



Spring 2006

In This Issue

Practical Challenges in Water Withdrawal Permit Transfers: A Rejoinder	... cover
Message From The Chair	... page 2
Restoration-Based Settlements: The Need for Resource Banking	... page 9
Preemption and Removal in Toxic Tort Cases	... page 6

Upcoming Events

July 28 - 29**Annual Summer Seminar**

Crown Plaza Hilton Head Island Resort
Hilton Head, SC
<http://www.iclega.org>

Practical Challenges in Water Withdrawal Permit Transfers: A Rejoinder

Joseph W. Dellapenna, Professor of Law, Villanova University

The previous issue of the Georgia Environmental Law newsletter featured an article by James Renner, analyzing Georgia water law and advocating that the law be changed to authorize the transfer of water withdrawal permits. (Renner) The article quoted both from the Regulated Riparian Model Water Code (for which I served as the principal draftsman) and from a law review article that I wrote. Because I disagree with the article's analysis of Georgia water law and the author's faith in the utility of markets for water withdrawal permits, I have written a brief rejoinder to this article.

Who owns water in Georgia and what do they own?

The Renner article's analysis of Georgia water law is built around a quotation apparently of a passage of a single, fairly old Georgia decision. *Price v. Hughs Shoals Mfg.*, 132 Ga. 246, 64 S.E. 87 (1909):

Riparian proprietors have a common right in the waters of the stream.... Riparian proprietors have no title to the water which flows over their land, but are entitled to a reasonable use thereof.... The property, therefore, consists, not in the water itself, but in the added value which the stream gives to the land through which it flows.

These words are in the opinion, but they are torn from their context, appearing in widely separate parts of the text shorn of the surrounding discussions that provide clarity and meaning to these general statements. The point of the court's discussion is that one does not have an absolute property in water, but the right to make a reasonable use as determined by a jury in light of the impact of the use in question on uses by other owners. This case, along with every other case regarding on water rights in Georgia, says nothing about the rights, if any, of the State in the waters in question. The article, however, concludes its discussion of the quotation by asserting that "the state does not own the water, either;" but cites no legal authority for this proposition.

Consideration of the rights of the State in Georgia's waters should begin with the public trust doctrine—a doctrine that Georgia recognizes to some extent. *State v. Ashmore*, 236 Ga. 401, 224 S.E.2d 334 (1976). The only Georgia decisions regarding the public trust deal with the ownership of the shores of tidewaters and to the tidewaters themselves. *Rouse v. Department of Nat. Resources*, 271 Ga. 726, 524 S.E.2d 455 (1999). No Georgia case discusses

Continued on page 2

Message From the Chair

David Meezan

The Environmental Law Section kicked off 2006 with its annual luncheon at the State Bar's Midyear Meeting in January. Linda DiSantis, City Attorney for the City of Atlanta, was our distinguished keynote speaker. Linda reflected on her first three years as City Attorney and discussed some of the significant environmental issues facing the City. We are very grateful to Linda for taking time out of her very busy schedule to speak to the Section.

The Section's annual Summer Seminar is set for July 28 and 29 at the Crowne Plaza Hilton Head Island Beach Resort on Hilton Head Island, South Carolina (<http://www.cphiltonhead.com/>). The program agenda and registration information will be sent out soon, but it isn't too early to reserve your hotel room. I hope to see all of you there. As always, the Section also will be providing many additional educational and social opportunities throughout the year, and we will be announcing a more expanded agenda in the near future.

Finally, I would like to express my thanks to the Section for providing me the opportunity to serve as your Chair for the upcoming year. I will be joined by a group of excellent Board members: Andrea Rimer (Chair-Elect), Martin Shelton (Secretary), Bill Sapp (Treasurer), and Ann Marie Stack (Member-At-Large). I must also thank outgoing Chair Jeff Dehner, who did a terrific job leading the Section in 2005.

The Section's officers are always eager to hear from section members. If you have a brown bag or article idea, or want to add something to the Section's website (http://www.gabar.org/sections/section_web_pages/environmental_law) please contact one of us. We look forward to hearing from you.

Regards,

David Meezan

Practical Challenges in Water Withdrawal Permit Transfers: A Rejoinder

Continued from page 1

whether the public trust extends to non-tidal or non-navigable waters. This is no small omission. The public trust, like any trust, arises when one entity holds title to a res and other persons are beneficiaries of the trust. The beneficiaries of the public trust are the members of the public, while the owner of the trust res—arguably, all of the waters of the State—is the State. In other words, if the public trust applies to some or all of the waters of Georgia, those waters belong to the State in trust for the public. The closest we find to a Georgia decision that addresses the public trust is the case of *Givens v. Ichauway*, 268 Ga. 710 (1997). In that decision, the Georgia Supreme Court wrote, “A lessee of land on both sides of a creek has the right to exclude others from the creek unless the stream is navigable or some servitude exists.” The court did not mention the public trust, so it is not clear whether that is the servitude it had in mind, or whether it meant to suggest that the public trust did not apply unless the waters are navigable.

The absence of cases in Georgia on the public trust doctrine is hardly surprising.

The public trust doctrine has rarely been applied to water rights in a state adhering to the riparian rights tradition. While the public trust doctrine invalidates actions by the legislative or executive branch that do not serve trust purposes, courts usually approach such questions by balancing the trust interests against other public and private interests to determine whether the legislative or executive branches have acted improperly. In *re Water Use Permit Applications*, 94 Haw. 97, 9 P.3d 409 (2000). In western states, such decisions are becoming common because under appropriative rights no balancing of interests could otherwise occur. *National Audubon Soc'y v. Superior Ct.*, 33 Cal. 3d 419, 658 P.2d 709, 189 Cal. Rptr. 346 (1983). Under riparian rights, the public trust theory adds little directly to water allocation decisions. Rather, in riparian rights states, the doctrine serves to justify the legislature in enacting broad regulatory statutes to protect the public interest in the waters of the states. Georgia's legislature has done so in several statutes, including statutes that create a regulated riparian system for Georgia, applicable both to surface water and to

groundwater. OCGA §§ 12-5-31, 12-5-90 to 12-5-107.

The Renner article interprets Georgia's regulated riparian system simply as a permit requirement imposed on the preexisting riparian rights, limiting them but not changing them in their core requirements—that water use must be reasonable and is limited to riparian land *Stewart v. Bridges*, 292 S.E.2d 702, 704 (Ga. 1982) (use limited by a requirement of reasonableness); *City of Elberton v. Pearle Cotton Mills*, 50 S.E. 977 (Ga. 1905) (use on non-riparian land is per se unreasonable). Again, the article does not cite to any legal authority for these conclusions, for there is none. Georgia statutes require those using more than 100,000 gallons per day to obtain a permit from the State for such use. The statutes do not indicate that permits to use water are limited to riparian land; nor do they indicate that the permits may authorize uses on non-riparian land. Moreover, there have not been any decisions by a Georgia court construing the Georgia regulated riparian statutes. Without relevant Georgia authorities, one can only draw upon the general learning regarding regulated riparianism to interpret the import of these important statutory changes to the water law of Georgia.

About half of the states that fall within the riparian rights tradition now have enacted regulated riparian statutes. The prevailing interpretation is that these statutes have worked a fundamental transformation of the State's water law. *City of Waterbury v. Town of Washington*, 260 Conn. 506, 800 A.2d 1102 (2002). Under traditional riparian rights, the right to use water is treated as a species of common property, under which each user decides individually when, where, and how to use water, subject only to the limitations that the use must be on riparian land and that the use not unreasonably injure other users. (Dellapenna 2001, ch. 7) Under regulated riparianism, the State exercises its ownership of the water (already extant under the public trust doctrine) to transform the use of water into a form of participation in a system of public property. The State, through its permits, authorizes particular uses by particular persons for particular purposes, and usually for particular periods of time. (Dellapenna 2001, ch. 9) As in Georgia, some smaller uses are allowed to continue under the rules of the old common property regime, but they too are subject to the rights of the State to exercise its proprietary interest under the public trust doctrine.

Suppose the Renner article is correct that Georgia

remains a riparian rights state in which the permit requirement does not significantly affect the law applicable to water users. First, the article concludes that its interpretation means that permits to use water in Georgia are “inseparable from riparian land,” basing this conclusion on a reading of traditional riparian rights. It is true that traditionally the right to use water is tied to riparian land under riparian rights. See, e.g., *City of Elberton v. Pearle Cotton Mills*, 50 S.E. 977 (Ga. 1905). The Georgia Supreme Court, however, has attempted to accommodate transfers to owners of non-riparian land to some extent, although that extent is not altogether defined. *Pyle v. Gilbert*, 245 Ga. 403, 265 S.E.2d 584 (1980). The Renner article completely overlooks this aspect of Georgia water law, perhaps because the decision did not generate much of a market for riparian rights apart from the land. The lack of a functioning market could be explained by the continuing pervasive uncertainty about just the buyer obtains when purchasing non-appurtenant riparian rights. (Dellapenna 2001, §§ 7.04(a)(3) to 7.04(a)(3)(B)) Most potential water users apparently find it easier and more certain to buy riparian land rather than to buy non-appurtenant riparian rights.

This last point leads us to the real problem with traditional riparian rights—that the system merely leads into the tragedy of the commons. (Harden) As biologist Garrett Hardin explained some thirty five years ago, when common goods approach the carrying capacity of the resource, a “tragedy of the commons” ensues because each co-owner receives the full benefit of any added use, while the cost of this added use is spread over all co-owners. Acting purely rationally, each co-owner continues to place ever greater demands on the resource even as it is exhausted, if only because other co-owners are doing likewise. Adding demand is the only way to appropriate a share of a resource being grabbed by all. Many actual examples exist, including the exhaustion of fisheries in the high seas, national park access, and even the Federal treasury. (FAO; Sax; Fort & Baden) And this is precisely what happens under traditional riparian rights and which leads to the creation of more or less comprehensive regulatory systems in the riparian rights states.

Should Georgia allow permits to be traded?

As the Renner article notes, the State in Georgia already exercises a limited authority to impose involun-

tary changes in water usage, particularly during droughts under O.C.G.A. §§ 12-5-31(l)(1), 12-5-102, and has also used economic incentives, as in the Lower Flint Drought Protection Act, O.C.G.A. §§ 12-5-540 to 12-5-550. The article then asks why not simply add “voluntary transfers” to this mix. (By “voluntary transfers,” Renner primarily means market transactions, although it does suggest that some water users might prefer to make a gift to another potential user.) Put this way, it appears to be a modest suggestion indeed. Although the suggestion is introduced by recognizing that the State will have to exercise regulatory oversight over any such transfers which commensurate with the State’s interests in the waters of the State, the remainder of the article reads as if such oversight will not, or should not, play a major role in the market transfers. This point is misleading. It is in this regard that Renner cites the Regulated Riparian Model Water Code as imposing a duty on the State “encourage and enable the sale or other voluntary modification of water rights subject to the protection of third parties and the public interest.” Indeed, the Model Code does commit the State to encouraging such transactions, but the Code also explains, by way of commentary, that such transactions will likely always remain infrequent:

Yet, while the Code seeks to encourage voluntary modifications of permits to enable water to move to higher or better uses, two related problems make this ideal difficult to achieve. The first is the problem of the probability of externalities from any significant change in water use patterns. The second is the problem of “hold outs” who, in effect, can exercise a monopoly power if no voluntary modification of water use is possible without obtaining the contractual consent of every affected person related to a water source.

A case from Colorado pointedly illustrates the difficulty summarized in the above passage. In *City of Denver v. Fulton Irrigating Ditch Co.*, 179 Colo. 47, 506 P.2d 144 (Colo. 1972), the court considered an attempt to convey water from Denver to the Coors Beer Company. Colorado, like other western States, follows appropriative rights under which senior (older) water right holders are entitled to the full satisfaction of their water appropriations before a junior appropriator is entitled to take any water. Coors, seeking more water in order to produce enough beer to satisfy the demand for its product, and Denver, seeking

more water for its municipal needs, reached an agreement whereby Denver would take Coors’ clear mountain stream to augment its municipal supplies and Coors would have the right to use unlimited quantities of Denver sewage water for its brewery. The transaction failed not because of fear of possible outrage on the part of beer drinkers, but because a group of farmers downstream from Denver (organized as the Fulton Irrigating Ditch Co.) obtained an injunction against it because the trade would deprive the farmers of the water on which they were relying.

The problem illustrated by the Fulton Ditch case derives from the fact that water is an ambient resource—it moves from place to place and, in moving, is used and re-used by successive persons who obtain access to the resource at different points. This is equally true for groundwater as it is for surface waters. The question that arises when one changes the pattern of a use is not simply whether the new pattern of use is more efficient but how it impacts others dependent on the same water. A factory that recycles its wastewater may or may not cut off other users. It conceivably could even enhance the water available for other users if, for example, less water overall were withdrawn from a river and, with less effluent discharged into the river, the water were to flow down to other users in a purer state. If Denver had simply undertaken to recycle its wastewater through the municipal system, that too might not have affected the farmers in the Fulton Ditch case. It all depends on how that recycling fits into the overall pattern of use in Denver. But when water goes into a brewery, it goes out on trucks. There is no way that can fail to affect other users awaiting the water downstream.

In Colorado, as in all appropriative rights states, changes that affect other water users are properly understood as dispossessing the other users of their property in the right to use water. If one takes the idea of a property right to use water seriously, one must protect everyone’s property right, and not just the property of those engaged in a conveyance of such a right. Thus, in every appropriative rights state, the law prohibits changes in the time, place, or manner of use if the change would adversely affect the holders of other water rights, even junior water rights, without obtaining the consent of all affected holders of water rights. Denver and Coors might have paid the farmers in the Fulton Irrigating Ditch Co. to waive their objections. Yet this would simply have resulted in objec-

tions by the next group of users downstream, and so on, so long as any material effect of the transaction could be traced. The result is that on any sizeable stream, market transactions as well as other changes in patterns of water usage quickly become prohibitively expensive. Thus, even in appropriative rights states—states in which water rights most closely approach private property rights—markets for water rights never developed, except for small scale transactions between persons making similar uses in nearby locations. (Dellapenna & Draper) Markets—true markets—just have not been practical mechanisms for managing large bodies of water. If the open access that characterizes traditional riparian rights leads to the tragedy of the commons, the rights of nearly innumerable persons to forbid access to newcomers on fully appropriated streams that is characteristic of appropriative rights leads then to a “tragedy of the anti-commons.” (Heller) Uses are effectively frozen in place unless some mechanism other than voluntary transactions among current and potential water users. (Blumm)

Haven't markets for water been successfully implemented elsewhere?

The basic problem in many areas today, particularly in the dry western States but increasingly in the humid eastern States, is the difficulty in changing the location and pattern of use on a large scale. This has not been done through markets—it has been achieved, for example, in western States by administrative management masquerading as markets. (Dellapenna 2001, § 6.01(b)(2)) Consider the highly touted California Water Bank. During a five-year drought in California, the State transferred water from lower valued agricultural uses to higher valued urban uses by creating a “market” where none had existed by creating a “water bank.” The water bank involved in its peak year (1992) 400,000 acre-feet, while the shortfall alone exceeded 6,000,000 acre-feet. The water bank was a most unusual “market”: For the 350 persons willing to sell their water rights, the state was the only buyer; for the 20 institutions willing to buy water rights, the state was the only seller. California simply decreed that when it buys or sells it need not concern itself with the effects of its transactions on third parties, even valid third-party water rights. Nor did the resulting prices (\$125/ac-ft. to sellers, \$400/ac-ft. to buyers) result from bidding in the market place—the prices were set by administrative fiat. The State chose the sellers and decided that it would only sell to bedroom

communities in the greater San Francisco-San Jose area; other water users who might have been willing to pay more for the water simply were excluded from purchasing the water. The State, implicitly (and sometimes explicitly) underscored its “offers” to buy with the threat of condemnation, and the state sold at a standard price to buyers selected on the basis of criteria other than willingness to pay what the market will bear.

Under the California water bank system, the state applies economic incentives to encourage persons to comply with the State’s policy choices while disregarding the effects of the State’s actions on yet other actors whose claims would preclude accomplishment of the State’s goals. Flexibility was introduced to enable fundamental transformation of water uses within the state, but there were other effects, most notably that wealth is transferred from those who formerly used water to those who thereafter would use water. (Carter, Vaux, & Scuering) These may or may not be laudable goals in California in the late twentieth century, but the means used to achieve these goals do not involve either private property rights in water or the functioning of a true market. Nor have other highly touted “examples” of successful markets for water born up under close example of what actually happens in these institutions, as opposed to what economic theorists assume happens. (Bauer) For example, the recent efforts to cope with water shortages in southern California by arranging a sale of water from the Imperial Valley Irrigation District to San Diego represent a market—after the District board rejected the proposed sale, the Secretary of the Interior cut the water allocation of the District by 15%, informing them that they would get the water “back” only if they “sold” it to San Diego on terms approved by the Secretary. The board approved the deal by a 3-2 vote in April 2005, again on terms that effectively transferred wealth from the poor to the rich, so much for voluntary transactions. (Dellapenna 2005, § 6.01(b)(3))

How can Georgia cope with growing water shortages?

Governmental management of some sort, including economic incentives in proper cases, is necessary to cope with striking a balance between supply and various demands. And this is precisely the direction that states adhering to riparianism have taken in enacting regulated riparian statutes (a public property system) rather than

attempting to introduce appropriative rights (a private property system) into eastern states. Georgia, in fact, has already done so, although the system now in place in Georgia leaves lots of room for refinement and improvement. (Dellapenna 2002) This is not because governmental management will function perfectly. It certainly will not. (Dellapenna 2001, §9.01(a)(5)(D)) But governmental management provides the only mechanism whereby all affected interests can be considered and accommodated, especially given the utter failure of markets in this regard. The question, for Georgia and for other states, is how to design the system to minimize the risk of governmental mismanagement.

Mr. Renner referred to the Regulated Riparian Model Water Code, which has been approved by the American Society of Civil Engineers as a “standard” that it recommends for adoption in every state following the riparian rights tradition. The Model Code synthesizes the best provisions drawn from all 17 of the existing regulated riparian statutes while developing some new provisions that the Society has judged would refine and improve the regulated riparian system. One goal of the Society is greater uniformity in state law on these matters. Acceptance of the Model Code by state legislatures would foster a uniformity that not only would be convenient for engineers working in several states, but it would also make the resolution of cross-border problems easier. (Dellapenna 2005) Yet, not every provision in the Model Code will be suitable for every state, and the drafters fully expect that any legislature considering enacting it would revise the Model Code to fit the particular social, cultural, economic, hydrologic and other characteristics of the state.

Regulated riparian statutes create mechanisms for long-term planning and for otherwise providing for the public interest in the waters of the State. One of the major purposes of regulated riparian permits is to assure the gathering of the necessary information to enable planning on an on-going basis. The administering agency also usually has broad discretion, particularly for planning for and dealing with extreme water shortages. The statutes also provide minimum stream flows and otherwise protect the public interest in the waters of the State. (Bowman; Breckenridge) Under these statutes, the State takes primary responsibility for assuring that particular water uses are consistent with the public interest and do not unreasonably interfere with other authorized uses by requiring that, with only limited exceptions, no water is to be withdrawn from a water source without a permit from the state within which the withdrawal occurs. The Renner article’s suggestion

that markets would better protect these values—or, at least, better protect minimum flows—is disingenuous at best. The article cites economist Andy Keeler’s argument that markets would allow those who value maintaining instream flows to buy the necessary water from other water users—as if public interest environmental groups could ever raise sufficient funds to compete on an adequate scale with industrial, agricultural, and other consumptive uses.

Under regulated riparianism, permits determine the rights of water users, not the riparian nature of the use. (Often a principle motive for enactment of regulated riparian statutes was to authorize the use of water on non-riparian land.) The criterion by which permit applications are judged is whether the proposed use is “reasonable,” just as under riparian rights. The criterion of “reasonable use,” however, is applied very differently than under common law. The administering agency decides before a use begins whether the use is reasonable, both in terms of general social policy and in terms of the effects of the proposed use on other permitted uses. The administering agency is to impose conditions on permits designed to protect other lawful uses and public values. The statutes often contain preferences for certain classes of uses. Temporal priority has been accorded only a strictly limited role in the permit process. *Harloff v. City of Sarasota*, 575 So. 2d 1238 (Fla. Ct. App. 1991). Finally, permits are issued only for a period of time (3-20 years) so that when a permit expires the question of the continued reasonableness of the use can be reexamined. (Georgia limits the duration of permits other than for agricultural uses begun before July 1, 1988.) Some states (and the Model Code) authorize the voluntary transfer of water use permits. But in those states, the transfer must be reviewed and approved by the administering agency according to the same criteria as an original permit application.

The Renner article posits that the Regulated Riparian Model Water Code enhances the certainty of water rights because it provides, “a framework for identifying reasonable use that is vague enough to be applied broadly but clarifies the aims of reasonable use: necessary for economic and efficient use without waste, without unreasonable injury to other uses, and consistent with the public interest (which is further defined as a pervasive goal of sustainable development).” This is accurate as far as it goes, but the Renner article approaches the question of “reasonable use” in a fashion not supported by the Model Code or by regulated riparianism in practice. The article seems to suggest that the goal is to draw up a list of “reasonable uses” which, once completed, automatically leads to a permit for any proposed use that falls within the scope of that list. Because the administering agency is to evaluate permit applications for their individual impacts on other individual permitted uses, and not just classes of use on other classes of use, having a

list of “reasonable uses” (if such a list were to be created; such lists are not required by the Model Code or actual regulated riparian statutes) would not assure anyone a permit and would do little to facilitate the permit process. After all, only a rare use that was extremely destructive of the water resources themselves would be left off such a list. Reasonableness is a relational test and not an abstract test as the Renner article suggests.

Space does not allow an extensive analysis of regulated riparianism in general or even of the Georgia version of regulated riparianism. Suffice it to say that the Georgia version, like all versions of regulated riparianism, exhibit the core features of the new approach to water law while featuring numerous differences in detail from both the Regulated Riparian Model Water Code and from other actual statutes. Some of these features perhaps suggest that Georgia has not gone as far towards embracing the new system as some other states, while other features are more advanced along this direction than most regulated riparian statutes. Nor have we any court decisions in Georgia to confirm whether regulated riparianism is now the dominant form of water law in Georgia or whether traditional riparian rights remains the dominant form, in either case with the other form supplementing the dominant one. The Georgia Attorney General’s Office, on the other hand, has explicitly indicated that, at least for withdrawals of 100,000 gallons per day or more, “Georgia’s surface water law can be classified as a form of the Regulated Riparian doctrine and Georgia’s groundwater law can be classified as a form of the Regulated Reasonable Use doctrine for groundwater. These are the same legal doctrine under different labels.” (Bomar) Clearly, that both forms of law are significant in Georgia. For those using more than 100,000 gallons/day, regulated riparianism is the law; those using less than 100,000 gallons/day remain under the regime of riparian rights. Most agricultural uses have special rules that make the relationship of the regulatory regime and traditional riparian rights for them less than clear. For either legal regime, however, voluntary transfers (market transactions) cannot, for all of the reasons adduced, be more than marginal for water management. (Barmeyer)

Is the law of groundwater different?

The law applicable to groundwater, at least in Georgia, is not very different from the law applicable to

surface water. There is an open access regime—referred to in Georgia as the “absolute dominion” rule—supplemented or replaced, as the case may be, by a regulated riparian regime specifically applicable to groundwater. O.C.G.A. §§ 12-5-90 to 12-5-107. It is perhaps unfortunate that the courts in the nineteenth century spoke in terms of “ownership” or “dominion” when the reason they refused to recognize claims from neighboring landowners whose wells were drying up or otherwise interfered with by a defendant landowner’s use or abuse of groundwater was that too little was known or understood about groundwater for a court to be able to determine cause and effect or a remedy. *Saddler v. Lee*, 66 Ga. 45 (1879). Even in Georgia, however, the “absoluteness” notion was abandoned if the defendant acted maliciously or created a private nuisance. *St. Armand v. Lehman*, 47 S.E. 949 (Ga. 1904) (malice); *Tri-County Investment Group, Ltd. v. Southern States, Inc.*, 231 Ga. App. 632, 500 S.E.2d 22 (1998) (nuisance).

The old phrasing of “absolute dominion,” however, leads modern groundwater users to think in terms of private property in the classic model—mine alone, from which I can exclude all other users. This completely ignores the reality that groundwater passes through the hydrologic cycle in exactly the same way as surface water. While groundwater usually moves more slowly through the soil than a river on the surface, each is an ambient resource, the use of which by one person inevitably affects the uses of many others dependant on the same source. And, indeed, groundwater and surface waters are intimately interconnected, so much so that, as one hydrologist once commented, the base flow of a river is but exposed groundwater. (The “base flow” is the minimum flow in a stream during the driest part of the year.) Once one realizes the true nature of groundwater, the idea of a different legal regime for groundwater and surface waters is simply ludicrous. It is also clearly wrong to think of groundwater as subject to a regime of classic private property unless, as under appropriative rights, any affected user of groundwater is given a veto over any change in other landowner’s use of the water. Instead, at most the “absolute dominion” must be seen as recognizing a sort of common property which, given today’s knowledge about the behavior of groundwater, can hardly be thought of as absolute.

For groundwater no less than for surface waters, one landowner’s exercise of her “absolute” dominion interferes with or destroys other landowners’ “absolute” dominion.

Practical Challenges in Water Withdrawal Permit Transfers: A Rejoinder

Continued from page 7

Today, there is no shortage of knowledge or understanding of where groundwater comes from or how it behaves. There thus is no excuse for courts any longer to refuse to resolve disputes among common property owners whose uses of groundwater are interfering with each other. In the great majority of states that once embraced the “absolute dominion” rule, the courts have undertaken to do so under a reasonable use rule that is the same as is applied under traditional riparian rights, although some have embraced a “correlative rights” rule that attempts to apportion water on a pro rata basis among water users. (Dellapenna 2003, chs. 18-22) In Georgia, the law applicable to these disputes ought to be a mix of regulated riparianism and a common law based reasonable use rule depending on the particular circumstances of the dispute.

References

- Barmeyer, William B. 2005. “*Note: The Problem of Reallocation in a Regulated Riparian System: Examining the Law in Georgia.*” 40 Ga. L. Rev. 207.
- Bomar, Robert S., Deputy Attorney General. 2002. “*Georgia Water Law*” (White Paper to the Joint Comprehensive Water Plan Study Committee), available at www.cviog.uga.edu/water.
- Bowman, Bradford. 2002. “*Instream Flow Regulation: Plugging Holes in Maine’s Water Law.*” 54 Me. L. Rev. 287 (2002).
- Breckenridge, Lee P. 2004. “*Maintaining Instream Flow and Protecting Aquatic Habitat: Promise and Perils on the Path to Regulated Riparianism.*” 106 W. Va. L. Rev. 595.
- Dellapenna, Joseph W. 2000. “*The Importance of Getting Names Right: The Myth of Markets for Water.*” 25 Wm. & Mary Env’tl. L. & Pol’y Rev. 317.
- Dellapenna, Joseph W. 2001. “*Riparianism*” in Robert E. Beck, ed., *Waters and Water Rights* (2001 replacement vol.).
- Dellapenna, Joseph W. 2002. “*The Law of Water Allocation in the Southeastern States at the Opening of the Twenty-First Century.*” 25 U. Ark. Little Rock L. Rev. 9.
- Dellapenna, Joseph W. 2003. “*Quantitative Groundwater Law*” in Robert E. Beck, ed., *Waters and Water Rights* (2003 replacement vol.).
- Dellapenna, Joseph W. 2004. “*Special Challenges to Water Markets in Riparian States.*” 21 Ga. St. L. Rev. 305.
- Dellapenna, Joseph W. 2005. “*Interstate Struggles Rivers: The Southeastern States and the Struggle over the ‘Hooch.’*” 12 NYU Env’tl. L.J. 828.
- Dellapenna, Joseph W. & Stephen E. Draper. 2004. *Water Markets and Misinformation*.
- Food & Agric. Org. of the United Nations (“FAO”). 2002. *The State of World Fisheries and Aquaculture: Part 1: World Review of Fisheries and Aquaculture*, available at <http://www.fao.org/docrep/005/y7300e/y7300e00.htm>.
- Fort, Rodney D. & John Baden. 1981. “*The Federal Treasury as a Common Pool Resource and the Development of a Predatory Bureaucracy*” in John Baden & Richard L. Stroup eds., *Bureaucracy vs. Environment: The Environmental Costs of Bureaucratic Governance*.
- Hardin, Garrett. 1968. “*The Tragedy of the Commons.*” 162 Sci. 1243.
- Heller, Michael A. 1998. “*The Tragedy of the Anti-Commons: Property in Transition from Marx to Markets.*” 111 Harv. L. Rev. 621.
- Renner, James F. (Winter 2006) “*Practical Challenges in Water Withdrawal Permit Transfers.*” St. Bar Ga. Env’tl. L. Sec. Newsletter 4.
- Sax, Joseph L. 1980. *Mountains without Handrails: Reflections on the National Parks*.

Restoration-Based Settlements: The Need for Resource Banking

Jeffrey Andrienas, L.G., Premier Environmental Services, Inc.

Scott D. Lockert, L.G., Premier Environmental Services, Inc.

Environmental liability is not just a matter of site cleanup. Indeed the liability extends to Natural Resource Damages (NRD) and the costs of restoration. The National Oceanic & Atmospheric Administration (NOAA) active pursuit of NRD liability, has set in the motion the need to create means to quantify the damages by determining the value of NRD resources. With NRD claims it is not a matter of a one to one acre exchange in settlement; NRD resources are valued differently. In order to pursue NRD, new guidelines have been established and this article will focus on the need for an approach called resource banking. As defined by NOAA, resource or restoration banking “is the ability of an entity to gain ‘credits’ for restoration and to use these ‘credits’ to offset a liability for natural resource injury or to sell them to another entity for similar use.” Resource banking lays the groundwork for corporate entities to trade restoration for liability, and often discover resource assets in the process.

This article will examine how changes in environmental liability have evolved into a shift toward restoration-based settlements, the subsequent need for resource banking; and its benefits for all parties. In addition, a change in Financial Accounting, effective December 15, 2005, makes potential environmental liability an issue for every corporation and therefore increases the need for every business entity to be aware of resolution options, such as resource banking.

The Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) has been in existence nearly thirty years and the focus is now shifting to the provisions regarding Natural Resource Damages. Natural resource damages include injuries to land, fish, wildlife, biota, air, water, groundwater, drinking water and other such resources. Although CERCLA provisions

addressed NRD liability, funding was only available for site cleanup/remediation, not for quantifying natural resource damages or completing restoration. The NRD costs were typically documented and calculated as part of a second tier response. A major problem has always been the lag between CERCLA and NRD. CERCLA site investigations were usually precipitated by a specific spill incident or a pending property transfer. The NRD portion operated on a different timeline, without a well-defined regulatory framework, and with multiple stakeholders, thereby trailing remediation efforts and potentially delaying a settlement by five to ten years. Over the last six years, NOAA has been working with other trustees and industry representatives to develop what is known as a Cooperative Assessment Process (CAP) in order to better integrate the overall interests of all parties affected - by setting a common goal of restoration.

The historical path has always led from straightforward remediation (first response) to the NRD process, with its focus on restoration for resolution of a claim. Along this path has been the move towards cooperative planning between the trustees and PRPs. NRD trustees have developed models that are used to quantify the damages and costs of restoration. NRD trustees have been able to very successfully litigate against damages from historical pollution conditions from past practices of industry. Methods that quantify NRD damages, such as Habitat Equivalency Analysis (HEA) are becoming more widely accepted. Prior to the use of HEA, industry could satisfactorily argue that NRD was a punitive damage levied by regulatory agencies, and therefore could not be predicted. This is simply no longer the case; in 2002 alone NOAA settled over \$300 million in NRD liability; potential liability must be anticipated and the following accounting change stipulates that it must be shown on the corporate books.

As of December 15, 2005 (or no later than the end of the fiscal year ending after this date) the NRD path collides with that of financial accounting for corporations. The intersection of these two paths has the potential to completely change the issue of environmental liability. The policy change is set out in Financial Accounting Standards Board Interpretation No. 47: Accounting for Conditional Asset Retirement Obligations. This interpretation of Financial Accounting Standards Board (FASB) Statement No. 143 states: “An entity shall recognize the fair value of

Restoration-Based Settlements: The Need for Resource Banking

Continued from page 9

a liability for an asset retirement obligation in the period in which it is incurred if a reasonable estimate of fair value can be made.”

In very simple terms, industry now needs to account for future environmental conditions associated with any known assets as an asset retirement obligation. In Appendix A, Illustrative Examples, the FASB publication describes a scenario in which an entity has purchased kilns lined with refractory bricks. The bricks will become contaminated in the course of operations and once removed will incur costs associated with hazardous waste disposal. Once operations begin, the entity is responsible for estimating the costs of disposal, known as fair value of the liability, using a present value technique. Although the refractory bricks may not need to be replacement or disposal for many years, as of the start of operations the asset retirement obligation needs to be carried on the corporate books. Now, take this scenario and apply it to an entity that will be responsible for a large-scale site cleanup and restoration; future NRD costs must be considered as an asset retirement obligation even if a value cannot be determined for many years.

This convergence of FASB and NRD, as quantified through HEA, would seem to create a nearly insurmountable challenge due to the inability to fully account for future regulations that might affect site contamination. This is where the alternative and non-adversarial approach emerges: resource, or restoration, banking. This approach accepts that a restoration-based settlement is going to prove beneficial to all parties and will increasingly be the accepted model. Resource banking involves examining the present site and its role within a habitat to determine if there are potential assets that may offset future liability. For example an entity may actually own a resource that they are not aware of, such as an underground spring that could be extremely beneficial if restored. An example from industry is that environmental consultants are currently in negotiations to create one of the first groundwater NRD banks which will replenish several billion gallons of clean water to depleted aquifers. This asset was created for a non-PRP landowner as a cost-effective way of meeting Trustee expectations at a price affordable to industry and

their carriers. This is an emerging field and represents a breakthrough in strategic environmental planning.

The focus of CERCLA has always been on determining the damages, identifying an acceptable remediation plan and establishing the dollar costs. Remediation would occur with the NRD component scheduled to occur as a second tier response; even though remediation planning and funding of the pre-NRD phase could take up to ten to fifteen years. The specific NRD process, once reached, includes many additional steps, and by definition must involve the Trustees (NOAA, Department of the Interior (OI), Indian tribes, state and local government) and the PRPs. The dollar amount for damages, including restoration costs, has not historically been presented until the end of the process. The process usually takes years, so a considerable length of time passes before an entity can be free of its liability and many years before the habitat restoration even occurs. This is not a situation that benefits any party. In addition, a frequent scenario in the last 25 years has been the necessity for the federal government to bring suit against an entity in order to force cleanup or recover cleanup costs. These suits have led to protracted legal battles, with the government and PRP spending up to \$1 million/year in legal fees. If the legal battle takes ten years this may have resulted in \$10 million spent, with none of it going to habitat restoration.

Luckily, the objectives of NRD lend themselves to the cooperative assessment model introduced earlier, because the overall goal is not to have a punitive element but rather to “make the public whole” through restoration. NRD includes both primary and compensatory restoration stages. Primary restoration returns injured natural resources and services to baseline, and includes efforts to restore, replace, rehabilitate, or acquire the equivalent of injured natural resources or services. Compensatory restoration addresses the interim losses from the date of the incident until natural resources are restored to baseline. Hence, another reason to move the process more quickly, to reduce the costs of services lost that continue to accrue during the interim period. The economics of NRD include the costs of assessing the damages, the value of lost services, and determining the costs to restore the injured

natural resources. In cases involving oil spills, the PRP is offered a choice of implementing restoration themselves (with Trustee oversight) or simply paying the costs of restoration. This model is increasingly used for hazardous waste situations as well, once again illuminating the shift to restoration-based settlements.

The Cooperative Assessment Process was developed by a workgroup in response to the desire by industry to play an increased role in the early stages of damage assessment. The focus in CAP is for the stakeholders to agree to the common goal of restoration, with the benefit of lowering restoration costs by acting quickly, creating a restoration plan that serves the interests of all Trustees, and allowing a consensus approach to resolving liability that helps to avoid litigation. The key elements of CAP are streamlined coordination with response agencies, increased data sharing, mutual framework for planning and decision-making, public input and pooled funding. The result is a quicker route to an overall solution and one that benefits the habitat, the Trustees, the PRP and their carriers, and the public. With the increasing success of CAP has come the ability to be more proactive about potential asset liability, through the concept of resource banking.

In order to understand this concept, let's return to the hypothetical entity with the brick kilns that will need hazardous disposal in the future. Let's assume that site cleanup will be necessary as well. What if this entity is located so that its property fronts the river but operations are inland, the waterfront acreage unused? And what if it so happens that restoration is underway so that this river will again provide a habitat for birds and fish; perhaps even a threatened or endangered species. At this point the corporation that owns the kilns may have the potential for reducing its liability by booking a value for the habitat restoration credits by maintaining the waterfront or agreeing to make it available as a waterfront park.

There have been many references to banking of these resource credits, but how does such a virtual bank operate? The currency is in what is known as Discounted Service Acre-Years (DSAY). DSAYs are the crux of resource banking because they are the standard and accepted unit of measure. DSAYs are determined from the results of Habitat Equivalency Analysis (HEA). HEA is the methodology used to determine compensation for resource

injuries. The framework of HEA calls for: 1) resource/service losses to equal the resource/service gains, 2) for injured and restored resources to be of similar type, quality and value, and 3) depending on the specific situation an agreed valuation type will be used (resource to resource, service to service, value to value or value to cost). Whether compensation will be in the form of cash or constructed resources, the process of determining the value is the same and relies on determining the active and passive uses of the resource, as well as lost use (scaling).

Depending on the specifics of the damages, a specific value can be assigned to each DSAY. For example, one DSAY is assumed by NOAA to be the equivalent of \$50,000 although the actual amount of a DSAY for a specific habitat is negotiated. Depending on calculated DSAY value, a PRP and its insurance carrier may cash out their liability. A financial transfer occurs based on value per DSAY, and is banked to cover the actual restoration costs. The monies are held in a NRD Trust, with Trustee oversight. The process is similar to that used in wetland mitigation but instead of acres changing hands, there are dollars exchanged for mitigation. Just as DSAYs are used to calculate resource losses, they are also used to calculate gains that will occur through restoration.

The benefits of offsetting liability through restoration can be broad and affect many parties. Consider past lessons involving complex multiple party sites such as Boston Harbor or Commencement Bay in Tacoma, Washington. These early Superfund sites have been mired in bureaucratic processes and litigation for decades. With injuries beginning in the early 1900's, multiple parties, and multiple Trustees, the timeline of the Commencement Bay settlement and restoration process has stretched over twenty years, with nearly \$30,000,000 spent on studies and litigation, but not as much on habitat restoration as Natural Resource Trustees would have liked. Ultimately the restoration efforts of such multiple party sites may resemble more of a patchwork quilt, with little ecologically significant coherency derived from restored areas interspersed with non-restored. In the end the public has not been made whole.

Another case with a different outcome involves wastewater discharge from an oil refinery into Bayou Trepagnier in Louisiana. The investigation process lasted from 1984 to 1992 the subsequent eight years were mostly

Restoration-Based Settlements: The Need for Resource Banking

Continued from page 9

wasted due to the threat of litigation, concealed data, and the lack of involvement by Trustees and the public. In 2002, in a pilot of CAP, the parties agreed to work together with a focus on restoration. The results were such that in less than a year a legal agreement had been reached, cleanup had started and restoration was on target for completion in 2005. Note how the shift to restoration broke the bottleneck. With the ability to cash out or bank ahead for restoration the PRPs may be particularly motivated to settle.

The potential for resource banking has other benefits to PRPs as well. Resource or restoration banking through use of market forces allow for greater value to be realized at what might be a significant cost reduction. At the same time, the ecological value of a restoration project or project (s) may be maximized especially where ecological value is rewarded versus simply a cash recovery. Working with experts in NRD, all parties can be involved in more strategic environmental planning that will have the potential to restore an entire habitat, not just a site. This process also allows corporations to discover their assets, in the form of potential DSAYs, and assign real costs associated with restoration projects for these DSAYs. Other PRPs can reap the reward that a larger more ecologically robust project might have by cashing out its injury at a reduced price. In these types of projects a cash value can also be assigned to a DSAY unit in a given settlement and a PRP will have the choice of cash payout or providing restoration. Another plus is that if industry does choose to do its own restoration, it is generally done more quickly, thereby reducing the cost of interim losses.

Resource banking also creates a winning situation for many stakeholders. For the Trustees it reduces the dollars that would otherwise be spent on litigation, because it builds consensus thereby breaking the bottleneck. Of greatest benefit for the Trustees, the habitat is restored more quickly and with greater likelihood of increasing the positive ecological impacts by increasing the restoration area beyond the original area. The process offers benefits to industry by quantifying the liability and making it finite, which is also helpful to shareholders and insurers by the elimination of uncertainty. Not only is restoration

banking usually the most economic solution it is usually the fastest. It can work extremely well for sites with just one PRP but is also very well-suited to complex sites with many PRPs.

The benefits for attorneys are that liability issues can be settled more quickly, in turn benefiting the client. Attorneys need to know the Federal government has been winning its NRD suits against private properties. By working with clients to resolve liability issues quickly and offset future liability, assets remain available that would otherwise not be available. The client is able to manage the project directly with contractors and in many cases derive good public relations through the positive impact on the community from restoration projects. Another reason that the shift to resource banking is effective is the reality, "that often an injured resource cannot be restored and the trustees may seek the cost of acquiring resources having an equivalent value." Working with clients to identify hidden resources that may have equivalent or greater value opens the door to alternatives in dispute resolution.

Just as in any complex negotiations resource banking is not without the potential for problems, just as is true for any complex negotiations. The economics may not be feasible for the site, for example if there is not sufficient ecological impact potential for DSAY credits. Also, changes in circumstances (including leadership or the habitat) could cause costs to escalate or render the restoration plan infeasible.

In general the potential rewards are greater than the potential for problems, and the timing of this concept is especially fortuitous. Why the demand for resource banking at this time? Consider the recent stance towards NRD in the State of New Jersey. As per Policy Directive 2003-07, issued by the State of New Jersey's Department of Environmental Protection on September 24, 2003, "the Assistant Commissioners for Natural and Historic Resources (NHR) and for the Site Remediation Program (SRP) have begun the process of addressing the more than 4,000 potential claims for natural resource damages (NRD)." This relatively small state, in the eighteen months preceding the directive had begun actions on nearly

4,000 potential claims. The state even began using private attorneys working on a contingency fee to pursue these NRD claims. This type of aggressive NRD enforcement has not gone unnoticed and has implications throughout the United States. As part of the language of the directive, “voluntary restoration will be considered in settling claims.”

Strategic environmental planning should be discussed within every corporation throughout the United States. Education and awareness of the alternatives afforded by resource banking are crucial. Resource banking is not just for companies with current liability, the new interpretation of FASB makes it an economic reality for every corporation. Every company is well-served by learning more about resource banking because resource banking can help companies discover potential assets in addition to resolving liability. NRD claims are increasing in frequency and severity and the trend is upward, will your clients be ready?

Preemption and Removal in Toxic Tort Cases

Douglas A. Henderson and Lynette E. Smith
Troutman Sanders LLP

In amending the Clean Air Act in 1990, Congress required the use of reformulated gasoline to improve air quality in certain non-attainment areas throughout the United States. The idea was simple enough. By requiring the addition of certain “oxygenates,” gasoline would burn cleaner, and there would be less air pollution. Although several oxygenates were available under the Clean Air Act, the substance of choice for gasoline producers quickly became MTBE. Among its benefits, MTBE could be added early on in the production process, unlike ethanol, another oxygenate, which had to be added at the pump.

Soon after gasoline producers embraced MTBE as the dominant oxygenate, MTBE went from air quality savior to groundwater menace. The problem with MTBE, was its solubility in water, and in particular its solubility in groundwater after leaking from underground storage tanks. MTBE was soon detected in groundwater through-

out the United States. Few studies documented serious health effects from MTBE exposure, but the distinctive taste and odor of MTBE were enough for many to file suit.

Now banned in several states, MTBE is today at the center of hundreds of lawsuits throughout the United States. At issue in these cases are the standard toxic tort issues-- product liability claims involving personal injury, nuisance and trespass actions alleging property devaluation, and putative class actions seeking medical monitoring and emotional distress. While defendants in these suits usually represent a small set of producers and distributors of MTBE, plaintiffs include states, municipalities, and individuals. Today, MTBE litigation is a cottage industry of its own, with a specialized bar and small circle of experts.

Arguably, however, MTBE differs from the “standard” toxic tort substance of concern in one critical dimension. Although the Clean Air Act Amendments of 1990 did not mandate the use of MTBE by gasoline producers and distributors, the structure of the Clean Air Act, combined with the economics and technical benefits of MTBE production, ultimately pushed MTBE as a preferred oxygenate of choice to improve ambient air quality in the United States. It is this statutory and regulatory pressure fueling MTBE use that colors its place in toxic torts litigation.

Largely because of this unique conception, litigation involving MTBE has pushed and pulled civil procedure in ways previously unknown. The last year has witnessed an unusual stream of MTBE cases addressing fundamental issues in federal jurisdiction, in particular removal jurisdiction and pre-emption. In a set of Multi-District Litigation cases involving MTBE, Judge Shira Sheindlin of the Southern District of New York, a colleague of Senior Judge Jack Weinstein of civil procedure fame, has investigated the MTBE conundrum head on, issuing several key decisions dealing with the role that toxic substances can play in shaping civil procedure. If bencectin is known for its causality case law and asbestos for its class action holdings, MTBE may become known for its effect on removal and preemption jurisprudence.

Preemption as a Basis for Removal to Federal Court

The blackletter law on removal is well known.

Preemption and Removal in Toxic Tort Cases

Continued from page 13

Absent diversity jurisdiction, a case will not be removable to federal court if the complaint does not affirmatively allege a federal cause of action. But there are two general exceptions to this general rule: when federal law preempts an area of state law, and when Congress specifically provides for removal to federal court. If federal law preempts an issue, then the matter may be heard in federal court, if certain conditions are met, and it means certain state common law—and perhaps state statutory—claims may be unavailable for plaintiffs. For virtually all lawsuits involving toxic substances, preemption is at the top of the key defense strategies.

Given the backdrop of the Clean Air Act Amendments, preemption claims have been a favorite of defendants in MTBE lawsuits, both as a way to end up in federal court and as a way to completely preempt state common law causes of action. In the context of MTBE, the preemption issue arises in two general contexts: first, does the framework set up by the Clean Air Act which encouraged the use of MTBE preempt recent state MTBE bans arising throughout the United States, and, second, does this very same framework preempt state common law claims involving MBTE?

Clean Air Act Preemption of State Common Law Claims

Only a few courts have addressed whether the Clean Air Act preempts state common law claims. The most recent—and the most important—of these are several MTBE MDL decisions in the Southern District of New York. In a series of well researched decisions, Judge Scheindlin considered whether the Clean Air Act's implied preference for MTBE amounts to preemption, and thus supports removal to federal court. In addressing the preemption argument, Judge Scheindlin surveyed the legal landscape of preemption, summarizing the three types of preemption—express, implied or field preemption, and conflict preemption. Defendants contended plaintiffs' numerous state law claims were expressly and conflict preempted.

As for express preemption, Judge Scheindlin noted that, absent some clear and manifest direction of Congress,

there would be no preemption, especially for matters dealing with the traditional police powers of a state, such as environmental protection or health and safety. But in the case of the Clean Air Act, Judge Scheindlin held, the express preemption argument fell short as a matter of law. Specifically, because the plaintiffs brought their claims to protect groundwater quality, and not to protect air quality, and especially not to address fuels or fuel additives, their claims were not preempted. The saving clause in the Clean Air Act likewise supported this view, the Court held, because it clearly permitted “relief” under any statute of common law.

The court then turned to the conflict preemption argument. To find a claim was conflict preempted, a court is required to determine whether it would be impossible for the defendants to comply both with the state law and federal law, or whether state law would provide an obstacle to the achievement and execution of the Clean Air Act. Defendants, in their main argument, claimed that finding them liable for using MTBE, one of the limited number of “federally approved” oxygenates, would present an obstacle to the achievement of the federal objectives of the Clean Air Act and the reformulated gasoline program. Defendants further argued that at this time there are no “practicable” alternatives to MTBE sufficient to satisfy the oxygenate requirements of the reformulated program. In this discussion, Judge Scheindlin rejected the conflict preemption argument.

In a subsequent opinion two years later, Judge Scheindlin reexamined the preemption argument following defendants' renewed plea for reconsideration. At this point, defendants argued that plaintiffs' claims are completely preempted because EPA regulations governing reformulated gasoline content and the “anti-dumping” rules, which required gasoline to remain at its current quality after the reformulated gasoline program took effect, have preemptive force, even if the Clean Air Act does not displace state law specifically. In making this argument, defendants alleged that, if plaintiffs were successful, defendants would be barred from using MTBE because it would be classified as a defective product, based, in part, on its discharge into the air when gasoline is combusted.

Defendants maintained that federal law provided the exclusive remedy to deal with MTBE, namely, through the regulatory process.

For these questions, the issue was whether EPA meant to preempt state law claims based on groundwater contamination and, if so, whether EPA was acting within its scope of delegated authority. After scrutinizing a number of Federal Register interpretations, the Court concluded EPA did not intend to preempt state common law claims, only those claims involving “motor vehicle control.” Similarly, through its anti-dumping rules, EPA only intended to preempt the field of conventional gasoline content to the extent pollutant emissions could become worse as a result of the reformulated gasoline program. But more important than EPA’s interpretation was the fact that EPA did not have the authority to preempt the field of fuel content for all purposes. According to the court, “logic would dictate that EPA would only have the power to preempt areas of state law over which the agency itself has regulatory authority.” In its savings clause, Judge Scheindlin concluded, the Clean Air Act assumes there are some common law actions left to save. The savings clause, in other words, reflects a Congressional determination that occasional non-uniformity was acceptable to promote the public health and welfare.

In their final argument, Defendants maintained that plaintiffs’ claims were preempted because MTBE is emitted from car tailpipes and falls back to earth as rain throughout the United States. Rejecting this argument, the court held finally that plaintiffs’ claims were preempted only if they would impose a state law regulation of gasoline for emissions purposes. Because the state tort claims are principally aimed at regulating certain behaviors by defendants, rather than the control of fuel itself, they were not preempted. Accordingly, plaintiffs could sue the defendants on state common law claims despite the framework set up by the Clean Air Act Amendments to rely on MTBE as a preferred oxygenate.

Clean Air Act Preemption of State MTBE Bans

As true for preemption of state common law claims, the case law on preemption of state MTBE

prohibitions is likewise limited. Last year, however, the United States Court of Appeals for the Ninth Circuit addressed whether the State of California’s ban on MTBE was preempted by the Clean Air Act, which specifically permits gasoline producers to use MTBE as a oxygenate to improve air quality in non-attainment areas. In *Oxygenated Fuels Association, Inc. v. Davis*, the Ninth Circuit addressed whether the Clean Air Act permitted California to ban MBTE.

After reviewing preemption generally, the court addressed express preemption—namely, whether anything in the Clean Air Act preempted California’s ban. To answer this question, the court turned to the statutory language. Under the Clean Air Act, no state is permitted to enforce, for purposes of motor vehicle emissions control, any control or prohibition on any fuel or fuel additive. 42 U.S.C. 7545(c)(4)(A). Defendants argued, however, that the Clean Air Act specifically exempted California from this section, pointing to 42 U.S.C. 7545 (c)(4)(B), which provided that California may “prescribe and enforce, for the purpose of motor vehicle emission control, a control or prohibition respecting any fuel or fuel additive.”

In response, plaintiffs argued the MTBE ban was not for “the purpose of motor vehicle emission control,” but for groundwater protection. Framing the relevant question as the MTBE ban itself, and not California’s emissions regulatory framework, the court noted that, on a motion to dismiss, the ban did not fall within the exemption from preemption set aside for California. Its reading of “for purposes of motor vehicle emissions,” the Court noted, was in line with those of other courts on this point. A ban to stop groundwater contamination was not a ban on MTBE as a fuel or fuel additive, and the matter was largely that simply.

The Ninth Circuit then turned to the more difficult question, whether California’s MTBE ban was “conflict” preempted by the Clean Air Act. Plaintiffs claimed the California MTBE ban conflicted with the goals of the Clean Air Act, citing two reasons. Plaintiffs claimed, first, that, in enacting the Clean Air Act, Congress intended to give gasoline producers an unrestricted choice

Preemption and Removal in Toxic Tort Cases

Continued from page 15

among oxygenate fuel additives, and, second, Congress meant to ensure an adequate and reasonably priced supply of oxygenated gasoline, and the California MTBE ban would substantially disrupt the gasoline market and cause an increase in prices.

Addressing these argument in turn, the Ninth Circuit reviewed the statutory language and legislative history of the Act, finding that neither suggested that Congress required producers to chose MTBE as the oxygenate of choice. In addressing this argument, the Ninth Circuit rejected it quickly, referring to its holding in *Exxon Mobile Corp. v. EPA*, a challenge to Nevada’s plan to “require 3.5 percent minimum oxygen content for wintertime gasoline,” which, because MTBE may not be blended in gasoline at concentrations greater than 2.7 percent, effectively banned the use of MTBE in Nevada. From its analysis in this case, the Ninth Circuit could find no evidence the Clean Air Act was intended to give gasoline producers a comparable choice of oxygenates. In other words, the State’s MTBE ban was not preempted for this reason.

Turning to the second argument put forth by plaintiffs, the Court looked at the effect California’s MTBE ban would have on the market for gasoline. Here the court addressed the larger preemption issues involved—even though the Clean Air Act and the MTBE ban operate in different areas, one protects air and the other protects water, the Court had to decide whether the effects of the latter interfere with the goals of the former. Questioning whether one of the goals of the Clean Air Act is a smoothly functioning gasoline market, the Court turned to the fundamental presumption of preemption analysis, that Congress did not intend to preempt areas of law that fall within the traditional exercise of the police powers of the state. According to the Ninth Circuit, only where there is “clear evidence” that Congress meant to assert federal control should there be conflict preemption. Finding none, the Court held that California’s MTBE ban was not preempted, either expressly or impliedly.

On a similar tract to the Ninth Circuit, the United States District Court for Northern District of New York addressed a similar question, whether a state MTBE ban, in

this case, the New York MTBE ban, was conflict preempted by the Clean Air Act. After reviewing preemption law in detail, the Court found the ban not expressly or impliedly preempted by federal law. The court was unable, however, to determine on summary judgment whether the ban was conflict preempted by the Clean Air Act, a question that required a bench trial.

Unlike the Ninth Circuit, which suggested the Clean Air Act was not concerned with the impact oxygenates would have on gasoline supplies and related issues, in *Pataki* the Northern District of New York considered whether and to what extent the state MTBE ban would affect gasoline supplies and air quality in New York. Numerous witnesses testified for the plaintiffs on these issues. One expert testified that, without MTBE, ethanol-blended gasoline in New York would worsen air quality emissions. Another expert testified for plaintiffs that the use of ethanol over MTBE would cause increased emissions of ozone precursors, and still another expert testified that MTBE ban would lead to gasoline shortfalls and price increases in New York. Rejecting all of these witnesses as unreliable, the Court found the MTBE ban did not frustrate the Clean Air Act. It was, the *Pataki* Court concluded, the prerogative of the State to protect groundwater, the main goal of the MTBE ban, and this was a power reserved to the State.

Federal Agent Removal

In a claim more unique than pre-emption, defendants argued the MTBE cases should be in federal court based on “federal agent” jurisdiction. Under 28 U.S.C 1442(a), a civil action commenced in State court against “any officer” of the United States may be removed to federal court. In short, this is yet another exception to the well pleaded complaint rule—Congress provided that federal agents may remove a case to federal court, despite the absence of any federal cause of action. Under this provision, a private party may remove a state court action if (1) it acted under the directive of a federal agency or officer; (2) it has a colorable federal defense, and (3) there is a causal nexus between the federal direction and the conduct in question.

Here, given the 1990 Clean Air Act Amendments and EPA's guidance to use MTBE, defendants argued they should be in federal court on the basis of federal agent jurisdiction. According to defendants, although the EPA identified seven additives, MTBE is the only approved oxygenate that is available in quantities sufficient to comply with the Act and regulations. At the time of the 1990 Amendments, both Congress and EPA were aware that defendants would have to use MTBE to comply with the Act's requirements.

For Judge Scheindlin, the case law and the policies underlying the federal agent provision supported removal. As for the federal defense required for federal agent removal, the court pointed to preemption, noting that the defense was "colorable" for purposes of removal, and that was all that was necessary to effect removal. In response to plaintiffs' claim they resided in attainment areas not encompassed by the oxygenated fuel mandates of the 1990 Clean Air Act Amendments, Judge Scheindlin clarified the federal agent removal provision in the context of the Clean Air Act in a subsequent order. Plaintiffs claimed the use of oxygenated fuels in these areas was completely voluntary. Defendants countered these arguments with two points. First, the act required reformulated gasoline and conventional gasoline be classified as gasoline, and, second, reformulated gasoline is sometimes delivered and sold in non-reformulated fuel areas and the fuel distribution networks do not coincide.

The court rejected the first argument, noting that the defendants had a choice in not blending the reformulated gasoline with conventional gasoline. But the second argument proved a winner for the Court. For Judge Scheindlin, it was critical to the federal agent removal issue that EPA knew reformulated gasoline would spill over into areas where it was not required. Congress was also aware that some producers and distributors would need to direct at least some MTBE to non-reformulated gasoline states. For the defendants in "spill-over" states, removal to federal court under the federal agent provision was proper. Conversely, federal officer removal is not available if the plaintiff is located in an area where the sale of reformulated gasoline is not required by the Clean Air

Act Amendments and where there is no reasonable basis to anticipate the spillover of reformulated gasoline from an adjacent non-attainment area.

The Intertwined Preemption/Removal Issue

Further confusing matters, plaintiffs in the MTBE MDL litigation argued that "preemption" was not a sufficient federal defense for purposes of the federal agent removal statute. For Judge Scheindlin, the issue was whether the preemption defense was "federal" enough for purposes of the federal officer removal statute. As a general rule, in considering whether a claim arises under federal law, courts follow the "well-pleaded complaint rule," which essentially requires the court to look only at the allegations, and not the defenses, in complaint. But the two exceptions to this rule were at issue in this case, where a federal statute displaces the state cause of action and where Congress specifically gives federal courts jurisdiction over a particular subject. Still, under the federal officer removal statute, a defendant must have a "colorable" federal defense. The plaintiffs noted that state courts regularly determine federal preemption defenses, which are not normally removable. Rejecting this claim, the court noted that when a party is an entity that has acted under the direction of a federal officer, it is logical to recognize other federal defenses because the situation may not fit the historical model. It was appropriate for defendants to permit defendants to remove their defenses to federal court.

Bankruptcy Removal

In the MBTE MDL litigation, defendants alleged yet another basis of federal court jurisdiction given Texaco's bankruptcy (the predecessor in interest to defendant ChevronTexaco) in April 1987 after it lost a massive case to Pennzoil. Defendants alleged federal court jurisdiction because plaintiffs were asserting pre-petition claims that threatened Texaco's discharge in bankruptcy court. Plaintiffs countered they had no claim when Texaco's bankruptcy was concluded.

Accepting defendants' bankruptcy arguments, the court noted that several acts alleged by defendants involved

Preemption and Removal in Toxic Tort Cases

Continued from page 17

actions prior the bankruptcy. The court had bankruptcy jurisdiction over these claims because questions concerning when certain “claims” arose and whether those claims were discharged involved enforcement and construction of the bankruptcy discharge injunction. Having reached this conclusion, the court declined to abstain the bankruptcy jurisdiction, noting that if it did abstain, it would waste judicial resources and result in the risk of inconsistent judgments. Noting that it had federal agent jurisdiction over 40 MTBE cases (including those in the “spill-over” states discussed above), the court exercised bankruptcy jurisdiction to bring the remaining cases into federal court. In addition, the court noted, plaintiffs right to a jury trial would not be affected if they were adjudicated in federal court. More importantly for the court, because of plaintiffs’ theories of collective liability caused the defendants to be inextricably intertwined, they will all stand or fall together, and federal court was an appropriate forum for this to occur.

Sovereign Immunity

Another procedural issue surfacing in the MTBE MDL litigation has been sovereign immunity. Notwithstanding the federal question jurisdiction for the MTBE MDL litigation, New Hampshire and California moved to remand the MTBE MDL cases back to state court based on state sovereign immunity. For the Southern District of New York, the question was whether principles of sovereign immunity are violated when a state plaintiff voluntarily prosecutes a claim and its case is removed from state to federal court without its consent.

In raising this issue, the state plaintiffs argued federal officer removal cannot trump sovereign immunity, noting that the Supreme Court established a presumption against proceedings in federal court. Defendants counter that Congress created federal officer removal to protect the supremacy of federal law and the sovereignty of the federal government against intrusion by the states. They argued the Eleventh Amendment does not bar removal, but only prohibits lawsuits against the states—i.e., the immunity only applies when a state is a defendant. Reviewing the common law origins of sovereign immunity and the issues

of federalism involved in the MTBE cases, the Court held that, with few exceptions, sovereign immunity does not prohibit the removal of state-initiated actions to federal courts without the state’s consent. Moreover, the court noted, when a state is a defendant, it may have greater interest in having its case litigated in its own courts because a judgment could impact the state treasury or public administration. In addition, remanding the cases to state court would improperly shift the balance toward the states because it would permit them to achieve unfair tactical advantage at the expense of the people. The motion for remand was thus denied.

Conclusion

Judging by the recent case law addressing MTBE procedure, the shadow of the 1990 Clean Air Act Amendments provides no cover for MTBE defendants procedurally in toxic tort lawsuits. The irony of MTBE procedure cannot be overlooked. The MTBE cases were largely removable to federal court because of the Clean Air Act framework, but many of the claims involving MTBE were not preempted by the very same Act. For defendants, the rule is straightforward. It may be possible to litigate MTBE disputes in federal court, but the truly challenging tough state law claims still remain.

Environmental Law Section Officers

Chair

David M. Meezan
Alston & Bird LLP
1201 W. Peachtree Street
Atlanta, GA 30309
404-881-7000 (phone)
404-881-7777 (fax)
dmeezan@alston.com

Chair-Elect

Andrea L. Rimer
Troutman Sanders LLP
600 Peachtree Street, N.E., Suite 5200
Alanta, GA 30308
404-885-3000 (phone)
404-962-6669 (fax)
andrea.rimer@troutmansanders.com

Secretary

Martin A. Shelton
Stack & Associates
260 Peachtree Street, Suite 1200
Alanta, GA 30303
404-525-9205 (phone)
404-522-0275 (fax)
mshelton@stack-envirolaw.com

Treasurer

William W. Sapp
Environmental Protection Agency
61 Forsyth St.
Atlanta, GA 30303
sapp.bill@epamail.epa.gov
404-652-9545 (phone)

Member-at-Large

Ann Marie Stack
Bouhan, Williams & Levy, LLP
P.O. Box 2139
Savannah, GA 31402-2139
912-236-2419 (phone)
912-233-0811 (fax)
amstack@bouhan.com

State Bar of Georgia
104 Marietta Street, NW
Suite 100
Atlanta, Georgia 30303

NON-PROFIT ORG
US POSTAGE
PAID
ATLANTA, GA
PERMIT NO 1447