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Corporate Marketing as “Carbon Neutral” Legal Issues

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To anyone surfing the internet on environmental topics, climate change is perhaps -- rather appropriately -- the hot issue. It has been the subject of ongoing scientific discussion and the focus of international treaties, foreign and state legislation and national legislation and legislative proposals, voluntary standards established by non-governmental organizations (NGOs), and corporate programs, focusing on the control of greenhouse gases (GHGs), especially carbon dioxide -- sometimes referred to by the shorthand term, “carbon.” The focus of this paper is on liabilities to which corporations that develop these types of programs may be exposed by virtue of their marketing claims, and in particular their assertions of carbon reductions or carbon neutrality.¹ This paper provides background information on cap-and-trade programs, which create marketable emissions reductions or credits, and then discusses the various bases for liability for inaccurate representations concerning these credits, including claims of being carbon neutral.

Background

In the 1970s, Congress enacted a series of regulatory statutes dealing with air, water, and solid waste pollution, which relied on a model of command and control and which included, among others, the Clean Air Act, amended in 1970 and 1977,² the Clean Water Act, amended in 1972 and 1977,³ and the Resource Conservation and Recovery Act, enacted in 1976.⁴ Under each of these statutes, the federal government, through the United States Environmental Protection Agency (EPA), established guidelines for pollution control programs for which states could assume responsibility. These programs relied on agency rulemaking, to establish general requirements, and permitting, to establish site-specific, tailored requirements.

In the mid-1970s, EPA established a new market-based emission control program under the Clean Air Act to allow sources to locate in areas with poor air quality without causing additional air quality problems. New and modified sources were required to offset their emissions by

¹ For a discussion of the broader topic of corporate sustainability, of which carbon neutral marketing may be a component, see “Corporate Sustainability and Social Responsibility: A Legal Perspective,” J. Civins and M. Mendoza, Texas Bar Journal (May 2008)

² 42 U.S.C. §§ 7401 et. seq.

³ 33 U.S.C. §§ 1251 et. seq.

⁴ 42 U.S.C. §§ 6901 et. seq.

acquiring reductions or emission credits from other sources. For an emission reduction credit to be transferable, it was required to be “additional,” *i.e.*, not required by regulation, as well as enforceable, permanent, and quantifiable. In 1979, EPA established a cap and internal trade emission control program -- the “bubble” policy. This policy allowed individual sources to meet emission limitations by applying a single aggregate emission limit to multiple sources within a facility rather than individual requirements to each source.

Both the emission offsets and bubble programs were regulatory add-ons to existing programs, which sought to reduce emissions attributable to individual facilities. Reductions in overall emissions were the subject of comprehensive state implementation plans or SIPs.

Establishment of Cap-and-Trade Programs

In 1990, Congress enacted the first in a series of statutory emission trading programs labeled “cap and trade,” the SO₂ Allowance Trading Program, commonly known as the Acid Rain Program. EPA has promulgated rules implementing this program, which has been working and working well. EPA more recently has promulgated rules for two other cap-and-trade programs -- the Clean Air Interstate Rule (CAIR), which deals with NO_x and SO₂, and the Clean Air Mercury Rule (CAMR), which recently was struck down by the D.C. Circuit Court because it was created after EPA delisted mercury as a hazardous air pollutant without having met the statutory requirements for delisting.⁵ Other, regional cap-and-trade programs, not directly related to GHGs, also have sprung up, including: the Regional Clear Air Incentives Market (RECLAIM) in Southern California, the Ozone Transport Commission (OTC), and the Regional NO_x Trading Program in the Northeastern United States or NO_x Budget Trading Program. Additionally states, including Texas, have established cap-and-trade programs, including ones designed to address exceedances of national ambient air quality standards (NAAQs).

Basic Aspects of Cap-and-Trade Programs

An EPA document entitled “Tools of the Trade: A Guide to Designing and Operating a Cap and Trade Program for Pollution Control (the “Guide”)⁶ provides a useful discussion of the mechanics and intricacies of these market driven programs. As the Guide explains, under cap-and-trade programs, the regulatory authority sets a cap on total mass emissions for a group of sources for a fixed compliance period, *e.g.*, 1 year. The authority then divides the cap into allowances, each representing an authorization to emit a specific quantity of the pollutants, *e.g.*, 1 ton of SO₂, which are then distributed among the various sources in the group. For the compliance period, each source must measure and report its emissions of that pollutant, at the end of which the sources must surrender their allowances to cover the quantity of the pollutants they emitted. If a source does not have sufficient allowances to cover its emissions, the authority penalizes it, usually by reducing the number of allowances the source will receive in future years.

⁵ *New Jersey v. EPA*, No. 05-1097 (D.C. Cir. Feb. 8, 2008)

⁶ A Guide to Designing and Operating a Cap and Trade Program for Pollution Control, EPA 430-B-03-002, www.epa.gov/airmarkets June 2003.

The Guide asserts a cap-and-trade program provides a number of benefits over a program of command-and-control. For example, there is greater certainty as to what the total emissions of the subject pollutants are likely to be because the authority sets the total maximum allowable amount that sources can emit.⁷ Additionally, because of the economic value of allowances, sources are encouraged to decrease their emissions and either sell the difference, to obtain an economic benefit, or bank it, to obtain future flexibility regarding the timing and location of emission reductions.⁸ A cap-and-trade program also results in improved consistency and accountability: each source is required to follow protocols to ensure completeness, accuracy, consistency of emission measurement and timeliness of reporting.⁹ The authority then can compile and make public available the reported information, promoting transparency.

According to the Guide, a key advantage of cap-and-trade programs is that they give sources the flexibility as to how best to achieve their emission targets, *e.g.*, through onsite implementation of capital or operating measures, such as installation of abatement equipment or energy efficiency measures, switching fuels, and shutdown or reduction in output from higher emitting sources, or through purchasing allowances from others, at costs lower than might be necessary to implement onsite measures. New sources may have to acquire allowances from existing ones, as under non-attainment and PSD emission offsets programs.¹⁰ The bottom line is that the program creates incentives for sources to find ways to reduce their emissions of the subject pollutant.

Alternatives to Cap-and-Trade Programs

The Guide recognizes that there are other programs besides command-and-control and cap-and-trade that regulatory policy makers may wish to consider. These approaches include environmental taxes, emissions trading, which may be project-based or rate-based, and voluntary agreements and eco-labeling. Environmental taxes make it less attractive to maintain high levels of emissions, but do not impose an absolute cap.¹¹ According to EPA, emission trading, both project-based and rate-based, also have shortcomings.

Project-based trading, also known as credit or offset trading, generally is used in conjunction with a regulatory program to allow sources the ability to acquire offsets from sectors not in the regulatory program, *e.g.*, CO₂ offsets to be obtained from a project to protect a forest slated for de-forestation.¹² Emission offsets or credits are typically calculated by comparing actual emissions against a baseline. A key challenge for such programs is establishing the baseline and insuring that emission reductions are real and not theoretical. Another challenge is embodied in the concept of “additionality,” being sure the reductions would not have occurred anyway. Another concern relates to the permanence of the credits, *e.g.*, if a saved forestry project years later is allowed to be de-forested.

⁷ Guide at p. 1-3.

⁸ Guide at p. 2-4.

⁹ Guide at p. 2-4.

¹⁰ Guide at p. 2-5.

¹¹ Guide at p. 2-5.

¹² Guide at p. 2-7.

A key difference between project-based trading and cap-and-trade relates to the development of a baseline and the tracking of the offsets. In a cap-and-trade program, the universe of activities that need to be examined is relatively confined -- to the specific sources in the program. In a project-based program, other, more difficult to identify-and-track sources such as forests must be examined and kept track of, to insure the integrity of the program, resulting in higher administration and transaction costs.

Under rate-based trading, the authority sets a performance standard, *e.g.*, tons of pollutant per KW of electricity generated, and sources performing at higher efficiencies can earn credits and those at lower efficiencies must obtain additional ones.¹³ Rate-based trading programs have been used to phase out lead in gasoline and to control mobile source emissions. A key concern with such programs is that overall emissions not increase with an increase in number of sources or source outputs. To address this concern, the authority must periodically impose new rate standards to achieve and maintain an emission target.

Status of GHG Cap-and-Trade Programs

In 2005, the 1997 Kyoto Protocol came into force, binding nations to a cap-and-trade system, based on the US's Acid Rain Program, for the six major GHGs. Under the treaty, emission quotas were assigned to each participating country, with the goal of reducing their overall emissions to 1990 levels by the end of 2012. The United States participated in the development of the Kyoto Protocol, particularly pushing the cap-and-trade program, but ultimately chose not to implement the protocol and presently is the only developed nation not to have signed.

The goal of carbon trading generally is "to allow the market to put a price tag on GHG emissions, thus allowing companies to buy and sell them to offset their emissions and meet emissions caps established in developed companies."¹⁴ Developed countries may sponsor carbon projects that provide a reduction in greenhouse gas emissions in other countries as a way of generating tradable carbon credits. The signatories to the protocol, including the European Union, have begun implementing greenhouse gas cap-and-trade programs. The European Union Emission Trading Scheme or EU ETS is the largest multi-national, greenhouse gas emissions trading scheme in the world and is currently the world's only mandatory carbon trading program. Presently 25 of 27 member states are participating in the first phase of the program.

Not only has the United States not implemented the Kyoto Protocol, up until the recent U.S. Supreme Court decision of *Massachusetts v. EPA*, 127 S.Ct. 1438 (2007), EPA had taken the position that GHGs are not a pollutant subject to regulation. In *Massachusetts v. EPA*, the Supreme Court declared that GHGs are pollutants and that EPA has the authority to regulate the emission of greenhouse gases from new motor vehicles. The Court directed the agency to determine if sufficient information exists for it to make the necessary endangerment finding to trigger regulation. Although the EPA has yet to act, the conventional wisdom is that EPA will be forced to regulate greenhouse gases, not only from new motor vehicles, but more broadly as pollutants under the Clean Air Act, although federal GHG legislative initiatives may overtake it. There are numerous GHG bills pending in Congress, and all three major presidential candidates

¹³ Guide at p. 2-9.

¹⁴ State of Green Business 2008, Greenbiz.com (GreenBiz Report) at p. 22.

are on record supporting greenhouse gas reduction legislation. And on April 14, 2008, President Bush announced that he wants to develop a national plan to combat global warming and laid out principles for that plan.¹⁵ The Consolidated Appropriations Act, 2008 does contain requirements for EPA to establish mandatory GHG reporting requirements.

In the absence of federal GHG legislation, states, individually and in conjunction with other states in a region, have developed a range of programs to address GHG emissions. Regional programs with cap-and-trade mechanisms include the Regional Greenhouse Gas Initiative (RGGI), the Western Climate Initiative, and the Midwestern Regional GHG Reduction Accord. State programs range from taxation to goal setting to actually imposing CO₂ caps on particular industrial sectors. California sought to develop GHG emission standards for motor vehicles, based on the waiver from preemption of Section 177 of the Clean Air Act, and 14 states chose to follow suit. But EPA denied California's petition. California filed an appeal in the Ninth Circuit challenging that denial.

Interestingly, although there is no mandated U.S. program, more than thirty prominent corporations have joined with a coalition of environmental groups to form the United States Climate Action Partnership, which has urged the federal government to adopt a strong national policy to reduce US GHG emissions, including a mandatory cap-and-trade program.¹⁶ Combat Climate Change, a coalition of 46 international companies, has pushed countries to join together for action climate change. In the meantime, voluntary GHG emissions trading programs have arisen and emission credits are being bought and sold on markets such as the Chicago Climate Exchange, self-described as "North America's only and the world's first global marketplace for integrating voluntary legally binding emissions reductions with emissions trading and offsets [worldwide] for all six greenhouse gases." The Exchange boasts more than 350 members.¹⁷

In addition to the creation of a carbon market, climate change regulatory programs and voluntary initiatives are forming the basis for commercial marketing efforts and various corporate disclosures. Two commentators have observed:

Products providing a rational economic contribution to climate change problems are gaining momentum. Eco-friendly products and climate change thematic indices are being launched by financial institutions keen to take advantage of growth in this market.¹⁸

GreenBiz.com, an online information resource on how to align environmental responsibility with business success, issued a report entitled, "State of Green Business 2008." In it, GreenBiz notes that "[t]he green marketplace roared back to life [this past year], as products making environmental claims became more prevalent, including some from bigger companies" such as Philips Electronics, Procter & Gamble, REI, Wal-Mart, Whole Foods, and Home Depot.¹⁹ And, many companies, they announced, not only were thinking about climate change, but also were

¹⁵ <http://www.washingtontimes.com/apps/pbcs/dll/article?A1D=120080414/NATION/676175489/1001>.

¹⁶ See Ceres Petition at p. 27.

¹⁷ GreenBiz Report at p. 22.

¹⁸ "Green Structured Products are Likely to Proliferate," Ed Parker & Nicole Purin, Financial News, December 3, 2007.

¹⁹ GreenBiz Report at p. 7.

anxious to make public commitments: Nike said it would be a climate-neutral company by 2011; and “Green Mountain Power announced that it already was nearing zero-carbon status, with just 2 percent of its fuel mix for 2006 coming from carbon dioxide-emitting sources, compared to 70 percent for U.S. utilities overall.”²⁰ GreenBiz states companies were not merely competing against others, they were outdoing themselves: Xerox announced that it had met its goal of reducing its GHG emissions by 10% by 2012 with an 18% reduction in 2006, compared to 2002. And companies also focused on carbon footprints of specific products and processes, for example, Dole Food Co. announced plans to make its banana and pineapple supply chain carbon neutral, working with Costa Rica’s National Forestry Financing Fund to neutralize emissions from its operations.²¹

In addition to pressing for mandatory GHG programs, NGOs, including the Climate Group, the International Emissions Trading Association, and the World Business Council for Sustainable Development launched a new global carbon-offset standard at the London Stock Exchange to increase participation in the global voluntary carbon market. And two companies, AES Corp. and GE Energy Financial Services, partnered to develop GHG emission-reduction projects in the U.S, which will form the basis for a credit card that will reward holders with offsets based on purchases.²²

Disclosure Liabilities

As a practical matter, the calculation of CO₂ emissions from power plants and other heavy industrial activities is relatively straightforward, but, in the absence of a federal regulatory program, the calculation and verification of CO₂ offsets involves a number of uncertainties. And there also are significant uncertainties associated with accounting for carbon involved in the production and distribution of products and in business activities, *e.g.*, transportation, as well as in obtaining and verifying offsets.

Because of the uncertainties associated with accounting for carbon credits, corporations, in disclosing carbon-related information to investors and others, in their SEC filings or stand-alone sustainability reports, or to consumers, in marketing and advertising, may be exposed to liability if their claims or the underlying facts upon which they are based are found to be misleading and untrue, perhaps even if they exercised due care. These disclosure-based liabilities may arise under state deceptive practice statutes and the common law, in climate change litigation, under the Federal Trade Commission Act, under securities law, and possibly under developing GHG-specific programs. Although not strictly speaking a liability, significant reputational “liability” also may arise from inaccurate green disclosures.

State Deceptive Practice Statutes/Common Law Disclosure Liabilities

Regardless of whether the focus of a corporation’s green marketing campaign is on its investors, its consumers, or other stakeholders, the company faces the potential for liability under both common law and fraud-based statutes for statements that prove to be untrue. A key case cited

²⁰ GreenBiz Report at p. 4.

²¹ GreenBiz Report at pp. 4-5.

²² GreenBiz Report at p. 5.

for this proposition is *Nike v. Kasky*,²³ a case that settled after the California Supreme Court ruled against Nike on a matter of law and the U.S. Supreme Court dismissed as improvidently granted a petition for certiorari.

As the U.S. Supreme Court explains, beginning in 1996, Nike was besieged with a series of allegations that it was mistreating and underpaying workers at foreign facilities. In response, Nike sent out press releases and letters to newspaper editors and asked former UN Ambassador Andrew Young to prepare a report on labor conditions at its facilities. In 1998, Kasky sued Nike for unfair and deceptive practice under two California statutes, asserting Nike had made false statements and/or material omissions of fact concerning working conditions at its manufacturing facilities. Kasky brought his suit on behalf the general public and the State of California.

In response, Nike filed a demurrer, contending that Kasky's suit was absolutely barred by the First Amendment. The trial and appellate courts sustained Nike's demurrer, the appellate court explaining that Nike's statements formed "a part of a public dialogue on a matter of public concern within the core area of expression protected by the First Amendment." The California Supreme Court disagreed.

In reversing and remanding for further proceedings, the court held:

[b]ecause the messages . . . were directed by a commercial speaker to a commercial audience, and because they made representations of fact about the speaker's own business operations for the purpose of promoting sales of its products, . . . [the] messages are commercial speech.

27 Cal. 4th 939, 946, 45 P.3d 243, 247 (2002). The court did not reach the underlying issue of whether Nike's representations were false.

The two issues the Supreme Court was about to take on, before it decided to dismiss the writ, were:

- (1) whether a corporation participating in a public debate may "be subjected to liability for factual inaccuracies on the theory that its statements are 'commercial speech' because they may affect consumers' opinions about the business as a good corporate citizen and thereby affect their purchasing decisions"; and
- (2) even assuming [that to be the case], whether the "First Amendment as applied to the states through the Fourteenth . . . permit[s] subjecting speakers to the [state] legal regime . . .

The court dismissed the petition as improvidently granted based on finality, standing, and ripeness. Although the case settled before trial, it illustrates the potential for liability to which a corporation may be exposed for false and misleading statements regarding green claims generally and for carbon neutral claims in particular.

²³ *Nike v. Kasky*, 27 Cal.4th 939 (2002), cert. dismissed, 539 U.S. 654 (2003).

A key issue likely to arise relates to the state of mind necessary to give rise to liability, *e.g.*, knowing versus negligent dissemination of false information. If the standard is negligence, then the pertinent inquiry is whether, before making a representation as to being carbon neutral, a corporation is under an obligation to determine if the underlying facts upon which it relies for its claim are correct, that is, whether it needs to independently evaluate the assumptions and methodology of its carbon credit provider, assuming it purchases credits, or of its own professionals, if the company is relying on reductions it itself creates.

Litigation Liabilities

Green disclosures regarding climate change, as well as the failure to make such disclosures, may be used in nuisance suits filed by plaintiffs alleging damages from global warming. In *Native Village of Kivalina v. ExxonMobil Corporation*,²⁴ a native village brought a public nuisance suit against various energy companies for damages to the village caused by global warming. Plaintiffs asserted, on the one hand, that one defendant's statement--that there is an emerging consensus that climate change is, at least in part, linked to the production and consumption of carbon based fuels--constituted an admission. Plaintiffs asserted, on the other hand, that another defendant's statements "downplay[ing] the severity of global climate change" were intended to mislead and were elements in a conspiracy. The petition in the *Kivalina* litigation suggests that a corporation may be damned if it admits its activities may contribute to global warming and damned if it denies it.

FTC Disclosure Liabilities

In its announcement of a January 2008 public workshop on whether the agency should update its "Green Guides" to address advertising claims relating to the emerging market for carbon offsets, *i.e.*, GHG emission reduction products and renewable energy certificates or RECs, the Federal Trade Commission (FTC) provided an overview of the market for sale of carbon offsets, describing the products as well as the current regulatory framework.²⁵ The FTC explained that carbon offsets are credits or certificates that represent the right to claim responsibility for GHG emission reductions. By acquiring these credits, purchasers seek to reduce their "carbon footprints" and possibly to become "carbon neutral."²⁶ So for example, an airline passenger may pay a fee equal to the percent of the carbon emitted by the fuel burned by the plane during that person's trip, which the airline uses to buy an equivalent amount of carbon in RECs.

Retail electric customers have two particular options: they may buy either renewable energy, where it is available, paying a premium, or RECs, from generators who do have available renewable energy sources, selling the difference in value; under that approach, one REC represents the right to describe one megawatt of electricity as renewable. Some states require electricity providers to purchase a minimum percent of their electricity from renewable sources and allow providers to satisfy this requirement through the purchase of RECs. Because the sale of RECs does involve some state oversight, the FTC focused on marketing in the voluntary market. In the

²⁴ No. CV 08-1138 (N.D. CA. 2008)

²⁵ Hereafter, the notice is referred to as the "FTC Notice."

²⁶ FTC Notice at p. 5.

voluntary market, marketers and purchasers of carbon credits must rely, if at all, on voluntary third-party certification programs.²⁷

The basic liability under the Federal Trade Commission Act (FTC Act) arises from the general prohibition against unfair and deceptive trade practices. 15 U.S.C. § 45. The FTC has determined that “a representation, omission, or practice is deceptive if it is likely to mislead consumers acting reasonably in the circumstances and is material.”²⁸ “An act or practice is unfair if the injury it causes, or is likely to cause, is substantial, not outweighed by other benefits, and not reasonably avoidable.” 15 U.S.C. §51(n). Sanctions under the FTC Act for dissemination of false advertisements, which are proscribed by 15 U.S.C. § 52, include civil penalties, 15 U.S.C. § 45, injunctive relief, 15 U.S.C. § 53 and criminal penalties. 15 U.S.C. § 52. The FTC, working with state agencies, routinely seeks restitution.

The FTC explains that, under the FTC Act “all marketers making express or implied claims about attributes of their product or service must have a reasonable basis for their claims at the time they make them.”²⁹ Reasonableness is determined from the perspective of the consumer, not the marketer. Elaborating, the FTC adds that in green marketing, competent and reliable scientific evidence will be required, including tests, research, and studies, performed by qualified professionals using generally accepted procedures that produce accurate and reliable results.³⁰

In implementing the FTC Act, the FTC has developed a variety of rules and guides related to energy and environmental marketing practices, including the “Guides for the Use of Environmental Marketing Claims” or “Green Guides” that address the application of Section 5 of the FTC Act to environmental advertising and marketing practices. The Green Guides, like other FTC guides, are administrative interpretations of law to assist the public in complying. See 16 CFR § 260.1. According to the FTC, the guides focus on the way in which consumers understand environmental claims rather than on technical definitions. The Guides offer markets that follow them safe harbors. 16 C.F.R. § 260.3.

The nature of offset and REC claims raise particular challenges because consumers cannot easily verify that they are receiving that for which they paid. For example, most consumers would have great difficulty confirming that their payments actually fund projects that may take place in a distant location. Moreover, even if a consumer could verify a project’s existence, it likely would be impossible for the average consumer to determine whether the scientifically complex project actually reduces atmospheric carbon in the amount claimed, or how much the consumer’s offset purchase actually contributes to the project. As a result, the FTC explains, the potential for deception is greater than with more tangible products for which consumers more easily can confirm most advertising claims.

The FTC raised a number of related questions: when consumers buy these products, do they know what they are buying; how do consumers interpret express or implied claims about

²⁷ FTC Notice at p. 8.

²⁸ See *FTC Policy Statement on Deception* appended to *Cliffdale Associates, Inc.*, 103 F.T.C. 110, 174 (1984) (<http://www.ftc.gov/bcp/policystmt/ad-decept.htm>). See also 15 U.S.C. §45.

²⁹ Ft. Notice at p. 9.

³⁰ FTC Notice at p. 9.

environmental benefits from offsets and RECs; do consumers assume that their offset purchases are creating reductions in greenhouse gas emissions beyond what would have otherwise occurred without offset sales; how quickly do they believe reductions occur; should marketers consider consumer understanding about the incidental benefits of renewable energy, such as air pollutant reductions or regional environmental improvements; and do consumers interpret REC and offset claims to include implied claims of broader (or narrower) environmental benefit? The FTC's view is that these questions are important because marketers must ensure that all reasonable interpretations of their claims are truthful, not misleading, and substantiated.³¹

Substantiation in particular can pose challenges in the REC and offset markets. One difficulty is that bringing RECs and offsets to market may involve multiple transactions and a large number of entities making the methods used to track RECs and offsets through the market complicated. In addition, efforts to verify the validity of these products can be difficult because the underlying activities may take place in remote locations or over an extended time period. Inadequate tracking and verification systems could lead to substantiation problems, even for marketers acting in good faith, and could create opportunities for bad actors to deceive consumers.

The concept of "additionality" is another concern.³² As noted, "additionality" addresses whether carbon offset consumers are paying for a project that would have occurred without the offset market. In the view of many involved with this market,³³ offset sellers have a duty to demonstrate that their underlying GHG reduction projects would not have occurred but for the sale of the offset; otherwise, they argue, sellers are not really reducing greenhouse gas emissions. Under this view, for example, it would not be appropriate to sell offsets based on a project (e.g., capturing methane from a landfill) implemented to comply with existing environmental regulations because any greenhouse gas reductions would have occurred without the sale of the offsets. The April 14, 2008 edition of *The Wall Street Journal* contains an article about two leading carbon marketers that fund clean-air projects in poorer nations whose stock price is dramatically dropping amidst allegations by the U.N. that the credits they are selling may have been for projects that would have happened anyway.

SEC Disclosure Liabilities

Another federal regulatory program, which focuses on investors rather than consumers, also creates the potential for liability based on inaccurate marketing. Section 10(b) of the Securities Exchange Act of 1934 creates the potential for disclosure liabilities also. It makes it unlawful for

³¹ FTC Notice at pp. 13-15.

³² "Additionality" is a term generally associated with mandatory carbon reduction programs implemented pursuant to the Kyoto Protocol, an international agreement under the United Nations Framework Convention on Climate Change (<http://unfccc.int/resource/docs/convkp/kpeng.pdf>). While no such mandatory program exists in the United States, many offset marketers and other interested parties in the United States have looked to the Kyoto framework in developing practices in the voluntary offset market in the United States.

³³ See, e.g., "A Consumers' Guide to Retail Carbon Offset Providers," Clean Air-Cool Planet (2006) (<http://www.cleanair-coolplanet.org/ConsumersGudetoCarbonOffset.pdf>); Kollmus, A., "Voluntary Offsets For Air-Travel Carbon Emissions: Evaluations and Recommendations of Thirteen Offset Companies," Tufts Climate Initiative (De. 2006) (http://www.tufts.edu/tie/tci/pdf/TCI_Carbon_Offsets_Paper_april-2-07.pdf); and "The Green-e Greenhouse Gas Emission Reduction Product Certification Program Standard," Center for Resource Solutions (June 2007) (http://resource-solutions.org/mv/docs/Ge_GHG_Product_Standard_VI.pdf).

anyone to make an untrue statement or to omit to state a material fact in connection with the purchase or sale of any security. Rule 10b-5 is the general anti-fraud rule of the Securities and Exchange Commission (SEC).

To establish fraud, a plaintiff must plead and prove a misrepresentation or omission of material fact, made with the intent to defraud, on which plaintiff relied, that proximately caused the plaintiff's injury. Liability under the Securities Exchange Act include exposure to third party actions and civil and criminal sanctions and injunctive relief . It also is the likely basis for a complaint or a judicial attack by plaintiffs on a company's allegedly false green or carbon neutral claims.³⁴

Liabilities Associated With Other Reporting Obligations

A key aspect of reporting relates to how various parameters of corporate social responsibility are to be measured. At present there are no regulatory metrics, but there are a number of voluntary frameworks that provide guidance. The Global Reporting Initiative (GRI) is a multi-stakeholder network of thousands of experts in dozens of countries who pioneered the world's most widely used sustainability reporting framework. The GRI Sustainability Reporting Guidelines provide organizations detailed guidance on how to report their sustainability performance, including as regards: strategy and analysis; organization profile; report parameters; and governance,

³⁴ With regard to SEC disclosures, the focus up to now has been on whether there is a duty to report rather than on the accuracy of the reports that have been filed.

SEC regulations provide some general guidelines that may bear on reporting on sustainability issues such as climate change. The SECs rules require that various filed reports contain discussions of trends, events or uncertainties that will be reasonably likely to have a material effect on the company. See 17 U.S.C. §§ 229.101, 229.303.

Regulation S-K Item 101, regarding disclosure of capital expenditures, requires disclosure of any material effect that environmental compliance costs may have on earnings, and competitive position. But presently, corporate sustainability is not regulatory required.

Regulation S-K Item 103 requires the disclosure of material pending legal proceedings, other than "ordinary routine litigation incidental to the business." 17 C.F.R. § 229.103. Litigation is increasingly being used to determine corporate sustainability responsibilities, especially as regards climate change.

Regulation S-K Item 303, which sets out guidance for management's discussion and analysis (MD&A), creates a potential basis for corporate sustainability and climate change disclosure. The MD&A typically identifies and discusses "known trends or any known demand, commitments, events, or uncertainties that will reasonably result in or that are reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way," and known trends or uncertainties reasonably expected to have a material impact on sales, revenues or income 17 CFR § 229.303(a)(1), (a)(3)(ii); Securities Act Release No. 33-6835. In 2007, New York Attorney General Cuomo launched an investigation of five major energy companies, questioning whether their disclosures adequately informed investors of the risks and liabilities posed by carbon dioxide emissions from new power plants.

Various stakeholders have pressured the SEC to put more teeth into reporting requirements relating to corporate social responsibility in the area of greenhouse gases. In September of 2007, a group of pension plans and institutional investors, in conjunction with Ceres (a network of investors, environmental organizations and public interest groups focused on sustainability issues,) filed a petition calling for the SEC to issue an interpretive release clarifying that material climate change information must be included in corporate disclosures under existing law. The SEC has declined to act on that petition.

commitments and engagement.³⁵ The Carbon Disclosure Project (CDP), international non-profit servicing institutional investors with a combined \$57 trillion of managed assets, has requested from 3,000 of the world's largest corporations information on business risks and opportunities presented by climate change, as well as greenhouse gas emissions data.³⁶ CDP asserts their methodology has become the gold standard for carbon disclosure.

Some reporting however, may not remain voluntary for long. The "Consolidated Appropriations Act, 2008" contains requirements for the US Environmental Protection Agency (EPA) to establish mandatory greenhouse gas reporting requirements. EPA is directed to draft rules by September 2008 and finalize rules by June 2009. Incorrect reporting under those rules, when drafted, likely will create the potential for regulatory sanctions.

Reputational Liabilities

Because so much of what is seen in the market place regarding carbon disclosures is driven by consumers, investors, lenders, and other stakeholders rather than by regulation, the greatest risks to a company of an untrue disclosure are perhaps as much to its reputation in the market place as to its exposure to liabilities from government enforcement actions or third party claims. These reputational liabilities are more likely to arise in representations that involve the purchase of credits and estimation of GHGs associated with the lifecycle of a product, rather than with estimation of GHG emissions, because of the uncertainties associated with verifying those representations.

Conclusion

Because there is no national mandatory cap-and-trade program for GHGs, it is difficult to assure that purchased carbon credits are real. It also is difficult to estimate indirect GHG production associated with product manufacture and distribution. As a result, even a well intentioned company may make disclosures that turn out to be untrue. Untrue disclosures may give rise to liability under a number of regulatory programs and under the common law, as well as to a corporation's reputation. In preparing carbon neutral or other green disclosures or claims, therefore, companies should consider potential liabilities as well as benefits.

³⁵ Global Reporting Initiative at <http://www.globalreporting.org/Home>.

³⁶ Carbon Disclosure Project at <http://www.cdproject.net/>.