As Rick previously blogged, the U.S. District Court for the Eastern District struck down California's Low Carbon Fuel Standard (LCFS) last month on the grounds that the standard discriminates against out-of -state ethanol producers in violation of the Commerce Clause of the United States Constitution. The decision — *Rocky Mountain Farmers Union v. Goldstene* — is likely to be only the first of several court decisions that grapple with the extent to which states can regulate the importation of high greenhouse gas emitting fuels for transportation and for electricity generation. North Dakota has already sued to invalidate a Minnesota statute that prohibits the importation of coal-based electricity from plants built after 2007. Challenges to California's prohibition on long-term electricity contracts may also follow.

Here's the conundrum states face. The dormant Commerce Clause — which really isn't a clause at all but an implicit constitutional limitation on states' rights to regulate — prohibits states from discriminating against or improperly burdening interstate commerce. States may not, for example, explicitly favor their own businesses while discriminating against out-of-state ones. This "facial" discrimination, especially when geared at "simple economic protectionism," is virtually always impermissible. Leading Supreme Court cases include *City of Philadelphia v. New Jersey* and *Hunt v. Washington State Apple Advertising Comm*. Even a state statute that doesn't on its face discriminate against out-of-state commerce can still be found unconstitutional if it imposes an excessive burden on out-of-state businesses as compared to the in- state benefits the law produces. But the constitutional test for such "incidental" effects on commerce is much easier for a state to pass than the test imposed on state statutes that discriminate directly. (For a great analysis of dormant Commerce Clause issues and state climate change legislation, here's an article by Dan).

So, why is California's LCFS vulnerable to constitutional challenge? Because in attempting to lower the carbon content of transportation fuels by 10 percent by 2020, the state requires providers of fuel to determine the "carbon intensity" of the fuel throughout its lifecycle, including not only direct emissions from the burning of the fuel but also emissions from transporting the fuel to California. The result is that fuel imported into California can have a higher carbon intensity that fuel produced in California even if the fuel is otherwise identical. The regulations themselves say that the location of the production facility affects the carbon intensity of the fuel. Thus, the challengers to the California rule say, the California LCFS is discriminatory *on its face*. Their argument is based on part on a Table

published by the California Air Resources Board, which adopted the rule, that assigns different carbon intensity values to ethanol depending on where it's produced so that midwestern ethanol has a higher carbon intensity than California ethanol. (The chart is reproduced on page 7 of the court opinion).

So does the California Low Carbon Fuel Standard discriminate against out-of-state ethanol producers on its face? Or only incidentally? The answer to those questions results in a very different constitutional standard being applied. If the standard discriminates on its face, a court is very likely to strike it down. If it discriminates only incidentally by imposing a greater burden on out-of-state fuels, then a court will be much more deferential to the state. The U.S. District Court in *Rocky Mountain Fuels* agreed with the midwestern ethanol producers and said that the California LCFS discriminates against out-of-state producers on its face and is, therefore, unconstitutional.

But the tough question in the case is that California's LCFS is motivated not by an attempt to favor in-state business over out-of-state ones (which is what the dormant Commerce Clause is designed to guard against) but to lower the overall carbon intensity of the fuel (and therefore total greenhouse gas emissions). And the LCFS doesn't explicitly say it will favor in-state versus out-of-state fuel producers; instead the regulations are designed to measure carbon intensity by taking into account the full life cycle of the fuel produced. Without including the greenhouse gas emissions emitted in transporting the fuel to the state, California could actually *increase* total emissions rather than decreasing them. So should the standard be subject to the same constitutional analysis as a blatantly discriminatory statute designed to promote in-state businesses? The *Rocky Mountain* court, while recognizing these issues, nonetheless felt bound by higher court precedent to strike the LCFS down.

The North Dakota challenge to Minnesota's Next Generation Energy Act of 2007 (*North Dakota v. Swanson*) raises similar issues. The Minnesota Act prohibits the importation of greenhouse gas intensive electricity from facilities built after the operative date of the statute. Additionally, utilities are prohibited from entering into long-term power agreements that would increase overall greenhouse gas emissions in the state. The effect is to prohibit the importation of coal-based electricity generation, principally from North Dakota. The same questions will arise in the North Dakota challenge. Is the statute discriminatory on its face even though it also prohibits the construction of new coal fired power plants in-state? Does it matter that the purpose of the statute is to limit greenhouse gases, not to favor in-state businesses?

California has a law somewhat similar to Minnesota's. The California law prohibits utilities from entering into long term contracts for electricity that is more greenhouse gas intensive than an efficient natural gas facility. The effect is to bar reliance on coal either from in or out-of-state. California currently has no in-state coal generation but imports a fairly high percentage of its electricity from coal generators in Utah. We may well see a commerce clause challenge to the California prohibition.

The California opinion will not by any means be the last word on the constitutionality of state efforts to regulate carbon-based fuels originating outside state borders. Interestingly, if one or more of these cases reaches the U.S. Supreme Court, California, Minnesota and environmentalists may have some unusual allies. Both Justices Thomas and Scalia do not believe the states are subject to a dormant Commerce Clause. As Thomas has written, "the so-called 'negative' Commerce Clause is an unjustified judicial intervention, not to be expanded beyond its existing domain." Thus in the view of Thomas and Scalia, the California LCFS and the Minnesota ban on coal-fired electricity ought to be constitutionally acceptable.