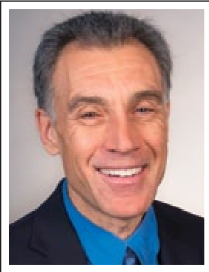
Climate Control



Schneiderman Targets Peabody Energy

Shareholder Protection or War on Coal?

By Marlo Lewis, Jr.

Did New York Attorney General Eric Schneiderman investigate Peabody Energy to protect shareholders against "misrepresentation" of climate-related shareholder risks? No. Schneiderman's investigation is part of the broader political campaign against fossil fuels. While it goes by various names – "war on coal," "divestment," "keep it in the ground," or "climate action" – the goal is clear: suppress the production and use of energy from coal, gas, and oil.

Schneiderman investigated Peabody under New York's Martin Act, a securities-fraud statute with a low bar for establishing guilt. To convict, the prosecutor need not prove intent to defraud, shareholder injury, or even that the company made false statements. Rather, he only has to show that the company omitted "material" facts in shareholder communications.

In his settlement agreement with Peabody, Schneiderman faults the company for: (1) claiming an inability to "reasonably predict" the financial impacts of potential climate policies; (2) citing one set of International Energy Agency (IEA) coal market projections but not others; and, (3) not publishing the results of analyses Peabody conducted or commissioned on the coal market impacts of particular climate policies.

Schneiderman does not call those actions fraud, but rather "misrepresentation" of "material" facts. Accordingly, the settlement agreement does not impose fines, damage awards, or jail sentences. Rather, Peabody agrees henceforth to abstain from claiming an inability to predict the costs of potential climate policies, disclose any cost estimates it makes, and include all coal market projections by experts it cites.

Interestingly, the agreement does not even require Peabody to acknowledge that it misrepresented material facts. Which raises an obvious question: Did Peabody do anything wrong?

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In its annual reports, Peabody has made clear that domestic or international climate policies "could result in electricity generators switching from coal to other fuel sources" (*2011 Annual Report*, p. 28). But Schneiderman objects that Peabody "denied its ability to reasonably predict" the financial impacts of such policies (agreement, p. 2).

According to Peabody: "[P]otential financial impact … will depend upon the degree to which any such laws or regulations force electricity generators to diminish their reliance on coal as a fuel source." That in turn will depend on "the specific requirements imposed by any such laws or regulations, the time periods over which those laws or regulations would be phased in, the state of commercial development and deployment of CCS [carbon capture and storage] technologies and the alternative markets for coal."

That explanation is correct. As the IEA stated in its *World Energy Outlook 2002*: "Major new [climate] policy initiatives will inevitably be implemented during the projection period, but it is impossible to predict precisely which measures among those that have been proposed will eventually be adopted and in what form" (p. 38).

Modesty in estimating the costs of potential future policies is standard in annual reports. In their 2014 filings with the Securities and Exchange Commission, General Electric, Siemens, and Vestas all acknowledge the financial importance of the wind production tax credit, but none includes estimates of adverse business impacts if the credit is not renewed. Schneiderman does not investigate those companies for "misrepresentation." Is that because those

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companies are considered "green"?

Moreover, Peabody's omission of IEA coal market projections under climate policies not yet implemented – or even proposed – would be "material" only if the IEA could predict which policies governments will adopt and when. Such prediction is inherently speculative, as the IEA itself has acknowledged.

What we do know is that coal's contribution to electricity generation among Organization for Economic Cooperation and Development countries in 2010 was 14.5 percent greater than the IEA projected in its *2002 Alternative Policies Scenario* (which was based on assumptions about future climate policies). Even IEA "current policies" scenarios can underestimate coal demand. China's demand for coal in 2010 was 87 percent greater than in the IEA's *2002 Reference Scenario*, while world demand outstripped the IEA's estimate by 28 percent.

Not reporting a carbon tax analysis that Peabody commissioned might be a "material" omission if Congress were hotly debating such a tax. But President Obama has declined to propose carbon taxes, and majorities in both the House and Senate have preemptively voted against them. What canon of law or ethics requires Peabody to publish assessments of policies with no current prospect of enactment?

Besides, publishing the analysis would not tell shareholders anything "material" they don't already know. Onerous restrictions on coal mining, coal-electric generation, and coal exports could obviously put Peabody out of business. That is not insider information. Just ask the Sierra Club; they'll gleefully tell you.

Anyone who hasn't been asleep for the past 20 years knows that an aggressive political movement wants to bankrupt fossil-energy companies via cap-and-trade, renewable energy quotas, and various keep-it-in-the-ground policies. The institutional investors who reportedly own 83% of Peabody stock monitor climate policy and do their own coal market projections.

So why did Schneiderman sue Peabody? Because Peabody is America's biggest coal company. He also likely wanted to establish a precedent before launching a Martin Act investigation of even bigger game: ExxonMobil.

Schneiderman has no ax to grind against coal companies? He is lead attorney for the 25 states and municipalities intervening on behalf of the U.S. Environmental Protection Agency in litigation over the agency's Clean Power Plan, which is designed to accelerate coal plant retirements.

Climate campaigners for years have urged fossil-energy companies to spotlight the risks their shareholders will face in a carbon-constrained world. But who created those risks in the first place if not the same politicians and activists trying to bankrupt fossil fuel producers?

The campaigners demand that coal and oil companies either confess to being "unsustainable" or face prosecution for fraud. Both confession and prosecution are expected to produce the same result: scare away investors and depress shareholder value. Schneiderman claims it's all to protect shareholders. PUF