SUPERIOR COURT OF CALIFORNIA

COUNTY OF SACRAMENTO

CALIFORNIA CHAMBER OF COMMERCE, et al. **v.** **CALIFORNIA AIR RESOURCES BOARD, et al.**	Case No.: 34-2012-80001313 Related Case No.: 34-2013-80001464 **JOINT RULING ON SUBMITTED MATTERS**
MORNING STAR PACKING COMPANY, et al. **v.** **CALIFORNIA AIR RESOURCES BOARD, et al.**	**Date:** August 28, 2013 **Time:** 9:30 a.m. **Dept.:** 29 **Judge:** Timothy M. Frawley

Introduction

In 2006, the Legislature enacted Assembly Bill 32 (AB 32), the California Global Warming Solutions Act of 2006. AB 32's stated goal is to reduce greenhouse gas (GHG) emissions in the State to 1990 levels by the year 2020. AB 32 delegates to the California Air Resources Board (ARB) the responsibility to adopt regulations to achieve the statewide GHG emissions limit. As part of its regulations, ARB has adopted a cap-and-trade program, under which covered entities must acquire an "allowance" for every ton of GHG emissions they emit. ARB distributes some of the allowances to covered entities free of charge, and sells the remainder (primarily at auction), with proceeds to be used by the State of California to further the regulatory purposes of AB 32. The Legislative Analyst's Office has estimated that over the life of the program the sales will raise as much as $12 to $70 billion in revenues for the State.

Petitioners challenge the sale/auction provisions of ARB's regulations, on two grounds. First, Petitioners contend the provisions are invalid because they exceed the scope of authority delegated to ARB in AB 32. Second, even if AB 32 were construed to authorize the sales of allowances, Petitioners contend the charges for the allowances constitute illegal taxes adopted in violation of the supermajority vote requirement of article XIIIA of the California Constitution (Proposition 13). The court shall deny the petitions.

Background Facts and Procedure

In 2006, the Legislature enacted Assembly Bill 32 (AB 32), the California Global Warming Solutions Act of 2006. The purpose of AB 32 is to reduce greenhouse gas (GHG) emissions in California. AB 32's stated goal is to reduce GHG emissions in the State to 1990 levels by the year 2020. AB 32 designates the California Air Resources Board (ARB) as the state agency to implement the statute and delegates to ARB the responsibility to design and implement a package of regulations to achieve the statewide GHG emissions limit by 2020. In adopting the regulations, AB 32 authorized ARB to include the use of a "market-based compliance mechanism" to reduce GHG emissions, such as a cap-and-trade program.

In 2011, ARB adopted regulations to implement AB 32. The regulations primarily rely upon a "market-based," cap-and-trade approach to reducing GHG emissions. Under the cap-and-trade program, ARB establishes an enforceable, firm limit (or "cap") on the total amount of GHG emissions that can be released by regulated sources. Regulated entities then must acquire a permit, known as an "allowance," for every ton of GHG emissions they emit during the compliance period.

The total number of allowances available in any year is equal to the cap for that year. Thus, the cap limits the total number of allowances available to regulated entities during a compliance period. Over time, ARB lowers the cap, reducing the total number of allowances available to regulated sources, thereby guaranteeing a reduction in overall emissions.

Allowances are tradable. Trading lets regulated sources buy and sell allowances, and thereby creates a market for carbon allowances. The cap determines the supply of allowances, and the quantity of emissions generated by the regulated sources determines the demand. The interaction between supply and demand sets the market price.

If a covered entity does not have sufficient allowances to cover their GHG emissions, it may acquire additional allowances from other covered entities. Since the total number of allowances in circulation is capped at a specified level, this does not increase overall statewide GHG emissions. Conversely, if an individual entity does not need all of the allowances it has in a given compliance period, the entity may "bank" those allowances for later use, or sell the allowances to another covered entity.

As the cap declines, regulated sources must decide how they will cover their emissions. Some entities will find it less costly to reduce their emissions to match their allowances, whereas others will find it less costly to purchase additional allowances to cover their emissions. Either way, the less they emit, the less they pay, so there is an economic incentive to reduce emissions. As ARB reduces the supply of allowances, the market price for allowances should rise, and the incentives to reduce emissions should become even stronger.

Throughout the rulemaking process for ARB's regulations, the question of allowance allocation was a prominent and controversial topic. Allowance allocation refers to how ARB will distribute the available allowances to regulated sources. ARB ultimately settled on a mix of distribution methods. In the beginning, ARB will distribute most of the allowances to certain regulated sources free of charge, to help ease their transition into the cap-and-trade program.[1] ARB will sell the remainder of the allowances at public auctions.[2] The proportion of allowances distributed for free will be reduced over time. By 2020, ARB plans to auction approximately 50% of GHG allowances.

ARB's regulations provide that auctions will consist of a single round of bidding, with sealed bids. Allowances will be sold in 1,000-unit bundles. There will be an "auction reserve price," which shall constitute the minimum acceptable bid price.

ARB's regulations provide that the proceeds from the sale of allowances at auction (excluding consignment sales) will be deposited into a special fund and available for appropriation by the Legislature for the purposes designated in AB 32. Several statutes enacted in 2012 give further direction on the expenditure of cap-and-trade auction proceeds.

The first bill, SB 1018, enacted on June 27, 2012, creates a new special fund, the Greenhouse Gas Reduction Fund, for monies collected by ARB from its auction of

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[1] The industrial sector, for example, will receive approximately 90% of the allowances needed to comply during the first two years of the program.

[2] In addition, a small percentage of allowances are set aside for a strategic price containment reserve and thereafter made available for sale at pre-established price or prices to buffer against higher than expected auction prices.

allowances. (See Cal. Health & Saf. Code §§ 16428.9, 16428.9.) To receive an appropriation from the Legislature, the bill requires state agencies to demonstrate how a proposed expenditure will further the regulatory purposes of AB 32 and how a proposed expenditure will contribute to achieving and maintaining GHG emission reductions pursuant to AB 32. (*Ibid.*) SB 1018 also authorizes the Controller to use monies in the fund for cash flow loans to the General Fund, as provided in Government Code §§16310 and 16381.

The second bill, AB 1532, enacted on September 30, 2012, mandates that monies collected from the State's sale of allowances be used to facilitate achievement of reductions in GHG emissions in California consistent with AB 32. AB 1532 directs the Department of Finance to develop a three-year investment plan that, among other things, will identify programmatic investments toward feasible and cost-effective GHG emissions reductions. Monies in the fund shall be appropriated through the Budget Act consistent with the investment plan. (See Cal. Health & Saf. Code §§ 39712, 39716, 39718.) AB 1532 provides that upon appropriation, monies in the Greenhouse Gas Reduction Fund shall be available to the state board and to administering agencies for administrative purposes in carrying out the investment plan. (*Ibid.*)

The third bill, SB 535, also enacted on September 30, 2012, requires the investment plan developed pursuant to Health & Safety Code §39716 to allocate a minimum of 25% of available monies in the Fund to projects that benefit disadvantaged communities and to allocate a minimum of 10% of the available monies to projects located within disadvantaged communities. (See Cal. Health & Saf. Code § 39713.)

The fourth bill, AB 1464, which is part of the Budget Act of 2012, enacted on June 17, 2012, makes up to $500 million in proceeds derived from the sale of allowances in fiscal year 2012-13 available to ARB to assist in achieving the goal of reducing GHG emissions and furthering the "regulatory purposes" of AB 32. (AB 1464, §15.11 [Defendant/Respondents' Request for Judicial Notice, Exh. K].) The Budget Act assumes that these proceeds will be used to offset General Fund costs of existing GHG mitigation programs. (*Ibid.*) Although AB 1464 was enacted in 2012, the State contends it has not yet expended any proceeds from the sale of allowances in fiscal year 2012-13.

The Legislative Analyst's Office estimated that the fiscal year 2012-13 auctions would generate roughly $660 million to upwards of $3 billion in revenues for the State. Through May of 2013, the auctions raised approximately $260 million in revenues for the State. Additional auctions have been (or will be) held in August and November of

2013. Over the life of the program, the LAO estimates that the auctions will raise as much as $12 billion to $70 billion in revenues for the State.

In addition to the auction revenues, AB 32 and the implementing regulations authorize ARB to collect a fee to recover the administrative costs of carrying out AB 32. (Cal. Health & Saf. Code § 38597; 17 C.C.R. § 95200 *et seq.*) The fees are intended to collect an amount of funds necessary to recover ARB's costs of implementing and enforcing AB 32 each fiscal year. The revenues collected pursuant to this section are deposited into the Air Pollution Control Fund and are available upon appropriation, by the Legislature, for purposes of carrying out AB 32

Petitioners/Plaintiffs California Chamber of Commerce, et al., and Morning Star Packing Company, et al., separately filed actions challenging ARB's cap-and-trade regulations. National Association of Manufacturers intervened in Case No. 34-2012-80001313 on the side of Petitioners/Plaintiffs. Environmental Defense Fund and Natural Resources Defense Council intervened on the side of Case Nos. 34-2012-80001313 and 34-2013-80001464 on the side of Defendants/Respondents. The court ordered the cases related.

Arguments of the Parties

These lawsuits do not challenge the ARB's authority to regulate GHG emissions in California, or the ARB's decision to regulate GHG emissions using a cap-and-trade program. The only thing challenged in these lawsuits is the provisions of the ARB's regulations that permit the ARB to sell GHG allowances at auction.

Petitioners contend the auction provisions are void because they exceed the scope of authority conferred on ARB in AB 32. Although Petitioners concede that the Legislature authorized ARB to adopt a cap-and-trade program, Petitioners contend the Legislature never intended to authorize ARB to raise billions of dollars by auctioning GHG allowances.

Further, Petitioners contend, AB 32 cannot authorize the auctions because it was not passed by two-thirds of the members of the Legislature, as required by Proposition 13. Under Proposition 13, any act to increase state taxes for the purpose of increasing revenues must be passed by a two-thirds supermajority vote of the Legislature. Petitioners contend that to the extent AB 32 is construed to authorize ARB to sell allowances, it constitutes a revenue-generating tax that was required to be adopted by a two-thirds supermajority vote. Since AB 32 was not adopted by a two-thirds

supermajority vote, Petitioners argue, AB 32 cannot lawfully authorize ARB to impose the tax.

Likewise, Petitioners argue, the post-AB 32 legislative enactments cannot supply after-the-fact authorization for the auctions because those enactments were not adopted by a two-thirds supermajority of the Legislature as required by Proposition 26.

Respondents/Defendants contend that the Legislature expressly delegated to ARB the authority to promulgate regulations to implement AB 32, including the choice of whether to adopt a cap-and-trade program and, if a cap-and-trade program is adopted, the choice of how to distribute emissions allowances as part of the program. Respondents argue that at the time AB 32 was adopted the Legislature understood that a cap-and-trade program requires the distribution of allowances, and that distribution may include the sale of allowances at auction. Since AB 32 does not expressly forbid this method of distribution, argue Respondents, the Legislature plainly intended ARB to have the discretion to include as part of a cap-and-trade program the sale of allowances by auction.

The administrative fee regulation does not restrict ARB's authority to "design" the "distribution" of allowances to include auction sales because the proceeds from the administrative fees are used for different purposes. Whereas the administrative fees will be used to cover the costs of administering AB 32 and the implementing regulations, the auction proceeds will be used for the broader purpose of reducing GHG emissions.

Moreover, even if AB 32 is deemed ambiguous, Respondents argue that ARB's interpretation is entitled to deference from this court.

Further, Respondents contend the Legislature removed any lingering doubt about whether it intended to allow the sale of allowances by enacting the post-AB 32 statutes addressing the use of the auction proceeds. According to Respondents, the post-AB 32 statutes unequivocally reflect a legislative understanding that ARB has the authority to sell allowances at auction.

Respondents also dispute that the auction of allowances authorized by AB 32 imposes a "tax" subject to Proposition 13. Respondents contend that Proposition 13 applies only to taxes "enacted for the purpose of increasing revenues." Respondents contend that the sale of allowances was enacted not for the purpose of increasing revenues, but for regulatory reasons, namely to (1) ensure market prices remain sufficiently high to stimulate reductions and encourage investment and innovation; (2) treat new businesses fairly and avoid windfall gains to established businesses; (3) foster

transparent market pricing and avoid market uncertainty and instability. Since the sale of allowances was enacted for regulatory reasons, and not for the purpose of increasing revenues, Respondents contend Proposition 13 does not apply.

In addition, Respondents assert that the auctions differ fundamentally from taxes in several respects. First, unlike taxes, auction participants pay a market price for a tradable benefit or privilege. Second, unlike taxes, the auction is not compulsory. Third, unlike tax revenues, auction sale proceeds will not be used for the general support of the government; under the post-AB 32 legislation, the auction sale proceeds must be used to further AB 32's goal of reducing GHG emissions. For these reasons, Respondents contend the sale of allowances is not subject to the two-thirds supermajority vote requirement of Proposition 13.

Discussion

There are two questions presented in these proceedings. First, are the ARB's auction provisions within the scope of authority conferred by AB 32? Second, if authorized, do the auction provisions constitute an illegal tax enacted in violation of the supermajority vote requirement of article XIIIA of the California Constitution (Proposition 13)?

Does AB 32 authorize the sale of allowances?

An administrative regulation is not valid unless it is within the scope of authority conferred on the adopting agency by the enabling statute. (Cal. Gov. Code §11342.1, 11342.2.) Administrative regulations that alter or amend the statute or enlarge or impair its scope are void and courts are obligated to strike them down. (*Samantha C. v. State Dept. of Developmental Services* (2010) 185 Cal.App.4th 1462, 1481-1483.) While the agency's construction of the enabling statute is entitled to consideration and respect, it is not binding. The court, not the agency, is the ultimate arbiter of the interpretation of the law. (*Ibid.*; see also *Western States Petroleum Assn. v. Board of Equalization* (2013) 57 Cal.4th 401, 416.)

On the other hand, the absence of specific provisions regarding the regulation of an issue does not necessarily mean that such a regulation exceeds statutory authority. (*Association of California Ins. Cos. v. Poizner* (2009) 180 Cal.App.4th 1029, 1047; see also *Association of Irritated Residents v. State Air Resources Bd.* (2012) 206 Cal.App.4th 1487, 1495.) The doctrine prohibiting delegations of legislative power does not invalidate reasonable grants of power to an administrative agency, when suitable standards or safeguards are established to guide the power's use and to protect against misuse. (*Hess Collection Winery v. Agricultural Labor Relations Bd.* (2006) 140 Cal.App.4th 1584, 1604.) Only in the event of a total abdication of power will this court strike down a legislative enactment as an unlawful delegation. (*Kugler v. Yocum* (1968) 69 Cal.2d 371, 384; see also *Coastside Fishing Club v. California Resources Agency*

(2008) 158 Cal.App.4th 1183, 1204 [noting that the doctrine prohibiting delegation of legislative power has been "virtually abandoned" for all practical purposes].)

When the Legislature has delegated to an administrative agency the responsibility to implement a statutory scheme through regulations, the agency is not limited to the exact provisions of the statute in adopting regulations to enforce its mandate. (*Batt v. City and County of San Francisco* (2010) 184 Cal.App.4th 163, 171.) The agency is authorized to "fill up the details" of the statutory scheme. (*Ibid.*) The agency's authority includes "the power to elaborate the meaning of key statutory terms." (*Ibid.*)

Moreover, when an agency acting pursuant to statutory authority adopts regulations, the regulations are presumed valid and a court will interfere only when the agency has clearly overstepped its statutory authority. (*Ford Dealers Assn. v. Department of Motor Vehicles* (1982) 32 Cal.3d 347, 356.) The burden of proof is on the party challenging the regulations. (*Tomlinson v. Qualcomm* (2002) 97 Cal.App.4th 934, 941.)

In this case, AB 32 expressly authorized ARB to adopt regulations that establish a market-based compliance mechanism. (See Cal. Health & Saf. Code §§ 38562(c), 38570.) As Petitioners admit, the ARB's cap-and-trade program is a market-based compliance mechanism. (See AR Add-A-006111.) Thus, Petitioners concede, AB 32 authorized ARB to adopt a cap-and-trade program.

Cap-and-trade programs operate through the creation and distribution of tradable rights, usually called allowances, to constrain access to a previously free resource. (Ellerman, et al., Pricing Carbon (2010) [AR Add-A-843] pp.32, 84.) Since the cap constrains supply and creates scarcity, these allowances have value. (*Id.* at p.32.) The distribution of these allowances is called allocation, which is a unique feature of cap-and-trade programs. (*Ibid.*)

In theory, under certain idealized conditions, the allocation choices will have no effect on the supply and demand for the good in question -- in this case emissions. Trade will occur until marginal valuations and marginal costs are equalized. In reality, "idealized conditions," such as perfect information and the absence of transactions costs, may not exist. (*Id.* at pp.85, 120.)

Moreover, even under idealized conditions, allocation choices will have financial consequences, and therefore create "winners" and losers" among those participating in the program. (*Id.* at p.86; see also AR Add-A-008513.) Thus, at bottom, allowance allocation involves a "tough political decision" about who is to be the recipient of the value created by the legal constraint.

Allowances can be allocated free of charge, sold by the regulating authority through an auction or direct sale, or allocated by some combination of these methods.[3] If covered

[3] Many different methods can be used to distribute allowances free of charge, such as a lottery-system; "grandfathering" based on historical emissions; first-come, first-served; and benchmarking or other merit-based schemes to reward and encourage efficiency or other regulatory goals. In addition, allowances

entities receive the allowances free of charge, they capture the value associated with the allowances. If allowances are sold or auctioned, the government captures the value created by the cap. Whatever the allocation, whoever receives the initial allocation of allowances will receive a "windfall" equal to the value created by the constraint. (Pricing Carbon pp. 236-238.)

In AB 32, the Legislature expressly authorized ARB to:

> Design the regulations, including distribution of emissions allowances where appropriate, in a manner that is equitable, seeks to minimize costs and maximize the total benefits to California, and encourages early action to reduce greenhouse gas emissions. (Cal. Health & Saf. Code § 38562(b)(1).)

But even without this express delegation of authority, ARB would have faced an inevitable choice of how to allocate the allowances. Thus, both the text and structure of AB 32 demonstrate that the Legislature delegated to ARB the choice of distribution methods.[4]

Petitioners do not dispute that the cap-and-trade program requires emission allowances to be distributed in some manner. However, Petitioners argue that the text, structure, and legislative history of AB 32 show that the Legislature did not intend to authorize the sale of allowances. According to Petitioners, ARB's discretion is limited to choosing a method for distributing the allowances free of charge (or at least in a "revenue-neutral" manner). Petitioners raise the following arguments in support of their position: (1) the statute does not explicitly authorize ARB to auction allowances; (2) the legislative history includes no discussion of the term "auction;" (3) at the time of AB 32's enactment, most cap-and-trade program allowances were distributed for free; (4) construing AB 32 as authorizing the sale of allowances renders the administrative fee provision of the Act (Health & Safety Code § 38597) surplusage; (5) the chief sponsor of AB 32 (ostensibly) assured his colleagues on the floor of the Legislature, just before the vote, that the only funds to be generated under AB 32 were those generated by the administrative fee provision; (6) there is no guidance in AB 32 as to how to spend any auction revenues; and (7) the Legislature failed to enact a bill in 2009 that would have expressly authorized ARB to auction the allowances.[5]

The court does not find Petitioners' arguments persuasive. Although AB 32 does not explicitly authorize the sale of allowances, it specifically delegates to ARB the discretion to adopt a cap-and-trade program and to "design" a system of distribution of emissions

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could be freely distributed to covered entities or to non-regulated entities, who could then convert the value of the allowances into cash by selling them in the allowance market.

[4] ARB's choices must avoid disproportionate impacts on low-income communities, reward early action, consider cost-effectiveness and overall societal benefits, and minimize administrative burdens and emissions leakage. (Cal. Health & Saf. Code § 38562(b)(2)-(8).)

[5] Petitioners also argue that if AB 32 is construed as authorizing a sale of allowances, it constitutes an unconstitutional tax. This argument is addressed below.

allowances. The breadth of the delegation of authority to ARB supports, rather than undermines, ARB's construction of AB 32.

Further, the phrase "distribution of emissions allowances" has a technical meaning in the context of a cap-and-trade program, referring to the initial allocation of the tradable rights (or allowances). At the time AB 32 was enacted, both auctions and free distribution were recognized methods of distributing allowances in a cap-and-trade program. Petitioners' admit that at least two well-known cap-and-trade programs preceding the adoption of AB 32 authorized allowances to be sold or auctioned. (Chamber of Commerce's Opening Memorandum at p.21.) Similarly, the U.S. EPA's 2003 guide to designing a cap-and-trade program states that the first major step in the allowance distribution process is to decide whether allowances will be allocated at no cost or sold by the regulating authority. (AR Add-A-008513.)

In addition, in March of 2006, five months before AB 32 was enacted, the State of California's Climate Action Team submitted a report to the Governor and the Legislature noting that in a "market-based program" for reducing GHG emissions, "[e]mission allowances can be auctioned (i.e., sold) or given away." (AR Add-A-006120; see also Add-A-006113.) It is therefore reasonable to assume that the Legislature understood the phrase "distribution of emissions allowances" to potentially encompass both giving away allowances and selling them via an auction or direct sale. It follows that, having broadly delegated the choice of distribution methods to ARB, if the Legislature had meant to exclude the sale of allowances, it would have said so. It did not.

Post-AB 32 legislation -- pertaining to the use of auction proceeds -- also reflects a legislative understanding that AB 32 authorized the sale of allowances. (*People ex rel. Lockyer v. R.J. Reynolds Tobacco Co.* (2005) 37 Cal.4th 707, 724; see also *Professional Engineers in California Government v. Schwarzenegger* (2010) 50 Cal.4th 989, 1044, 1046-47 [later legislative enactment operated to "ratify" and "validate" furlough plan that Governor lacked authority to impose unilaterally].)

Petitioners' reliance on a 2009 bill (SB 31) that did not become law is misguided. Unpassed bills of later legislative sessions are generally regarded as having "little value." (*Apple Inc. v. Superior Court* (2013) 56 Cal.4th 128, 146.) In any event, a Senate Committee report on SB 31 reflects an understanding that AB 32 already authorized auctions. (Respondents' Request for Judicial Notice, Exh. R.)

It is relevant, but hardly dispositive, that AB 32 did not specify how auction proceeds would be spent since, at the time AB 32 was enacted, it was unknown whether there would be a cap-and-trade program at all.

Likewise, the fact that AB 32 includes an administrative fee provision does not prove the Legislature intended to require ARB to distribute allowances for free or in a revenue-neutral manner. It only proves the Legislature intended to ensure ABR could collect fees to pay for the administrative costs directly incurred in carrying out the provisions of

the statute.[6] Construing AB 32 as authorizing the sale of allowances does not render the administrative fee provision surplusage.

The "Legislative Letter of Intent" submitted by the chief sponsor of AB 32 is not to the contrary. The letter simply confirms that fees collected under the administrative fee provision would be used solely for the direct administrative costs incurred in administering the statute. There is no suggestion, as Petitioners claim, that "the only funds to be generated under AB 32 were those required to administer the program."[7]

The court concludes that the sale of allowances is within the broad scope of authority delegated to ARB in AB 32.

Do the auction provisions constitute an illegal tax?

Petitioners argue that if AB 32 is interpreted to authorize ARB to sell allowances, then AB 32 imposes an unconstitutional tax in violation of article XIII A, section 3 of the California Constitution (Proposition 13).

California voters adopted Proposition 13 in June 1978, adding article XIII A to the California Constitution. Proposition 13 imposed important limitations upon the assessment and taxing powers of state and local governments. (*Amador Valley Joint Union High Sch. Dist. v. State Bd. of Equalization* (1978) 22 Cal.3d 208, 218.) Article XIII A consists of four major elements: a real property tax rate limitation (§ 1); a real property assessment limitation (§ 2); a restriction on state taxes (§ 3); and a restriction on local taxes (§ 4). These four elements worked together to form "an interlocking 'package' . . . to assure effective real property tax relief." (*Id.* at p.231.)

Former article XIII A, section 3, set forth the restriction on state taxes. It provided that "any changes in State taxes enacted for the purpose of increasing revenues" must be approved by a supermajority (two-thirds) vote of each house of the Legislature. (Former Cal. Const. art. XIII A, § 3, as added by Prop. 13.)

On November 2, 2010, the voters adopted Proposition 26, which amended article XIII A, § 3. The findings and declaration of purpose for Proposition 26 states that, despite the enactment of Proposition 13 (in 1978) and Proposition 218 (in 1996), California taxes have continued to escalate. In addition, the Legislature and local governments have "disguised new taxes as 'fees' in order to extract even more revenue from California taxpayers without having to abide by [the existing] constitutional voting requirements." (Proposition 26.) It continues that, "Fees couched as 'regulatory' but which exceed the reasonable costs of actual regulation or are simply imposed to raise revenue for a new

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[6] This is not to say that the administrative fee provision does not aid Petitioners' interpretation. It does, but, notwithstanding the administrative fee provision, the court is persuaded that AB 32 authorizes the sale of allowances.

[7] It is true that an Enrolled Bill Report for AB 23 suggests that the Governor made a commitment not to impose additional costs on industry beyond their own costs of compliance. (Chamber of Commerce's Request for Judicial Notice, Exh. 12.) However, it is not clear whether the Legislature honored the commitment, or what the commitment even means.

program and are not part of any licensing or permitting program are actually taxes and should be subject to the limitations applicable to the imposition of taxes." (*Ibid.*) Thus, "[i]n order to ensure the effectiveness of [the existing] constitutional limitations, this measure . . . defines a 'tax' for state and local purposes so that neither the Legislature nor local governments can circumvent these restrictions on increasing taxes by simply defining new or expanded taxes as 'fees.'" (*Ibid.*)

As amended by Proposition 26, article XIII A, section 3, now requires a two-thirds supermajority vote requirement for "any change in state statute which results in any taxpayer paying a higher tax."[8] (Cal. Const. art. XIII A, § 3.) In addition, Proposition 26 broadly defines a "tax" as "any levy, charge, or exaction of any kind imposed by the State," except:

> (1) A charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the State of conferring the benefit or granting the privilege to the payor.
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> (2) A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the State of providing the service or product to the payor.
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> (3) A charge imposed for the reasonable regulatory costs to the State incident to issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof.
>
> (4) A charge imposed for entrance to or use of state property, or the purchase, rental, or lease of state property, except charges governed by Section 15 of Article XI.
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> (5) A fine, penalty, or other monetary charge imposed by the judicial branch of government or the State, as a result of a violation of law. (*Ibid.*)

Proposition 26 also shifted to the State the burden of demonstrating that a levy, charge, or other exaction is not a tax. (*Ibid.*)

However, Proposition 26 is not retroactive; it does not apply to legislative enactments before its effective date (November 3, 2010.) The Legislature enacted AB 32 in 2006.

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[8] The purpose of this amendment was to end the Legislature's practice of approving, by a simple majority vote, so-called "revenue-neutral" laws that increased taxes for some taxpayers but decreased taxes for others. (See *Schmeer v. County of Los Angeles* (2013) 213 Cal.App.4th 1310, 1329.)

Thus, as Petitioners concede, the language of Proposition 13, not Proposition 26, governs AB 32.

As described above, the language of Proposition 13 required that "any changes in State taxes enacted for the purpose of increasing revenues" be approved by a two-thirds majority of the Legislature. It is undisputed that AB 32 was not passed by a two-thirds majority of the Legislature. Thus, if the auction provisions of AB 32 are "changes in State taxes enacted for the purpose of increasing revenues," the auction provisions are invalid.

The phrase "enacted for the purpose of increasing revenues" does not require Petitioners to prove the government acted with a subjective motivation to increase revenues. The phrase simply requires Petitioners to prove that changes in state taxes would, considered in their entirety, result in a cumulative net increase in state tax revenues. (*Schmeer v. County of Los Angeles* (2013) 213 Cal.App.4th 1310, 1329; Chamber of Commerce's Second Request for Judicial Notice, Exh. 3, pp.2-5.)

It is undisputed that the auction provisions of AB 32 will result in a cumulative net increase in state revenues. The auction provisions will raise as much as $12 to $70 billion in new revenues for the State. It follows that if the costs of allowances under AB 32 are "taxes," AB 32 violates Proposition 13.

Taxes are enforced contributions, levied by the authority of the state, for the support of the government. (See *McHenry v. Downer* (1897) 116 Cal. 20, 24.) The essence of a tax is that it raises revenue for general governmental purposes. Most taxes are compulsory, rather than imposed in response to a voluntary decision to develop or seek other government benefits or privileges. (*California Farm Bureau Federation v. State Water Resources Control Board* (2011) 51 Cal.4th 421, 437.) However, cases recognize that "tax" has no fixed meaning, taking on different meanings in different contexts. (*Sinclair Paint Co. v. State Bd. of Equalization* (1997) 15 Cal.4th 866, 874.)

Although no cases have defined "taxes" for purposes of Proposition 13, cases distinguishing "taxes" from "fees" provide helpful guidance. The cases have recognized several general categories of compulsory fees or charges that are distinguishable from taxes and thus can be imposed without a two-thirds majority vote. These categories are: (1) special assessments and related business charges, (2) development fees, (3) user fees, and (4) regulatory fees.

Special assessments are charges imposed on a property to defray, in whole or in part, the expense of a permanent public improvement. A special assessment is like a special tax in the sense that it is levied for a specific purpose, but is distinguishable in that it confers a special benefit upon the property assessed beyond that conferred on the public as a whole. (See *Knox v. Orland* (1992) 4 Cal.4th 132, 142, superseded by statute on other grounds as stated in *Not About Water Com. v. Board of Supervisors* (2002) 95 Cal.App.4th 982.) The cases hold that special assessments levied in amounts reasonably reflecting the value of the benefits conferred on the assessed

property are not "special taxes." (*Sinclair Paint Co. v. State Bd. of Equalization* (1997) 15 Cal.4th 866, 874.)

Closely related to special assessments are business improvement district fees imposed to defray the costs of permanent improvements specifically benefitting the entities subject to the fee. As with special assessments, courts hold that where the burden for the expenditures is borne by the group specifically benefitted by them, Proposition 13 is not violated. (*Evans v. City of San Jose* (1992) 3 Cal.App.4th 728, 735-738; *Howard Jarvis Taxpayers Assn. v. San Diego* (1999) 72 Cal.App.4th 230, 238.)

A development fee is an exaction imposed in return for the privilege of developing land, commonly to defray the adverse impacts generated by the development. Development fees are not considered special taxes so long as the amount of the fee bears a reasonable relationship to the development's probable cost to the community and benefits to the developer. (*California Building Industry Assn. v. San Joaquin Valley Air Pollution Control District* (2009) 178 Cal.App.4th 120, 130.)

User (or service) fees are those that are charged to offset the cost of a government service. The distinguishing feature of a user fee is that those who pay the fee receive a benefit not received by those who do not pay. (*Isaac v. City of Los Angeles* (1998) 66 Cal.App.4th 586, 597 [a user fee is "payment for a specific commodity purchased"].) Such fees are charged only to the person actually using goods or services provided by the government. To be valid, the amount of the fee must be reasonably related to the cost of providing the goods or services for which the fee is imposed, and the fee must not be used for any purpose other than that for which the fee or charge was imposed. (*Ibid.*) Otherwise, the fee may constitute a tax. (See, e.g., *Beaumont Investors v. Beaumont-Cherry Valley Water Dis*t. (1985) 165 Cal.App.3d 227,235.)

A regulatory fee is a fee imposed under the police power to carry out regulatory activities. A regulatory fee is valid so long as (1) the primary purpose of the fee is regulation, not revenue; (2) there is a reasonable relationship between the fee and the payers' burdens on or benefits from the regulatory programs the fees support; (3) the amount collected does not exceed the reasonable costs of the regulatory programs for which the fees are charged. (See *California Farm Bureau Federation, supra,* 51 Cal.4th at pp.437-442; *Sinclair Paint, supra*, 15 Cal.4th at pp.876-880; *California Building Industry, supra,* 178 Cal.App.4th at pp.131-132.)

Case law has established that because regulatory fees are imposed under the police power, they are not dependent on government-conferred benefits or privileges. They may be imposed as part of a broader regulatory scheme for which the fee payer does not receive any perceived "benefit." For example, the State may impose industry-wide "remediation" or "mitigation" fees to defray the actual or anticipated adverse effects of an industry's business operations. (*Sinclair Paint, supra*, 15 Cal.4th at pp.877-878.) However, for regulatory fees to be valid, there must be a nexus between the fee and the payers' burdens on or benefits from the regulatory activity. (See *Morning Star Company v. Board of Equalization* (2011) 201 Cal.App.4th 737.)

A regulatory fee does not become a "tax" simply because the fee may be disproportionate to the service rendered to an individual fee payer. The proportionality of the fees -- i.e., whether fees exceed the cost of the regulatory program they are collected to support -- need not be proved on an individual basis. The question of proportionality is measured collectively, considering all the fee payers. (*California Assn. of Professional Scientists v. Dept. of Fish and Game* (2000) 79 Cal.App.4th 935, 948-950.) Fees are permissible if they are reasonably proportional to the overall costs of the regulatory program. (*Sinclair Paint, supra,* 15 Cal.4th at pp. 870, 878.)

In this case, the charges at issue do not fit squarely within any of the recognized fee classifications, although the charges have attributes in common with several of them.

For example, the charges are like a development fee in that they are used to mitigate impacts related to the fee payer's business operations. However, unlike a development fee, the charges are not imposed in return for the privilege of developing land, and the amount of the charge is not tied to the individual payer's impact on the community.

Like a user fee, those who purchase allowances receive something that is not received by those who do not pay -- a tradable right to emit GHG. However, unlike a user fee, the charges are not imposed to offset the cost of a government product or service.

Like a regulatory fee, the charges are collected as part of a regulatory program and the funds collected are used to carry out regulatory activities. However, unlike a traditional regulatory fee, the charges are not intended to shift the costs of a specific regulatory program. (ARB Opposition Brief, p.34.) According to ARB, the sales of allowances produce revenue not for the purpose of funding a regulatory program, but as a byproduct of a regulatory program. (*Id.* at p.35.) The proceeds of the sales will be used to pay for a wide range of (as-yet-undetermined) regulatory programs (ostensibly) related to AB 32.

ARB concedes that the charges do not fit within any of the traditional "fee" classifications. However, this is not dispositive. The courts have recognized that not all revenue-producing measures fit into the traditional fee classifications. (See *Bay Area Cellular, supra*, 162 Cal.App.4th at p.694; *California Taxpayers' Assn. v. Franchise Tax Bd.* (2010) 190 Cal.App.4th 1139, 1146.) This does not mean such charges are invalid. (*Id.* at p.694.) Revenue measures may be valid despite having attributes of more than one fee classification. (*Ibid.*) Likewise, certain revenue measures may be valid despite not having the attributes of any of the traditional fee classifications.[9]

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[9] California receives revenue from several sources. California's sources of revenue can be classified into five principal categories: intergovernmental transfers; loans; asset sales; taxes; and fees, charges, and other miscellaneous receipts. Taxes generally are collected in the General Fund and user fees generally are collected in Special Funds, although this is not always true. (While the General Fund is the State's main funding pool, both the General Fund and Special Funds are used to fund state operations. In recent years, as General Fund revenues and expenditures have declined, Special Fund revenues and expenditures have increased. As a result, Special Fund expenditures now account for a large percentage (about one-third) of total state expenditures.) The largest source of revenues is taxes, and the largest

ARB contends that even if the charges are somewhat different from traditional regulatory fees, the charges nevertheless should be upheld as valid "regulatory" fees or charges because the charges do not bear any of the traditional attributes of a tax, in that: (1) the charges were imposed for regulatory purposes and not for unrelated revenue purposes; (2) those who purchase allowances acquire a valuable benefit not enjoyed by others; (3) the charges are not compulsory; (4) the amount charged is determined by the market and not by government fiat; and (5) the proceeds will be used to further the regulatory purposes of AB 32 and cannot be used for the general support of the government.

On balance, the court agrees that the charges are more like traditional regulatory fees than taxes, but it is a close question.

Contrary to what ARB argues, the charges have some traditional attributes of a tax. First, the charges are not entirely voluntary. It is important to remember that the allowances have value to covered entities only because the government has forbidden covered entities from emitting GHG without an allowance.[10] The covered entity either must reduce its GHG emissions to zero -- which, generally speaking, is impractical or impossible -- or acquire allowances. Thus, from the perspective of a covered entity, the purchase of allowances is little different from an emissions tax. In the case of an emissions tax, covered entities obtain the right to emit GHGs by paying the tax; in the case of the cap-and-trade auction, they obtain this right by purchasing allowances.

Similarly, an allowance has no value independent of the regulatory scheme. While those who purchase allowances may be said to acquire a "benefit" vis-à-vis other covered entities, they do not acquire any "benefit" vis-à-vis other (non-covered) entities, which retain the right to freely emit GHGs without the need for acquiring any allowances.

Third, the amount charged is determined, at least in part, by government fiat. Although the auction relies on bidding, there is only one round of bidding, using sealed bids, and the auction operator will not accept bids that fall below a pre-set "auction reserve price." The auction reserve price is a "price floor" set by "government fiat." In addition, sales of allowances from the "containment reserve" are sold at prices fixed by the government. Moreover, by definition, the government has artificially constrained the supply of

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sources of tax revenues are sales and use taxes and personal and corporate income taxes, but the State also imposes many other taxes, including estate taxes, franchise taxes, financial institution taxes, insurance taxes, gasoline taxes, motor vehicle license taxes, cigarette taxes, alcoholic beverage taxes, hazardous substances taxes, property taxes, and utility taxes. In addition, the State collects various fees and charges, such as license fees, inspection fees, permit fees, examination fees, credential fees, filing fees, processing fees, waste disposal fees, park access or service fees, and beverage container redemption fees.

[10] Virtually every tax is in some sense "voluntary" in that one can avoid the tax by choosing not to engage in the taxed activity. Taken to its logical extreme, even income, sales, and property taxes would not be "compulsory" because they must be paid only if one "voluntarily" earns income, purchases goods, or owns property. Yet no one would dispute these are taxes.

allowances -- indeed, this is the very purpose of the "cap." Thus, it is not factually accurate for ARB to claim that the price of allowances is determined by the "market."[11]

Fourth, whether the allowance proceeds can be used for "general government purposes" depends on how one defines "general government purposes." Under the post-AB 32 legislation, the proceeds must be used to further AB 32's regulatory goal of reducing GHG emissions. However, since nearly every aspect of life has some impact on GHG emissions, it is difficult to conceive of a regulatory activity that will not have at least some impact on GHG emissions. For example, the Three-Year Investment Plan has identified numerous GHG reduction strategies, including such things as energy efficiency and weatherization retrofits, rail modernization, expanded transit and ridership programs, transit-oriented development and "livable community" strategies, water system use and efficiency, forests and eco-system management, recycling, reduction, and waste diversion, conservation easements, and agricultural management practices. (Chamber of Commerce's Request for Judicial Notice, Exh. C; see also AR Add-A-007585; see also Gov. Code § 16428.8 [authorizing the proceeds to be loaned to the General Fund, where the proceeds could be used for any governmental purpose].) Thus, in practice, the allowance proceeds likely can be used for "general government purposes."

On the other hand, the allowance charges also have attributes of a regulatory "mitigation" fee or charge.

To begin, those who purchase allowances receive a "tradable" right to emit GHGs, which has economic value and can be traded. If the atmosphere's capacity to assimilate GHGs is viewed as a limited public resource, selling emissions allowances can be analogized to selling a right to use a public resource, similar to a hunting/fishing license, a mineral extraction permit, or a wireless electromagnetic spectrum license.

In addition, the purchase of allowances is, in some respects, voluntary. Because covered entities receive a significant portion of the allowances for free, covered entities have some control over when, and perhaps if, they participate in sales of allowances. Covered entities may be able to reduce their GHG emissions to reduce or completely avoid their need to purchase additional allowances.[12] Further, covered entities are not compelled to purchase allowances from the government; they also may purchase allowances from other regulated entities. Some courts find this to be an important distinction. (See *Schmeer v. County of Los Angeles* (2013) 213 Cal.App.4th 1310, 1326-1327 [the term "tax" in ordinary usage refers to a compulsory payment remitted to the government or that raises revenue for the government].)

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[11] In any event, the method of determining the price of allowances is of questionable relevance. (See *Weekes v. City of Oakland* (1978) 21 Cal.3d 386, 396.) If the constitution prohibits selling allowances for a fixed price, it is unclear how the State could avoid this proscription simply by using auction pricing.

[12] This reduces, but does not eliminate, the compulsory aspects of the scheme. Covered entities still must reduce their emissions to match their freely-allocated allowances, or purchase additional allowances.

Finally, the price of allowances is determined at least in part by market forces, the proceeds of sales will be used to further the regulatory purposes of AB 32, and the charges were imposed (ostensibly, at least) for regulatory purposes.

In sum, the charges have some traditional attributes of a tax and some traditional attributes of a regulatory fee but, on balance, the court finds the charges to be more like a regulatory fee/charge than a traditional tax. Accordingly, the court shall review the charges using the regulatory fee framework.

As described above, the police power is broad enough to include mandatory remedial fees to defray the actual or anticipated adverse effects of the fee payers' business operations. Proposition 13's goal of providing effective tax relief is not subverted by shifting the costs of environmental protection to those who seek to impact our natural resources. (*Equilon Enterprises LLC v. Board of Equalization* (2010) 189 Cal.App.4th 865, 883.)

However, for a mitigation fee to be a valid regulatory fee and not a tax, the following requirements must be met: (1) the primary purpose (or intended effect) of the fee must be regulation, not revenue generation; (2) the total amount of fees collected cannot exceed the costs of the regulatory activities they support; and (3) there must be a reasonable relationship between the fees charged and the regulatory burden imposed by the fee payers' products or operations. (See *California Farm Bureau Federation, supra,* 51 Cal.4th at pp.437-442; *Sinclair Paint, supra*, 15 Cal.4th at pp.876-880; *California Building Industry, supra,* 178 Cal.App.4th at pp.131-132.)

The term "purpose" refers not to the subjective motivation of the legislators, but to the intended result or effect of the legislation, as determined using the well-established rules of statutory construction.[13] (See also *Davis v. San Diego* (1939) 33 Cal.App.2d 190, 193.) The legislative designation of a given levy or charge, though relevant, is not determinative of its nature. (*Weekes v. City of Oakland* (1978) 21 Cal.3d 386, 392.) The character of a given tax or fee must be ascertained by its incidents, and from the natural and legal effect of the language employed. (See *Ingels v. Riley* (1936) 5 Cal.2d 154, 159; see also *Nat'l Fed'n of Indep. Bus. v. Sebelius* (2012) 132 S. Ct. 2566, 2595 [disregarding the designation of the exaction and viewing its substance and application].) The motives of the legislative body are beyond the inquiry of the courts. (*Oakland Raiders, supra,* 65 Cal.App.3d at p.628; see also *Schroeder v. Irvine City Council* (2002) 97 Cal.App.4th 174, 192-193 [a court determines the validity of legislation based on the facial content or effect of the enactment, not by examining the subjective motivations or purposes of the legislators].)

Indeed, a chief motivation of many taxes is to influence conduct by imposing an economic impediment to the activity taxed. (*Sebelius, supra*, 132 S. Ct. at p.2596.) One obvious example is a tariff, which is a tax imposed on the value of imported

[13] The term "purpose" also may refer to the actual effect of the measure, as distinguished from its intended effect, if the actual and intended effects of a measure are different. This does not appear to be a problem in this case.

products, intended to raise the cost of foreign producers and thereby benefit domestic producers. No one would suggest that a tariff is a regulatory fee even if the "principal" motivation of the tariff is to influence conduct, rather than generate revenue. Similarly, federal and state taxes can compose more than half the retail price of cigarettes, but the charges do not cease to be taxes even if they were motivated by a desire to discourage people from smoking.

In addition, caution must be used in determining whether the "primary" purpose of a fee is "regulatory" or "revenue-raising" since the taxing power is often applied for regulatory purposes. (*Nat'l Fed'n of Indep. Bus. v. Sebelius* (2012) 132 S. Ct. 2566, 2596-2597.) Every tax is in some measure regulatory, and every regulatory fee is necessarily aimed at raising revenue. (*Sinclair Paint, supra*, 15 Cal.4th at p.880; *Oakland Raiders v. City of Berkeley* (1976) 65 Cal.App.3d 623, 628; *United States v. Sanchez* (1950) 340 U.S. 42, 44.) Indeed, many taxes seek to regulate conduct by raising revenue. However, a fee is not any less a fee because it raises revenue, and a tax is not any less a tax because it has a regulatory effect. All of this just goes to show that courts must proceed carefully when determining whether a measure's primary purpose is regulation or revenue.

In this case, the court is persuaded that the primary purpose of the charges is regulatory. The court does not ignore that ARB recognized that the sale of allowances will provide revenues that can be reinvested for public benefit. However, this does not appear to be the "primary" purpose of either the auction or reserve sales. Rather, the apparent "primary" purpose of selling allowances is to help the cap-and-trade program achieve its regulatory goals. As described by ARB, the sale of allowances helps the program achieve its regulatory goals by (i) increasing the cost of compliance and thereby stimulating early action to reduce emissions; (ii) equitably, transparently, and efficiently distributing allowances to new and established businesses; (iii) creating a transparent pricing signal to facilitate trading of allowances and minimize the risk of market manipulation; and, in the case of sales from the containment reserve, (iv) moderating the effect of unexpectedly short supply or high prices.

In addition, the post-AB 32 legislation restricts how the proceeds of sales will be used. Under the legislation, the proceeds must be used to further the regulatory purposes of AB 32.

Petitioners argue the post-AB 32 enactments themselves constitute the imposition of an "illegal tax" under Proposition 26. However, the post-AB 32 enactments only concern the use of the auction/sale proceeds; they do not cause "any taxpayer to pay a higher tax." Thus, Proposition 26 does not apply.

Petitioners also complain that the evidence shows selling allowances is not necessary to achieve the emissions reduction target of AB 32. However, even if selling allowances is not "necessary" to achieve AB 32's goals, selling allowances still may advance those goals.

The court also finds that the total amount of fees collected will not exceed the costs of the regulatory activities they support. Granted, this is an unusual case. Unlike a typical Sinclair-type regulatory fee, the charges at issue are not intended to shift the costs of any particular regulatory program or program. The costs of the cap-and-trade program will be recovered by the fees collected under § 38597. The proceeds of the sales of allowances will not be used to offset the costs of the cap-and-trade program, but to support additional regulatory programs that further the emissions reduction goals of AB 32. It is true that neither ARB nor this court currently know what those programs might be. However, because the proceeds can only be used to advance the regulatory purposes of AB 32, by definition, the total amount of fees collected will not exceed the costs of the regulatory programs they support.

The only remaining question is whether there is a sufficient nexus between the fees charged and the regulatory burden imposed by the fee payers' products or operations.

There is no clear test for determining when a fee is "reasonably related" to the adverse effects addressed by the regulatory activities for which the fee is charged.

In *Morning Star Company v. Board of Equalization*, the Court of Appeal considered a hazardous materials charge imposed on any business with 50 or more employees in the state that uses, generates, stores, or conducts activities related to hazardous materials. In its regulations, the Department of Toxic Substances Control concluded that "every" nonexempt business in California with 50 or more employees uses, generates, stores, or conducts activities in the state related to hazardous materials. Thus, virtually all businesses with 50 or more employees in the state are required to pay the hazardous materials charge. When collected, the charge, which ranges from hundreds to thousands of dollars, is deposited in the state's Toxic Substances Control Account, to be disbursed to various programs relating to the control of hazardous materials. (*Morning Star Company, supra*, 201 Cal.App.4th at pp.750-755.)

The Court held that the hazardous materials charge is a tax, rather than a regulatory fee. (*Morning Star Company v. Board of Equalization* (2011) 201 Cal.App.4th 737, 750-755.) The Court reasoned that the charge seeks to raise revenue for a wide range of governmental services and programs that are unrelated to the activities of the fee payers. In short, the Court concluded that the charge is not a "regulatory fee" because it raised money for the control of hazardous material generally, and not to regulate the fee payers' use, generation, or storage of hazardous material. (*Morning Star Company, supra*, 201 Cal.App.4th at p.755.) *Morning Star* suggests that a regulatory fee must directly relate to the payers' burdens on the regulatory activity.

The holding in *Morning Star* is somewhat difficult to reconcile with two other decisions issued by the same Court: *Equilon Enterprises LLC v. Board of Equalization* and *California Association of Professional Scientists v. Department of Fish and Game*. (See *Equilon Enterprises LLC v. Board of Equalization* (2010) 189 Cal.App.4th 865; *California Association of Professional Scientists v. Department of Fish and Game* (2000) 79 Cal. App.4th 935.)

In *Equilon Enterprises*, the Court upheld a regulatory fee imposed on industrial manufacturers deemed responsible for environmental lead contamination, to pay for a Childhood Lead Poisoning Prevention program. The Court rejected the argument that the fee must be proportional the fee payers' responsibility for cases of childhood lead poisoning since the program addresses, more broadly, the consequences of childhood lead exposure. (*Equilon Enterprises, supra*, 189 Cal.App.4th at p.885.) The Court stated that the regulatory fees validly require manufacturers and others whose products have exposed children to lead contamination to bear a fair share of the cost of mitigating the adverse health effects their products created in the community. (*Id.* at p.886.)

In *California Association of Professional Scientists v. Department of Fish and Game* ["*CAPS*"], Court upheld the constitutionality of a flat fee imposed on those submitting project proposals to the Department of Fish and Game to defray the costs incurred in meeting its environmental review obligations. The Court held that a flat fee system is a reasonable means to allocate the costs of environmental review. The Court held that as long as the cumulative amount of the fees does not surpass the cost of the regulatory program, and cost allocations to individual payers have a reasonable basis in the record, a fee does not become a tax simply because the fee exceeds the individual payer's burdens on the regulatory program. (*CAPS, supra*, 79 Cal.App.4th at pp.947-950.)

Under the reasoning of *Equilon Enterprises* and *CAPS*, if every business in California with 50 or more employees uses, generates, stores, or conducts activities related to hazardous materials, as the Department had found in that case, the constitution should not prevent the Department from collecting a hazardous waste fee to address the harmful effects of hazardous waste contamination. However, in *Morning Star*, the Court concluded that the charge imposed is a tax, rather than a regulatory fee, because it pays for "the remediation, cleanup, disposal and control of hazardous materials generally, rather than for the regulation of [the] payers' business activities . . . ." (*Morning Star, supra*, 201 Cal.App.4th at p.755.)

However, none of the cited cases are directly on point with the facts of this case. ARB's sales of allowances are unlike the taxes and fees that have previously come before the courts. Unlike a traditional *Sinclair*-type fee, the allowance charges are not intended to shift the costs of a particular regulatory program to those responsible for the problem that the program was created to address. Rather, the charges are a byproduct of the implementation of a regulatory program. The proceeds are received in exchange for the purchase of a tradable right to emit GHGs. Participants bid because allowances have value and their bids (presumably) will not exceed the value they expect to receive from those allowances.[14] The revenues received in exchange for the sale of allowances are pledged to be spent in furtherance of the goals of the regulatory program.

[14] Admittedly, the allowances have value only because of the regulatory program.

Under the unique circumstances of this case, the court is not persuaded that the amounts charged for allowances must be closely linked to the payers' burdens on the specific regulatory programs that will be funded by them. Rather, all that is required is a reasonable relationship between the charges and the covered entities' (collective) responsibility for the harmful effects of GHG emissions. As the State's largest sources of GHG emissions, the court is persuaded that a reasonable relationship exists.

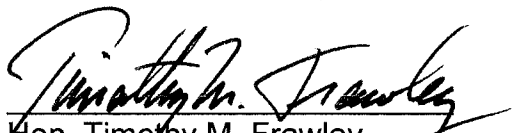
Accordingly, the court shall deny the petition.

Disposition

The court shall issue separate judgments denying the petitions. Counsel for Respondent ARB is directed to prepare formal judgments, incorporating this ruling as an exhibit; submit them to opposing counsel for approval as to form; and thereafter submit them to the court for signature and entry of judgment.

Pursuant to Government Code section 6103.5, Respondents shall be entitled to recover the amount of any fees they would have been charged had it not been for the provisions of Section 6103. If collected, such amounts shall be due and payable to the clerk of the court. If the public agency determines not to seek collection of the filing fee, it shall so notify the clerk.

Dated: November 12, 2013



Hon. Timothy M. Frawley
California Superior Court Judge
County of Sacramento

CERTIFICATE OF SERVICE BY MAILING
(C.C.P. Sec. 1013a(4))

I, the Clerk of the Superior Court of California, County of Sacramento, certify that I am not a party to this cause, and on the date shown below I served the foregoing JONIT RULING ON SUBMITTED MATTERS by depositing true copies thereof, enclosed in separate, sealed envelopes with the postage fully prepaid, in the United States Mail at Sacramento, California, each of which envelopes was addressed to:

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I, the undersigned deputy clerk, declare under penalty of perjury that the foregoing is true and correct.

Dated: November 12, 2013

By: F. Temmerman,
Deputy Clerk, Dept.29

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