Downstream Emissions as Climate Impacts

On the UK Supreme Court ‘s Landmark Finch Decision

Daria Shapovalova

20.06.2024 doi: 10.59704/4b7883bc5929bcc9

In a 3-2 majority, the UK Supreme Court delivered a landmark ruling today, significantly impacting the consideration of climate impacts in the oil and gas licensing process. While the Government’s approach so far has been to only consider exploration and production emissions, the Court’s decision establishes that emissions resulting from burning the produced oil and gas (regardless of where it occurs) have to also be considered.

The ruling is significant as it is the first highest court decision to adopt this interpretation on climate impacts of fossil fuel production. It will no doubt have a knock-on effect on at least three other cases pending before lower courts in the UK, and potentially affect cases both within and outside the European Union. Read together with recent case law in Norway and the United States, this decision underscores the shifting legal landscape towards the convergence of energy and climate law.

Downstream Emissions and Climate Goals

The climate impacts of the fossil fuel industry occur at every stage of development, from exploration and production to the final use of resources. However, the accounting of these emissions in the licensing of oil, gas, and mining development has traditionally been limited.

In the context of fossil fuel production, greenhouse gas emissions can be generally divided into upstream and downstream emissions. Upstream emissions occur during exploration and production. Most of the emissions, however, arise from the combustion of produced fossil fuels, so called ‘downstream’ or ‘Scope 3’ emissions. For instance, in the case of oil, downstream emissions account for 67 to 95% of total emissions, depending on the processes used. Estimating these emissions is possible but can be complicated due to the global nature of the energy market, where resources are often consumed thousands of miles away from their production site.

There is increasing recognition of the need to curtail fossil fuel production to meet the Paris Agreement goals. Integrating the full spectrum of climate impacts, including downstream emissions, into the decision-making process for fossil fuels projects is imperative to comply with climate law obligations.

Environmental Impact Assessment for Oil and Gas Projects

The main environmental regulatory tool in the process of approving oil and gas licenses is the Environmental Impact Assessment (EIA). This procedural requirement mandates energy companies to submit an in-depth report to the regulator, which is then made public and scrutinised before a final decision is made. The procedural nature of EIA means that if a significant risk of harm is found, the legislation does not require the regulator to reject the application. There have been some challenges of EIA on procedural grounds, used as a vehicle to bring the courts’ attention to substantive environmental issues, but this has not proven to be a successful litigation strategy.

In the UK, EIA regulations set out detailed process requirements regarding the content of the assessment including climate impacts. However, developers and regulators have interpreted these regulations to consider only upstream emissions, excluding downstream or Scope 3 emissions. The regulations are based on the EU EIA Directive, which defines impacts broadly to include “indirect, secondary, cumulative, transboundary, short-term, medium-term and long-term,

permanent and temporary, positive and negative effects of the project".

There have been many attempts to incorporate downstream emissions into the UK regulators' decision-making process. First, to reconcile the objectives of 'maximising economic recovery' and pursuing net zero, the Government developed a Climate Compatibility Checkpoint for the new oil and gas licenses, in time for the latest licensing round early last year. While the original conception of the Checkpoint was quite ambitious, the final draft turned into a watered-down non-statutory version, doing away with several criteria, including the assessment of Scope 3 emissions.

Second, there have been a number of cases brought by environmental NGOs challenging onshore and offshore oil and gas licenses on the grounds that Scope 3 emissions were not taken into account. So far, courts in the UK have sided with the Government in all these cases, including the lower courts' decisions in Finch and *Greenpeace Limited v The Advocate General*.

The Main Arguments in Finch

The lower courts' reasoning revolved largely around the meaning and scope of the 'project' under assessment, with the argument that consumption of any produced product is not included within the scope. The Court of Appeal in *Finch* held that the refinement process is a "separate and substantial" industrial activity carried out by separate companies. The effects of these activities were seen as not only "far removed from the proposed development itself" but also not "causally linked to it".

The dissent of Moylan LJ in the Appeal Court's decision adopted a wider definition of "project" from European Union law, which requires mandatory EIA for oil development "for commercial purposes". He concluded that a "purposive approach to the interpretation of the provisions applicable in this case points strongly towards their application not being so limited".

The Appeal Court, despite ruling in the Government's favour, left the door open regarding downstream emissions. It disagreed with the conclusion that downstream emissions impact is "legally incapable" of being assessed. Rather, the Court concluded, it was for the regulator to decide whether Scope 3 emissions should be considered, granting a wide margin of appreciation to the approving authority in the interpretation of the vague legislation.

A big question was to what extent the Supreme Court would rely on EU law in its interpretation. The Supreme Court did engage extensively with EU legislation, principles, and relevant case law. Concerning the meaning of the project, the Court found the recently decided similar case in the Oslo District Court in Norway to be "persuasive". The inclusion of Scope 3 emissions was examined in both the US and Norwegian courts, with the latter being particularly relevant as both the Norwegian and UK regulations are based on the same EU EIA Directive. As analysed in detail on this blog, the Norwegian case ruled three petroleum production licenses invalid largely due to the lack of consideration of Scope 3 emissions.

The Supreme Court rejected the Appeal Court's view on the regulators' margin of appreciation concerning the causal connection between fossil fuel extraction and final consumption. The Supreme Court's majority agreed that "extracting the oil from the ground guarantees that it will be refined and burnt as fuel". Rejecting the idea of the regulators' evaluative judgment, the Court concludes that this approach risks "unpredictable, inconsistent and arbitrary decision-making".

The argument about the refinement of oil transforming it into a different product was also rejected by the Supreme Court as refinement "does not alter the basic nature and intended use of the commodity". Therefore, having this intermediate process before burning the fuels does not break the causal connection between the extraction of the oil and emissions from its use.

There was further concern from the Appeal Court that ruling in favour of the claimants would result in ramifications for other industries. For instance, the production of steel ultimately used to manufacture lorries would need to account for transportation emissions. The Supreme Court considered these concerns to be "misplaced", arguing that while raw materials

can be put to many possible uses, this is not the case for oil.

Impact and Significance of the Finch Decision

The decision comes at a critical time as the future of the oil and gas industry is on political "trial". With the upcoming general election, the two main political parties are adopting radically different approaches, with the Conservatives advocating for more licensing rounds, and Labour for a presumption against new licensing rounds on climate grounds.

The decision will alter the regulation of the oil and gas industry in the UK as all future oil and gas projects will now need to include Scope 3 emissions in their EIA. The regulator will still have the final decision-making power on approvals and can apply its policies in this regard, likely influenced by the political party in power after the election.

Consequently, this decision does not mean that climate impacts will halt new licenses. Rather, it ensures that the regulator can make informed decisions with a comprehensive understanding of climate impacts. It further will provide for better public awareness of the full impacts of oil and gas production on climate. The regulator may proactively update its regulations and guidance to reflect this decision.

The pending judicial challenges to approvals for the Jackdaw and Rosebank oil fields in the UK Continental Shelf, which involve the failure to incorporate Scope 3 emissions, will now likely follow the *Finch* decision. The depth of the Court's analysis suggests that this ruling will be influential not only within the UK but also in other jurisdictions.

ABOUT THE AUTHOR

Daria Shapovalova
Dr Daria Shapovalova is a senior lecturer in energy law at the University of Aberdeen.

SUGGESTED CITATION

Shapovalova, Daria: Downstream Emissions as Climate Impacts: On the UK Supreme Court 's Landmark Finch Decision, Verfassungsblog, 20.06.2024, doi: 10.59704/4b7883bc5929bcc9.

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Langzeitarchiviert bei IntRechtDok unter: doi.org/10.17176/20240621-152116-0.