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Governor

WEST VIRGINIA DIVISION OF ENERGY

Jeff Herholdt
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MEMORANDUM

To: President Jeff Kessler, Chair
Speaker Richard Thompson, Chair
Joint Committee on Government and Finance

cc: Jason Pizatella, Legislative Director
Keith Burdette, Cabinet Secretary, West Virginia Department of Commerce
Angel Moore, Deputy Secretary/General Counsel, West Virginia Department of Commerce

From: Jeff Herholdt, Director
West Virginia Division of Energy

Date: January 5, 2012

Re: Quarterly Report Ending December 31, 2011
Legal Challenges Potentially Impacting the Energy Industry

As mandated by SB 518, 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. Future reports will be submitted on a quarterly basis.

REPORT ON LITIGATION RELATED TO

ENERGY AND NATURAL RESOURCES IN WEST VIRGINIA

FOURTH QUARTER 2011

(Ending December 31, 2011)

1. Cross State Air Pollution Rule Stayed

In July 2011, EPA promulgated the Cross State Air Pollution Rule (CSAPR). The rule directs lower sulfur and nitrogen oxide emissions in 27 "upwind states." Many contend that the rule as written will force the closure of numerous coal-fired power plants, and hurt the reliability of the nation's electrical power system. Indeed, many power companies have already announced proposed plant closures in response to the rule. Various legislative and judicial challenges have been launched to stop CSAPR. In September, the U.S. House of Representatives passed H.R. 2401, the Transparency in Regulatory Analysis of Impacts on the Nation Act ("Train Act"), which would have delayed CSAPR pending further study, but the measure received no traction in the U.S. Senate. Similarly, in November 2010, Senator Rand Paul (R-KY) introduced a resolution to repeal CSAPR that was defeated by a vote of 56-41. Notably, Senator Joe Manchin (D-WV) has partnered with some Senate Republicans to propose legislation that would delay implementation of CSAPR by three years without nullifying the rule outright. Other legislation has been introduced to delay the rule by at least one year. On the judicial side, 45 plaintiffs – including numerous upwind states and power companies – have brought litigation in the D.C. Circuit Court of Appeals to challenge the rule. On December 23, 2011, the D.C. Circuit Court of Appeals issued a stay of the rule until the Court could address the merit of the various challenges to the rule.

2. OSM Sued Over Ten Day Notice Policy

In a case which has implicates for West Virginia, Farrell-Cooper Mining Company, a small mining company in Oklahoma, has sued the U.S. Office of Surface Mining ("OSM") challenging the issuance of two 10-day notices ("TDN") to the state involving two of Farrell-Cooper's state-issued coal mining permits. TDNs are the mechanism by which OSM can initiate oversight over conditions existing on sites permitted by states with OSM-approved programs under the Surface Mining Control and Reclamation Act ("SMCRA").

SMCRA allows OSM to take direct enforcement action against mine operators in primacy states for violations of performance standards or permit conditions, but only after a state fails to respond "appropriately" to a TDN advising it that OSM believes a violation exists. *See* 30 U.S.C. §1271(c). In the event a state does not respond appropriately (by taking enforcement action or explaining why no violation exists), the OSM "shall" inspect "the . . . mining operation at which the alleged violation is occurring. . . ." 30 U.S.C. §1271(a)(1). If, as a result of the inspection, OSM finds a violation, it shall issue either a cessation order (if there is imminent harm) or a notice of violation ("NOV") "to the permittee" fixing a time for abatement of the violation. 30 U.S.C. §1271(a)(2) & (3). Historically, because the statute speaks to "inspections" of "mining operations" and issuance of NOVs "to the permittees," OSM has generally limited the application of this section of the statute to "on the ground" violations of performance standards. It generally has not used this authority to oversee individual state permit decisions. In fact, when an OSM field office attempted to use its TDN authority to review a state permit decision in West Virginia, former Assistant Interior Secretary Rebecca Watson intervened and informed complaining citizens that OSM did not possess the authority to veto state permit decisions.

In June 2009, however, the Interior Department signed a memorandum of understanding with USEPA and the Corps of Engineers which committed OSM to determine how it could "more effectively conduct oversight of state permitting . . . activities" under SMCRA—polite language for requiring OSM to rescind the Watson letter. By memo of November 15, 2010, OSM Director Pizarchik rejected the rationale of the Watson letter and advised his staff that OSM would henceforth use its TDN oversight authority with respect to "alleged violations of permitting requirements" in addition to violations of performance standards. That memo was subsequently embodied in a draft policy document.

The Farrell-Cooper situation involves a dispute over approximate original contour ("AOC"), where the state-issued permits allowed the company to create last cut lakes at two of its mines. According to the complaint, OSM and the state of Oklahoma formed a team to investigate the legislative history of AOC, and the team issued a report in 1997 approving such techniques. However, in 2010, OSM issued a draft oversight report on AOC and found that the state had not properly implemented its approved program by failing to require mines to be reclaimed to AOC.

In January 2011, OSM issued two TDNs to Oklahoma attacking the Farrell-Cooper permits and reclamation plans for its mines. Farrell-Cooper has since received a notice of violation ("NOV") from OSM. The complaint will almost certainly be met with the standard governmental defenses that: 1) a TDN is not a final agency action; 2) the operator must exhaust its administrative remedies in appealing the NOVs; and 3) that this is not an attack on the permit, but rather of a failure to meet on-the-ground performance standards.

3. Judge Allows Citizen Suits to Proceed in Federal Court Despite Parallel Enforcement Actions in State Court

On December 7, 2011, Judge Robert Chambers denied Defendants' Motion to Dismiss and ruled that Clean Water Act ("CWA") citizen suits against three subsidiaries of Patriot Coal Corporation (Apogee Coal Company, LLC, Catenary Coal Company, LLC, and Hobet Mining, LLC) could proceed in spite of ongoing enforcement actions by the West Virginia Department of Environmental Protection ("DEP"). *See OVEC v. Patriot Coal*, Case 3:11-cv-00115. Pursuant to the CWA, a citizen suit is precluded where the "State has commenced and is diligently prosecuting a civil or criminal action in a court of the United States, or a State to require compliance with the standard, limitation, or order [that the citizen alleges to have been violated]." 33 U.S.C. § 1365(b)(1)(B). Although Judge Chambers found that DEP had commenced an action in West Virginia state court at the time the citizen suits were filed, he found that they lacked diligence.

In addressing the actions against Catenary and Apogee, the Court referenced its decision from September of this year in *Ohio Valley Envtl. Coal., Inc. v. Maple Coal Co.*, 2011 WL 3874576 (S.D.W. Va. 2011). In *Maple*, the Court examined enforcement actions DEP brought against Maple Coal in Fayette County Circuit Court. There, the Court noted that DEP would have granted Maple's request to extend its selenium compliance deadline had EPA not objected to the modification. *Id.* at 23. According to the Court, DEP's options to diligently prosecute an enforcement action against Maple consisted of either, (1) agreeing with EPA, acting as though the EQB stays had never been granted, and seeking to enforce the selenium limits from April 5, 2010 when they were scheduled to go into effect; or (2) disagreeing with EPA and requesting relief from the Fayette County court akin to that which DEP had initially planned to grant. The Court characterized DEP's enforcement action as failing to pursue either of these avenues. Rather, according to the Court, DEP filed a vague complaint that sought neither to enforce the permit as is, inclusive of the selenium limits, nor to enforce the draft permit modification, with a compliance deadline of July 2012.

In *Patriot*, the Court viewed DEP's enforcement actions in Boone and Logan County against Catenary and Apogee in the same way:

> As in *Maple*, neither enforcement action appears to seek any enforcement whatsoever with regard selenium. Instead, as in *Maple*, both actions seek vague relief from the Logan and Boone County Circuit Courts that specifically excludes selenium from the request for immediate relief on the grounds that the selenium limitations are subject to the stay orders of the EQB and the Kanawha County Circuit Court. By acquiescing in the Stay Orders, excluding selenium from their claims for civil penalties on the basis of those Orders, and seeking in State Courts the delays already

> rejected by the Environmental Protection Agency, the WVDEP is not diligently prosecuting Defendants' selenium violations. Based on their context, timing, and the relief sought, Court **FINDS** that these actions, like the one at issue in *Maple*, are not diligent prosecutions.

OVEC v. Patriot, p. 12.

Next, the Court addressed DEP's Boone County enforcement action against Hobet for four NPDES permits at its mine in Boone County. The Court had previously addressed the diligent prosecution issue as to the same four Hobet permits in *OVEC v. Hobet Mining, LLC*, 3:08-cv-0088, 2008 WL 5377799 ("Hobet I"). In Hobet I, although the Court found that the DEP's prosecution was not diligent at the time the citizen suit was filed, it found that the September 5, 2008 consent decree entered by the Boone County Circuit Court mooted the citizen suit in federal court. *Id.*, at 4-5. That consent decree, however, was modified by the parties in December 2009. The Court addressed the impact of the modified consent decree on a separate NPDES permit in *Ohio Valley Envtl Coalition v. Hobet Mining, LLC*, 723 F. Supp. 2d 886 (S.D. W.Va. 2010) ("Hobet II"). In *Hobet II*, the Court found that the amended consent decree was more lenient than the original and was, therefore, not a diligent prosecution. *Id.*, at 906-913. In re-examining the modified consent decree in light of the four permits originally at issue in *Hobet I* and currently at issue in *Patriot*, the Court again found that the "regulatory climate for violations of selenium limitations is defined by continued extensions and enforcement actions that, rather than enforcing selenium limits, seek to accomplish in state courts the delays already rejected by the Environmental Protection Agency." Consequently, the Court ruled that DEP's ongoing enforcement action against Hobet was not diligent.

4. WV EQB Lifts Conductivity Stay

The West Virginia Environmental Quality Board ("EQB" or "Board") has lifted a stay it earlier imposed on the use of an NPDES permit for a surface mine.

The stay, issued in the fall of 2010, prohibited the use of a new NPDES permit issued to Patriot Mining which did not impose effluent limits on conductivity, total dissolved solids ("TDS") or sulfate. The Sierra Club had argued in 2010 that absent limits on these parameters, discharges from the mine would cause violations of the State "narrative" water quality standards. The EQB granted a stay pending resolution of the appeal.

West Virginia's narrative water quality standards prohibit certain in-stream conditions. The standards are set out at WVCSR § 47-2-3.2.e & 3.2.i and provide that:

> 3.2.e. Materials in concentrations which are harmful, hazardous, or toxic to man, animal or aquatic life;

> 3.2.i. Any other condition, including radiological exposure, which adversely alters the integrity of the waters of the State including wetlands; no significant adverse impact to the chemical, physical, hydrologic, or biological components of aquatic ecosystems shall be allowed.

Historically, the West Virginia Department of Environmental Protection ("WVDEP") has used a biologic index known as the West Virginia Stream Condition Index ("WVSCI") as the primary tool for determining whether waterbodies met the narrative standards. The WVSCI is used to compare the numbers, types and proportions of so-called pollution-intolerant aquatic insects (measured at the "family" level) in undisturbed "reference" streams with the populations in disturbed streams. At some point, a difference in scores between a disturbed site and a reference site is considered sufficient to find that a disturbed stream is "impaired" or not meeting the narrative standard.

WVDEP does not have numeric criteria for conductivity, TDS or sulfate. It has also evaluated the correlation between each parameter and WVSCI scores and determined that there is a poor correlation between them. Because of that, WVDEP does not believe it can adopt a reasonable numeric standard on these parameters which would not be greatly over- or under-protective of WVSCI scores.

The Sierra Club, however, claimed in the appeal that when insect populations are evaluated at the "genus" level, rather than the "family" level used in the WVSCI, there are clearer correlations between the insect populations found and the levels of conductivity, TDS and sulfate. It contended that significant impacts to those populations occur at conductivity = 300 μS/cm, and sulfate = 50 mg/l, and argued that these levels should serve as in-stream aquatic life criteria used to impose effluent limits. Without significant dilution or expensive treatment, such as reverse osmosis, however, these standards are generally considered unachievable by most surface mines. The Sierra Club's experts suggested that there was not necessarily a causal link between conductivity and TDS on the one hand and insect impacts on the other, but that unspecified individual ions comprising the conductivity and TDS were likely culprits. Its experts also suggested that the WVSCI was not as precise a test as a genus-level insect index and should, therefore, not be used.

The EQB generally agreed and in March 2011 issued an order requiring that WVDEP impose effluent limits on each of the three parameters. Significantly, however, it did not determine or suggest that the threshold numbers advocated by the Sierra Club were appropriate. The EQB also ruled that WVDEP was obligated to impose limits on manganese and selenium, and to do a further analysis whether arsenic limits were necessary.

WVDEP and Patriot Mining appealed the order with respect to conductivity/TDS/sulfate. In an order dated September 20, 2011, the Circuit Court of Kanawha County ruled that

the EQB had not adequately explained the legal bases for its order; that WVDEP was entitled to deference in its interpretation of the narrative standards; and that the Board had failed to discuss the role of the WVSCI in measuring compliance with the narrative standard. The Court remanded the matter to the EQB.

On remand, Patriot Mining moved to dissolve the stay, arguing that there was no summarizing requirement to impose limits on conductivity/TDS and sulfate; that the Sierra Club was unlikely to prevail on remand; and that Patriot and its employees would suffer real harm while there would be little impact to the receiving stream, which already had high levels of the three parameters which would not increase appreciably with the new mine. By order of November 10, 2011, the EQB dissolved the stay.

The Board's dissolution order determined that on the balance of equities the stay should be dissolved because there was little evidence that the mine would contribute to any substantial impact on the insect population or to the levels of the three parameters in the receiving stream. However, the Board also stated that the Sierra Club was likely to prevail on the merits on remand—a fact which suggests that it may again require WVDEP to impose effluent limits on conductivity/TDS/sulfate that cannot be obtained without techniques so expensive as to destroy the economics of the operation.

5. EPA Exceeded Authority in Blocking Permits

In a ruling released October 6, 2011, a DC federal court judge ruled that EPA has been exceeding its authority under the Clean Water Act with its implementation of an Enhanced Coordination Process (EC Process), including the Multi-Criteria Resource (MCIR) Assessment, that effectively nullified the authority of the US Army Corps of Engineers. The EC process was a two-step process that began with the MCIR Assessment and proceeded to a separate coordination process between the Corps and the EPA. The MCIR Assessment involved the EPA applying 404(b)(1) guidelines and directing the Corps on which permit application must go through the EC Process for further review and coordination. The Corps was not involved in developing the MCIR Assessment. The Plaintiffs' alleged that the EC Process is a "burdensome review that is wholly separate from the process outlined in Section 404, the Corps' implementing regulations, and the 404(q) [Memorandum]." Additionally, the Plaintiffs maintained that the "EC Process adds a good deal of time to the permitting process because 'it involves discussions among [the] EPA, the Corps, the permit applicant, and other potentially relevant agencies during a 60-day coordination period.'" According to the industry, the EC Process has been used to obstruct the timely issuance of hundreds of mining permits in Appalachia since enacted in first months of the Obama Administration in 2009.

Siding with Plaintiffs, Judge Reggie Walton held that the intent of Congress was clear with regard to the lines of authority under the Clean Water Act, noting, "[a]lthough the Administrator of the EPA is tasked with administering the Clean Water Act, the Administrator's authority is subject to limitations. First, and most important, Section 404

of the Clean Water Act provides an express limitation on the Administrator's authority with respect to the issuance of Section 404 permits. The statutory language explicitly establishes the Secretary of the Army, acting through the Corps, as the permitting authority, which strikes the Court as an express limitation. Congress established a permitting scheme in which the Corps is to be the principal player, and the EPA is to play a lesser, clearly defined supporting role." Walton further held that "[w]ith the adoption of the MCIR Assessment and the EC Process, the EPA has expanded its role in the issuance of Section 404 permits and has thus exceeded the statutory authority afforded to it by the Clean Water Act..., the MCIR Assessment and the EC Process are not consistent with the legal duties and authority accorded the EPA by Section 404 of the Clean Water Act."

This ruling dealt with EPA's "Enhanced Coordination Procedures," through which agency officials were to work with the Corps and mining companies to reduce potential impacts of 108 permits that were part of a backlog of pending applications for Clean Water Act Section 404 permits. However, most of the permit applications that were backlogged and technically subject to the ECP have either been issued or were withdrawn by the mine operators. A key issue moving forward will be whether this ruling can be applied to post-ECP permit applications which are still being held up by EPA objections.