and beyond). Other amendments toll specific deadlines for sources to certify monitoring systems and to start reporting emissions, for the EPA to allocate and record emission allowances, and for states to take optional steps to modify or replace their CSAPR FIPs through SIP revisions. The amendments toll the regulatory provisions that sunset the Clean Air Interstate Rule (CAIR) (CAIR was EPA's prior attempt at a rule to regulate emissions of NO_x and SO_x under the CAA's Good Neighbor Provision, which was rejected by the DC Circuit but left in temporarily in place) upon its replacement by CSAPR, and establishes a new deadline for removal of CAIR NO_x allowances from allowance tracking system accounts.

The NODA provides notice of allocations of emission allowances to certain units that commenced commercial operation before 2010 and only to the extent that states do not provide alternative allowance allocations following procedures set out in the rule for compliance with CSAPR. These allowance allocations, which supersede the allocations announced in a 2011 NODA, reflect the changes to CSAPR made in those subsequent rulemakings as well as what EPA calls "re-vintaging" of previously recorded allowances to account for the impact of tolling of the rule's deadlines.

4. The U.S. Supreme Court Will Decide if EPA Should Consider Costs in Connection with Mercury Rule

On November 25, 2014, the Supreme Court granted certiorari to review the D.C. Circuit's April 2014 decision, which held that United States Environmental Protection Agency (EPA) had the authority to issue the Mercury and Air Toxics Standards for power plants under the Clean Air Act (CAA) §112 without considering costs when determining if the rule was "appropriate or necessary" under CAA §112(n)(1)(A) known as Mercury Air Toxics Standards (MATS). The MATS rule sets standards for the emission of hazardous air pollutants (HAPs) from electric utility steam generating units (EGUs or power plants) under the CAA. MATS applies to numerous power plants and establishes emissions limits for mercury, filterable particulate matter as a surrogate for toxic metals and hydrogen chloride as a surrogate for acid gases. EPA projected that the MATS rule will result $9.6 billion in annual costs but will create only $4-6 million in annual reduced HAPs benefit. 77 Fed. Reg. at 9,306, Table 2, Pet. App. 208a.

The issue on review, consolidated from the petitions filed by the Utility Air Regulatory Group, the National Mining Association and 21 states, including Michigan and Texas, was stated in the National Mining Association's petition as "whether an administrative agency, when authorized by Congress to regulate only if "appropriate," can deem the cost of the regulation irrelevant, with the result that, by the agency's own estimate, regulatory costs outweigh the benefits by almost two thousand to one."