ARB's winning streak in climate cases continues. A California superior court has rejected a prominent set of industry challenges to the state's cap-and-trade program, upholding a significant element of California's suite of programs to comply with AB 32 and to reduce the state's greenhouse gas emissions back to 1990 levels by 2020. (Opinion here.) The cases were filed by the California Chamber of Commerce and the Pacific Legal Foundation, which charged that the cap-and-trade program was illegal both as an unconstitutional tax and because the program's auction was not authorized by AB 32. (I discussed the court's August tentative partial ruling in this case here, and Ann has discussed the case background here and here).

As he did in his tentative, Judge Frawley concludes that AB 32 gave ARB wide discretion to design a system of emissions reductions that meets the statutory goals, including authority to employ an auction as a reasonable means to allocate allowances. The Court writes that "both the text and structure of AB 32 demonstrate that the Legislature delegated to ARB the choice of distribution methods." This holding isn't really surprising given the very broad discretion the Legislature gave ARB to design a program to meet AB 32's goals. Every case that has challenged ARB's statutory authority under AB 32 has come up short (see, for example, my post here discussing another such case).

The more interesting element of the case involves the constitutional questions concerning whether the auction amounts to a tax. This set of arguments is trickier. The state is making a lot of money off the auction. The auction has raised more than $300 million so far, largely from businesses regulated under the cap, and much of this revenue will initially be loaned to the General Fund. But as I've written before, and as defendants argued, the auction is missing many of the classic hallmarks of a tax. Most strikingly, purchasers at auction get a tradeable commodity at its market value, and no regulated entity is required to participate as a buyer in the auction.

On this issue, the Court held that Proposition 13 is the legal regime that controls, rather than the more recently enacted Prop 26. He also eschewed what might have been the easiest way to dodge the tax conclusion, holding that regardless of the subjective intent of those designing the auction, it qualifies under Prop 13 as having been enacted "for the purpose of increasing revenues," since it will in fact raise revenue for the state. But he nevertheless declined to hold the auction a tax, concluding that it's more akin to a regulatory fee–though an imperfect match for any current category of fee. He cited the fact that those who purchase allowances receive a tradeable right to pollute, and he analogized the purchase of that right to a purchase of a hunting license or a mineral extraction permit. He also relied on the fact that auction prices are determined, at least in part, by market forces, not by government fiat. Having concluded that the auction imposed something akin

to a regulatory fee or charge, he applied a modified Sinclair Paint-type analysis and held the fee valid. Interestingly, this analytical approach reinforces the notion that auction revenues must be spent on projects that further AB 32's purposes — an idea that the State has embraced anyway, but that would not necessarily have been legally required had the Court come down another way.*

Plaintiff Pacific Legal Foundation has already sent out an email blast vowing to appeal, so this case is far from over. The longer the cap-and-trade program is in place, however, and the more auctions and private-party trades are conducted, the harder it becomes to imagine what remedy any judge might issue to claw it back.

*UPDATE: I mean to say not legally required by AB 32 and Prop 13 itself. I recognize that other laws have been passed, since AB 32, restricting the use of auction funds to these purposes (including SB 1018 and AB 1532).