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# COURT OF APPEAL OF CALIFORNIA
# THIRD APPELLATE DISTRICT

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| CALIFORNIA CHAMBER OF COMMERCE, et al.,<br>Plaintiffs and Appellants,<br>v.<br>CALIFORNIA AIR RESOURCES BOARD, et al.,<br>Defendants and Respondents,<br>NATIONAL ASSOCIATION OF MANUFACTURERS,<br>Intervener and Appellant;<br>ENVIRONMENTAL DEFENSE FUND, et al.,<br>Interveners and Respondents. | Case No. C075930<br><br>Sacramento County<br>No. 34201280001313<br>CUWMGDS<br><br>Hon. Timothy M. Frawley |

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| MORNING STAR PACKING COMPANY, et al.,<br>Plaintiffs and Appellants,<br>v.<br>CALIFORNIA AIR RESOURCES BOARD, et al.,<br>Defendants and Respondents,<br>ENVIRONMENTAL DEFENSE FUND, et al.,<br>Interveners and Respondents. | Case No. C075954<br><br>Sacramento County<br>No. 34201280001464<br>CUWMGDS<br><br>Hon. Timothy M. Frawley |

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# CALIFORNIA CHAMBER OF COMMERCE, et al.
# APPELLANTS' OPENING BRIEF

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NIELSEN MERKSAMER PARRINELLO
GROSS & LEONI, LLP
*JAMES R. PARRINELLO (SBN 063415)
2350 Kerner Blvd., Suite 250
San Rafael, CA 94901
Telephone: (415) 389-6800
Fax: (415) 388-6874
jparrinello@nmgovlaw.com

NIELSEN MERKSAMER PARRINELLO
GROSS & LEONI, LLP
STEVEN A. MERKSAMER (SBN 66838)
KURT R. ONETO (SBN 248301)
1415 L Street, Suite 1200
Sacramento, CA 95814
Telephone: (916) 446-6752
Fax: (916) 446-6106

*Attorneys for Plaintiffs and Appellants*
*CALIFORNIA CHAMBER OF COMMERCE, et al.*

[Additional counsel listed on following page]

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San Rafael, CA 94901
Telephone: (415) 389-6800
Fax: (415) 388-6874
jparrinello@nmgovlaw.com

NIELSEN MERKSAMER PARRINELLO
GROSS & LEONI, LLP
STEVEN A. MERKSAMER (SBN 66838)
KURT R. ONETO (SBN 248301)
1415 L Street, Suite 1200
Sacramento, CA 95814
Telephone: (916) 446-6752
Fax: (916) 446-6106

*Attorneys for Plaintiffs and Appellants*
*CALIFORNIA CHAMBER OF COMMERCE, et al.*

[Additional counsel listed on following page]

| | |
|---|---|
| Roger R. Martella (pro hac vice)<br>*Paul J. Zidlicky (pro hac vice)<br>Eric McArthur (pro hac vice)<br>Sidley Austin LLP<br>1501 K Street NW<br>Washington, DC 20005<br>pzidlicky@sidley.com<br><br>Attorneys for Intervener & Appellant<br>*National Association of Manufacturers* | *Theodore Hadzi-Antich (SBN 264663)<br>James S. Burling (SBN 113013)<br>Pacific Legal Foundation<br>930 G Street<br>Sacramento, CA 95814<br>Tel.: (916) 419-7111<br>tha@pacificlegal.org<br><br>Attorneys for Plaintiffs & Appellants<br>*Morning Star Packing Company, et al.* |
| *Sean A. Commons (SBN 217603)<br>Sidley Austin LLP<br>555 West Fifth Street<br>Los Angeles, CA 90013<br>Tel: (213) 896-6600<br>scommons@sidley.com<br><br>Attorneys for Intervener & Appellant<br>*National Association of Manufacturers* | Robert E. Asperger (SBN 116319)<br>Deputy Attorney General<br>1300 I Street<br>Sacramento, CA 95814<br>Tel. (916) 327-7582<br>Bob.Asperger@doj.ca.gov<br><br>Attorneys for Defendants & Respondents<br>*California Air Resources Board, et al* |
| *David A. Zonana (SBN 196029)<br>M. Elaine Meckenstock (SBN 268861)<br>Bryant B. Cannon (SB N 284496)<br>Deputy Attorneys General<br>California Department of Justice<br>1515 Clay Street, Suite 2000<br>P.O. Box 70550<br>Oakland, CA 94612-0550<br>Tel.: (510) 622-2145<br>David.Zonana@doj.ca.gov<br><br>Attorneys for Defendants & Respondents<br>*California Air Resources Board, et al.* | *Matthew D. Zinn (SBN 214587)<br>Joseph D. Petta (SBN 286665)<br>Shute, Mihaly & Weinberger, LLP<br>396 Hayes Street<br>San Francisco, CA 94102<br>Tel.: (415) 552-7272<br>Zinn@smwlaw.com<br><br>Attorneys for Interveners & Respondents<br>*Environmental Defense Fund* |
| *Erica Morehouse Martin (SBN 274988)<br>Timothy J. O'Connor (SBN 250490)<br>Environmental Defense Fund<br>1107 9th Street, Suite 1070<br>Sacramento, CA 95814<br>Tel.: (916) 492-4680<br>emorehouse@edf.org<br><br>Attorneys for Interveners & Respondents<br>*Environmental Defense Fund* | David Pettit (SBN 067128)<br>*Alexander L. Jackson (SBN 267099)<br>Natural Resources Defense Council<br>1314 2nd Street<br>Santa Monica, CA 90401<br>Tel.: (310) 434-2300<br>ajackson@nrdc.org<br><br>Attorneys for Interveners & Respondents<br>*Natural Resources Defense Council* |

**TO BE FILED IN THE COURT OF APPEAL**

**APP-008**

| COURT OF APPEAL, THIRD APPELLATE DISTRICT, DIVISION | Court of Appeal Case Number: C075930 |
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| ATTORNEY OR PARTY WITHOUT ATTORNEY *(Name, State Bar number, and address)*:<br>James R. Parrinello, State Bar # 063415<br>Nielsen Merksamer Parrinello Gross & Leoni, LLP<br>2350 Kerner Blvd., Suite 250<br>San Rafael, CA 94901<br>TELEPHONE NO.: 415.389.6800 FAX NO. *(Optional)*: 415.388.6874<br>E-MAIL ADDRESS *(Optional)*: jparrinello@nmgovlaw.com<br>ATTORNEY FOR *(Name)*: Appellants California Chamber of Commerce, et al. | Superior Court Case Number:<br><br>*FOR COURT USE ONLY* |
| APPELLANT/PETITIONER: California Chamber of Commerce, et al.<br><br>RESPONDENT/REAL PARTY IN INTEREST: California Air Resources Bd., et al. | |
| **CERTIFICATE OF INTERESTED ENTITIES OR PERSONS**<br>*(Check one)*: ☑ INITIAL CERTIFICATE ☐ SUPPLEMENTAL CERTIFICATE | |

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1. This form is being submitted on behalf of the following party (*name*): California Chamber of Commerce and Larry Dicke

2. a. ☒ There are no interested entities or persons that must be listed in this certificate under rule 8.208.

   b. ☐ Interested entities or persons required to be listed under rule 8.208 are as follows:

| Full name of interested entity or person | Nature of interest *(Explain):* |
|---|---|
| (1) | |
| (2) | |
| (3) | |
| (4) | |
| (5) | |

☐ Continued on attachment 2.

**The undersigned certifies that the above-listed persons or entities (corporations, partnerships, firms, or any other association, but not including government entities or their agencies) have either (1) an ownership interest of 10 percent or more in the party if it is an entity; or (2) a financial or other interest in the outcome of the proceeding that the justices should consider in determining whether to disqualify themselves, as defined in rule 8.208(e)(2).**

Date: October 17, 2014

JAMES R. PARRINELLO
(TYPE OR PRINT NAME)

▶ _____
(SIGNATURE OF PARTY OR ATTORNEY)



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## I. INTRODUCTION AND SUMMARY OF ARGUMENT

This lawsuit addresses only one component of the regulatory program adopted by California's Air Resources Board following the Legislature's enactment of Assembly Bill 32 to reduce greenhouse gas (GHG) emissions. The lawsuit does not challenge the merits of climate change science; it does not challenge the Legislature's authority to regulate GHG emissions in California; and it does not challenge the Board's decision to use a "cap and trade" method of reducing GHG emissions by placing a limit on the aggregate GHG emissions of covered entities, then issuing an emissions allowance for each covered entity but allowing an entity to increase its GHG emissions by acquiring additional allowances from other entities that "trade" part of their allowances for compensation. The only thing challenged is the part of the Board's regulatory program that allows the Board to allocate GHG allowances to itself and then sell the allowances to GHG emitters, thereby raising tens of billions of dollars of revenue for the state.

The challenged action by an unelected, politically-appointed state board to engraft into a regulatory program a massive revenue-raising device is unlawful because it exceeds the authority granted to the Board by AB 32 and it imposes what is an invalid tax.

Absent from AB 32 is any language giving the Air Resources Board the unprecedented authority to raise tens of billions of dollars of state revenue by withholding and auctioning off a percentage of the statewide GHG emissions allowances adopted by the Board. (See *American Federation of Labor v. Unemployment Ins. Appeals Bd.* (1996) 13 Cal.4th 1017, 1042 [an administrative agency has only the powers conferred on it by statute or by the Constitution].) The only money-making power that AB 32 conferred on the Board is the

authority to charge a regulatory fee limited to covering the ordinary administrative costs of implementing the GHG emissions regulatory program. (Health & Safety Code, § 38597.)

The fact that AB 32 explicitly allows the Board to impose a limited regulatory fee for ordinary administrative costs, but contains no language explicitly authorizing the Board to withhold and then auction off GHG emissions allowances for billions of dollars, indicates the Legislature did not intend to give the Board the novel and incredible power to adopt regulations to raise massive revenue for purposes other than the ordinary costs of administering the regulatory program.

And the legislative history of AB 32 reflects nothing that could be construed to support the granting of such massive revenue-raising authority. The bill's findings and declarations, and the seven legislative reports and analyses of the bill, make no mention of any such authority. To the contrary, the enrolled bill report *prepared by the Air Resource Board* explicitly noted AB 32 authorizes only fees necessary to support essential, direct program costs. Likewise, the bill signing letter *the Board prepared* for the Governor's signature emphasized that any fees collected from sources of GHG emissions would be used only to support essential and directs program costs associated with the bill.

Equally telling is the fact that when, during floor debate, legislators asked whether AB 32 would give the Board unlimited authority to impose a broad range of charges, the Speaker of the Assembly (and the bill's author) emphatically assured them that the bill authorized the Board to impose only a limited, narrow charge for program administration and costs. At this point debate ended, and the bill was passed.

Anyone remotely familiar with the Legislature knows that if AB 32 was intended to allow the Board to raise tens of billions of dollars of state revenue on the backs of a small sector of California's business community, there would have been more vigorous legislative debate and substantial opposition to AB 32. Yet, after legislators were assured the bill authorized only a limited administrative fee, debate ceased – obviously because it was understood that AB 32 was not intended to allow the Board to implement the unprecedented billions of dollars revenue-raising program it later did.

There is another separate and independent reason why AB 32 cannot be read to authorize the Board to raise billions of dollars of state revenue by withholding for itself a percentage of the GHG emissions allowances and then auctioning them off to the highest bidders. Such a charge for emission allowances constitutes a tax that is unconstitutional because it was not passed by a two-thirds vote in each house of the Legislature; and courts must presume that the Legislature did not intend to violate the Constitution.

The California Supreme's Court's decision in *Sinclair Paint Co. v. State Bd. of Equalization* (1997) 15 Cal.4th 866 sets forth the test whether a charge imposed by the state as part of an environmental regulatory program is a fee or a tax. If the charge (1) bears a reasonable relationship between the amount charged and the burdens imposed by the fee payer's operations, (2) the charge is not used for unrelated revenue purposes, and (3) the remedial measures funded with the charge have a causal connection or nexus to the fee payer's operations, then the charge is a regulatory fee. If the charge is lacking in *any* of those respects, it is a tax.

As explained in detail in this brief, the charge a GHG emitter covered by the administrative program must pay to the Board to acquire additional GHG emissions allowances does not meet the requirements to be a lawful regulatory fee. Simply stated, the amount of the auction charges lacks a reasonable relationship to the burdens posed by the payers' operations, the charges are used for unrelated revenue purposes, and the broad programs funded have no causal connection to the business activities of the payers. Consequently, the charges constitute taxes that are unlawful because they were not passed by a two-thirds vote in each house of the Legislature.

In sum, because the massive state-revenue-raising-device the Board engrafted into the regulatory program exceeds the authority granted to the Board by AB 32, and/or because it imposes an invalid tax, the judgment of the Superior Court upholding the charges must be reversed.

## II. PROCEDURAL BACKGROUND AND STATEMENT OF THE CASE

Procedural History.

California Chamber of Commerce, et al. v. California Air Resources Board, et al., action no. 34-2012-80001313. Appellants California Chamber of Commerce and Larry Dicke ("CalChamber") filed their verified complaint on November 13, 2012. The California Air Resources Board ("ARB") and its executive director and board members were named as respondents (sometimes collectively referred to as "ARB").

The complaint challenged the legality of ARB regulations 17 CCR sections 95870 and 95910 – 95914, which impose massive

financial burdens on a small segment of California's business community and raise tens of billions of dollars of state revenue. The petition alleged the regulations were *ultra vires* and not authorized by AB 32; and the regulations impose a tax not enacted by a 2/3 vote in each house of the Legislature, in violation of Cal. Const. article XIIIA. (Joint Appendix filed herewith ("JA") 0001-0010.)

ARB's answer generally denied the allegations. (JA 0248-0255.)

The National Association of Manufacturers ("NAM") intervened on behalf of petitioners and the Environmental Defense Fund ("EDF") and Natural Resources Defense Council ("NRDC") intervened on behalf of respondents. (JA 0307-0324; JA 0262-0294.)

Morning Star Packing Co., et al. v. ARB, action No. 34-2013-80001464. Appellants Morning Star Packing Co., et al., ("Morning Star") filed their verified complaint on April 16, 2013, naming the same respondents, and challenging ARB regulations 17 CCR sections 95830 – 95834, 95870 and 95910 – 95914, on substantially the same grounds as CalChamber. (JA 0549-0572.)

The CalChamber and Morning Star cases were deemed related and assigned to Judge Timothy F. Frawley. (JA 0579-0581.)

The CalChamber and Morning Star cases were argued together in a several hour hearing in the Superior Court on August 28, 2013. (Reporters Transcript dated 8/28/13 ("RT") at pp. 1-75.)

The Superior Court issued its Joint Ruling on Submitted Matters ("Ruling") on November 12, 2013, upholding the regulations. (JA 1566-1588.)

Judgment was entered in both cases on December 20, 2013; the Ruling was attached and its reasoning adopted. (JA 1589-1617; JA 1618-1645.)

Notices of Entry of Judgment were served in both cases on January 9, 2014. (JA 1646-1680; JA 1681-1714.)

Timely notices of appeal were filed. (JA 1738-1741; JA 1742-1745; JA 1746-1779.)

This Court consolidated the CalChamber and Morning Star cases. (JA 1953-1983.) The parties stipulated to the JA. (JA 1953-1983.)

Factual Background.

AB 32 was approved by majority vote in both houses of the Legislature in August 2006. (JA 107.) On September 27, 2006, the Governor signed AB 32 into law. Statutes 2006, chapter 488, Health and Safety Code sections 38500 - 38599.

AB 32's stated objective is to reduce GHG emissions in the state to 1990 levels by 2020. (Section 38550.)[1] The Legislative Counsel's Digest states: "The bill would require the state board [ARB] to adopt a statewide greenhouse gas emissions limit equivalent to the statewide greenhouse gas emissions levels in 1990 to be achieved by 2020, as specified." [2]

AB 32 requires the ARB to: (1) implement a GHG emissions monitoring program (Section 38530); (2) determine what the statewide GHG emissions level was in 1990, and then achieve that

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[1] Unless otherwise indicated, "section(s)" refers to the Health & Safety Code.

[2] ARB's Administrative Record ("AR") at A-000001.

level by 2020 (Section 38550); and (3) adopt a regulatory program to achieve the required GHG reductions in the "maximum technologically feasible and cost-effective" way. (Sections 38560 & 38562.)

In designing regulations, the ARB was authorized to consider "direct emission reduction measures, alternative compliance mechanisms, market-based compliance mechanisms, and potential monetary and nonmonetary incentives for sources" in order achieve "the maximum feasible and cost-effective reductions of greenhouse gas emissions by 2020." (Section 38561(b).)

A "market-based compliance mechanism" means either:

> (1) A system of market-based declining annual aggregate emissions limitations for sources or categories of sources that emit greenhouse gases.
>
> (2) Greenhouse gas emissions exchanges, banking, credits, and other transactions, governed by rules and protocols established by the state board, that result in the same greenhouse gas emission reduction, over the same time period, as direct compliance with a greenhouse gas emission limit or emission reduction measure adopted by the state board pursuant to this division.

(Section 38505(k).)

AB 32 required the regulations to be operative by January 1, 2012. (Section 38562(a).) In adopting regulations, the ARB was directed to minimize costs, consider the cost effectiveness of the regulations and minimize the administrative burden of complying with the regulations. (Sections 38562(b)(1), (5) & (7).)

The only revenue-raising authority mentioned in AB 32 is in section 38597, which authorizes the ARB to adopt "a schedule of fees

to be paid by the sources of greenhouse gas emissions" to pay program administration costs.[3]

The Regulations In Dispute. On January 1, 2012, the ARB's regulations went into effect. (Cal. Code Regs., Tit. 17, Div. 3, Ch. 1, Subch. 10, Art. 5 [§ 95801 et seq].)

The regulations impose a "cap and trade" system, placing a cap on GHG emissions from entities that emit at least 25,000 metric tons of GHG per year. (17 CCR, §§ 95810-95814.) These entities are "covered entities." (17 CCR, §§ 95802(a); 95811; & 95812.)[4]

Under the regulations, the ARB issues "allowances," each of which gives the holder the right to emit one ton of carbon dioxide equivalent. (17 CCR, §§ 95802(a)(8), (41), & (55); see also section 38505(a).) A covered entity must possess, and then surrender back to the ARB, one allowance for each ton of carbon dioxide emissions it produces within a given compliance period. (17 CCR, § 95856.) There are three compliance periods: 2013-14, 2015-17, and 2018-20. (17 CCR, § 95840.) The cap declines during each compliance period, reducing statewide emissions. (17 CCR, §§ 95811-12; 95841; & 95850-58.)

GHG allowances are not "property or a property right" but are tradable. (17 CCR, §§ 95802(a)(8); 95820(c); & 95921.) A covered entity may increase its GHG emissions by acquiring additional

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[3] The costs are limited and must be consistent with Health and Safety Code section 57001, the California EPA's fee accountability program.

[4] Covered industries include petroleum refining, cement production, cogeneration, glass production, hydrogen production, iron and steel production, petroleum and natural gas systems, electricity generating facilities, pulp and paper manufacturing, and other consumers and suppliers of electricity, natural gas, and petroleum. (17 CCR, § 95811.)

allowances from other covered entities without increasing overall statewide GHG emissions since the total number of allowances is capped.[5] This declining "cap" on the allowances in circulation, along with the ability to "trade" allowances among covered entities, are features of a cap and trade program.

Greatly expanding authority granted to it by AB 32, the ARB adopted additional regulations empowering itself to undertake an unprecedented, multi-billion dollar revenue-generating program. It allocated to itself a substantial portion of the allowances in order to sell them to the highest bidders to generate state revenue. (17 CCR, §§ 95870, 95910-95914.) The regulations initially directed the revenue to the Air Pollution Control Fund and now to the Greenhouse Gas Reduction Fund. (17 CCR §§ 95912(k) and 95913(i).)[6]

The ARB initially allocated to itself 10% of all allowances issued, and between 2012 and 2020, the ARB allocates to itself approximately half of all GHG allowances. (17 CCR, §§ 95870 & 95910.)

During the regulatory process, the ARB acknowledged "Traditionally, cap and trade programs have favored freely allocating allowances to the covered entities." (JA 0235.) ARB cited no instance of a cap and trade program auctioning emissions allowances to generate government revenue, let alone tens of billions of dollars.

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[5] The rules applicable to trading GHG allowances are in 17 CCR, §§ 95920 and 95921.

[6] To spend this windfall, the Legislature in 2012 adopted Stats. 2012, ch. 39, § 25 (SB 1018) which created a "Greenhouse Gas Reduction Fund" and required all moneys collected from auctions to be deposited into that fund "for appropriation by the Legislature." (Gov. Code, § 16428.8(a) & (b).) More on this later.

The ARB's initial auction of allowances occurred in November 2012; quarterly auctions have occurred since. (17 CCR, § 95910.) These auctions have generated over $831 million in state revenue,[7] which will increase substantially as self-allocated allowances increase.

As discussed herein, these revenues are being appropriated for general governmental purposes such as the bullet train, transportation, affordable housing, agricultural energy and operational efficiency, water efficiency, wetlands restoration, sustainable forests, and waste diversion.

The Legislative Analyst's Office ("LAO") estimates the ARB's auctions will produce $12 billion to $70+ billion in revenue for the state by 2020. (JA 0082.) This is one of the largest revenue-generating programs in state history. Nothing in the legislative history of AB 32 suggests that revenue generation was a purpose of the bill.

AB 32's objective to reduce GHG emissions to 1990 levels by 2020 can be achieved without the challenged revenue-raising regulations. (JA 0238, 0242-0244, 0235.) The ARB does not dispute this.

## III. STANDARD OF REVIEW

This case involves issues of law: whether the ARB's revenue-raising regulations are *ultra vires*; and whether they constitute an unconstitutional tax.

Statutory interpretation is a question of law which the Court decides *de novo*. (*Regents of Univ. of Calif. v. East Bay Mun. Utility Dist.* (2005) 130 Cal.App.4th 1361, 1372; *Environmental Defense*

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[7] http://www.arb.ca.gov/cc/capandtrade/auction/auction_archive.htm (Last visited 10/14/14.)

*Project of Sierra County v. County of Sierra* (2008) 158 Cal.App.4th 877, 889.) Furthermore, in considering whether the ARB has acted *ultra vires*, the ARB's interpretation of AB 32 is entitled to no deference. (*Citizens to Save California v. California Fair Political Practices Commission* (2006) 145 Cal.App.4th 736 at pp. 747, 748-754 ("*Citizens to Save California*").)

Whether the disputed regulations impose an unconstitutional tax is likewise reviewed *de novo*. (*Professional Engineers in California Government v. Kempton* (2007) 40 Cal.4th 1016, 1032.)

Finally, a statute must be construed so as to avoid serious constitutional question. (*Dyna-Med, Inc. v. Fair Emp. & Housing Com.* (1987) 43 Cal.3d 1379, 1387.) Thus if a statute is reasonably susceptible of two constructions, one of which will render the statute constitutional and the other will raise constitutional questions, the construction that will render the statute free from doubt as to its constitutionality must be adopted, even if the other construction might also be reasonable. (*Harrott v. County of Kings* (2001) 25 Cal.4th 1138, 1153; *Miller v. Municipal Ct. of the City of Los Angeles* (1943) 22 Cal.2d 818, 828.)

## IV. ARGUMENT

### A. The Legislature Did Not Authorize The ARB To Raise Billions of Dollars In Revenue – Had That Been AB 32's Intent, There Would Have Been A Huge And Bitter Fight In The Legislature.

The ARB regulations at issue are unprecedented. Never before has an unelected regulatory board imposed regulations that will generate $12 billion to $70 billion in revenue over eight years – a sum that would be the fourth single largest state funding source,

after the personal income tax, the sales and use tax, and the corporate income tax. (JA 0205-0211.)

History has shown that legislative efforts to raise large amounts of revenue have generated contentious debate and vigorous opposition. In 2012, for example, there was major debate over Proposition 30, which increased sales and use and income taxes to generate $6 billion a year in revenue for five years. (JA 0196-0203.) Because the Legislature declined even to submit such a tax increase measure for voter approval, the Governor had to qualify Proposition 30 for the ballot by gathering hundreds of thousands of initiative petition signatures.

There was no such vigorous debate and opposition to AB 32 on the ground that it would allow the ARB to raise tens of billions of dollars of revenue on the backs of a small sector of the State's business community. This is so because AB 32 does not express any intent to grant such unprecedented authority to the ARB.

If the Legislature intended to give the ARB the authority to raise billions of dollars of revenue:

- there would be words in AB 32 expressly granting such authority. But there are none.
- there would be words in AB 32's findings and declarations discussing such authority. But there are none.
- there would be mention in the Legislative Counsel's Digest of such authority. But there is none.

- there would be mention of such authority in AB 32's committee reports, bill analyses or other legislative history. But there is none.[8]

As anyone remotely familiar with the Legislature would know, it defies belief that the Legislature intended to authorize the ARB's massive revenue-raising program by stealth and without any public disclosure or heated debate.

In fact, both the ARB and the Speaker of the Assembly assured the Legislature and the Governor that the only revenue authorized by AB 32 would be the administrative fees necessary to cover the essential, direct program costs to implement the bill.

Accordingly, for these and other reasons explained below, this Court should conclude that the ARB exceeded its authority in promulgating regulations to raise billions of dollars of revenue through the sale of GHG allowances.

### 1. The Legislature passed AB 32 to reduce greenhouse gas emissions; nothing in the statute mentions creating a multi-billion dollar revenue raising program.

Findings and declarations or other statements of intent included in a statute assist in determining the scope and meaning of statutes. (*Palos Verdes Faculty Assoc. v. Palos Verdes Unified Sch. Dist.* (1978) 21 Cal.3d 650, 658-659.) The Legislature inserted substantial findings and declarations in AB 32. (Section 38501.) There is no mention of any intent to raise billions of dollars in

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[8] As noted above, the only fees authorized by AB 32 are the small sums needed to cover program administrative costs. (Section 38597.)

revenue. They focus exclusively on the potential harms posed by GHG and the need to reduce those potential adverse effects.

The Legislature found, for example, that global warming poses a threat to California's environment, economy, and public health (section 38501(a)); global warming will adversely impact important California industries (section 38501(b)); California has long been an international leader in environmental stewardship, and AB 32 will continue this tradition (section 38501(c)); action taken by California to reduce GHG emissions will encourage other governments to act to similarly (section 38501(d)); by exercising a global leadership role, California's economy will benefit from national and international efforts to reduce GHG emissions (section 38501(e)); and the ARB should design GHG emission reduction measures in a manner that minimizes costs and maximizes benefits to California's economy (section 38501(h)).

Nothing in the findings and declarations indicates the Legislature intended to authorize the ARB to construct a massive revenue program.

**2. AB 32's legislative history makes no mention of authorizing a multi-billion dollar revenue raising program.**

Seven separate legislative reports and analyses were prepared on AB 32.[9] There is not a word in any report about creating or

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[9] **(1)** Assem. Com. on Nat. Res., analysis of Assem. Bill No. 32 (2005-06 Reg. Sess.); **(2)** Assem. Com. on Appropriations, analysis of Assem. Bill No. 32 (2005-06 Reg. Sess.); **(3)** Assem. Floor Analysis, analysis of Assem. Bill No. 32 (2005-06 Reg. Sess.); **(4)** Sen. Com. on Environmental Quality, analysis of Assem. Bill No. 32 (2005-06 Reg. Sess.); **(5)** Sen. Com. on Appropriations, analysis of Assem. Bill No. 32 (2005-06 Reg. Sess.); **(6)** Sen. Com. on Rules, Ofc. of Floor Analyses, 3d reading analysis of Assem. Bill No. 32

authorizing a massive revenue-raising program.[10]

This silence is instructive. "Statements in legislative committee reports concerning the statutory objects and purposes which are in accord with a reasonable interpretation of the statute are legitimate aids in determining legislative intent." (*So. Calif. Gas Co. v. Public Util. Com.* (1979) 24 Cal.3d 653, 659; *National R.V., Inc. v. Foreman* (1995) 34 Cal.App.4th 1072, 1083.) "It will be presumed that the Legislature adopted the proposed legislation with the intent and meaning expressed in committee reports." (*Curtis v. County of Los Angeles* (1985) 172 Cal.App.3d 1243, 1250.)

If the Legislature intended to authorize the ARB to undertake a massive revenue raising program, AB 32 would have said so. It did not, and the legislative history says absolutely nothing that even remotely suggests AB 32 intended to give the ARB such a green light. Indeed, as discussed *post*, the legislative history plainly shows the ARB and the Speaker of the Assembly explicitly acknowledged that AB 32 authorized only fees necessary to support essential, direct program costs.

This disavowal of revenue-raising intent and the absence of explicit authorization for such fundraising, coupled with the absence of debate and opposition that otherwise would have been expected, compel the conclusion that it is wrong and absurd to read into AB 32 a grant of authority for the ARB to develop and implement a method

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(2005-06 Reg. Sess.); and (7) Assembly Floor Analysis, Concurrence in Senate Amendments to Assem. Bill No. 32 (2005-06 Reg. Sess.). (JA 0117-0155.)

[10] The only revenue raising discussed is that AB 32 "[a]uthorizes ARB to adopt a schedule of fees to pay for the costs of implementing the program established pursuant to the bill's provisions." (JA 0142.)

to raise billions of dollars of revenue from a small sector of California's business community.

### 3. The ARB's Enrolled Bill Report to the Governor makes no mention of any grant of authority to create a multi-billion dollar revenue raising program – to the contrary, the ARB conceded AB 32 allowed it to impose only fees limited to the direct costs of implementing the program authorized by the bill.

Shortly after AB 32 was passed by the Legislature, the ARB sent its Enrolled Bill Report to then-Governor Schwarzenegger, recommending the Governor sign the bill. (JA 0157-0171.)[11] This report is significant and bears careful study.

Nothing in the Enrolled Bill Report says or implies that AB 32 authorizes the ARB to adopt any state revenue-raising program, let alone a program on the massive scale subsequently adopted. In discussing the "Fee Authority" authorized by the bill, the Report emphasizes that the ARB's authority to impose fees on the sources of GHG emissions is very narrow:

> Fee Authority. AB 32 grants ARB the authority to adopt a schedule of fees to be paid by regulated GHG emission sources for program administration. Republicans feel that the fee authority language provides ARB with carte blanche authority to collect fees on anything including imposing a tax on sport utility vehicles (SUV). To clear confusion, Speaker Nunez added a letter to the file to clarify that **the fee is limited to ARB's direct implementation costs only**.

(Emphasis added; JA 0159.) The ARB's Report discusses no other "fee authority." It thus advised the Governor that the only fees

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[11] The ARB's report is part of AB 32's legislative history. *Conservatorship of Whitley* (2010) 50 Cal.4th 1206, 1218, fn. 3 ["'[W]e have routinely found enrolled bill reports, prepared by a responsible agency contemporaneous with passage and before signing, instructive on matters of legislative intent.' [Citations]"].)

authorized by the bill are those to pay for direct program implementation costs.

The ARB's Enrolled Bill Report also contains a section titled "Fiscal Impact." (JA 0163.) Nothing in this section states that AB 32 authorizes the ARB to adopt regulations generating billions of dollars. If AB 32 was understood to grant such authority, it would have been discussed in this Fiscal Impact section. To the contrary, this entire section focuses solely on fees to be paid for program administration.

The ARB's Bill Report appends a two-page chart titled "Fiscal Impact of AB 32." (JA 0166-0167.) It likewise discusses only program administration costs, and nowhere indicates that AB 32 authorizes the ARB to engage in a state revenue-raising program unprecedented in the history of the State. This is evidence that no one in 2006 thought AB 32 contained such authorization.

The ARB's Enrolled Bill Report also contains a section titled "Existing Market Based Programs," which does not mention any authorization for the ARB to self-allocate and auction off GHG emissions allowances to produce massive government revenue. (JA 0162.) In fact there is no indication anywhere in the Report that AB 32 authorizes the ARB to allocate emissions allowances to itself and auction them to generate revenue.

Finally, the ARB's Enrolled Bill Report concedes there was no intent in AB 32 to authorize ARB to impose billions of dollars of costs on California businesses. In its section on "Fees," the Report acknowledges that, in dealing with GHG emissions, the Governor "**made a policy commitment not to impose additional costs on industry beyond their own costs of compliance**." (Emphasis added, underscoring in original; JA 0163.) If AB 32

violated that policy by authorizing massive auction charges on industry, the ARB's Report would surely have informed the Governor, but it did not because the bill contained no such authorization.

Surely, the regulations thereafter adopted by the ARB allowing it to withhold for itself a percentage of the annual statewide GHG emissions allowances and to auction or sell them off to the highest bidders – thus raising from industry up to $70 billion or more of revenue for the State – are inconsistent with the policy commitment not to impose additional costs on industry beyond the fees authorized to cover essential, direct program costs.

To emphasize that AB 32 imposed no costs on industry beyond the costs of the regulatory program, the ARB prepared and attached to the Report a proposed "SIGNING MESSAGE FOR AB 32" by the Governor, containing the following statement:

> "I want to join the Speaker in assuring that **any fees that may be collected from sources of global warming emissions will only be used to support the essential and direct program costs associated with the bill**."

(Emphasis added; JA 0168.)

In drafting this statement, the ARB unequivocally admitted that "any fees that may be collected from sources of global warming emissions will only be used to support the essential and direct program costs associated with the bill."

This is strikingly important. The description in the ARB's Enrolled Bill Report is strong evidence of the Legislature's understanding of AB 32 when it was passed.

> [A]n enrolled bill report, generally prepared within days after the bill's passage, [is] likely to reflect such legislative understanding, particularly because it is written by a governmental department charged with

> informing the Governor about the bill so that he can decide whether to sign it, thereby completing the legislative process.

(*Conservatorship of Whitley, supra*, 50 Cal.4th at p. 1218, fn. 3.)

**4. Floor debate shows that the Speaker of the Assembly assured legislators that AB 32 did not authorize the ARB to impose any costs other than fees for program administration.**

That the Legislature did not intend to authorize the ARB to develop and implement a scheme to impose billions of dollars of charges on industry is evident from the record of the floor debate in the Assembly. (JA 0814.)[12] There was no mention of ARB's self-allocation or sale of emissions allowances. Nothing was said about raising billions of dollars of state revenues. However, several legislators raised concerns that under AB 32 the ARB could impose a broad range of fees: "Does that mean that the Air Resources Board on their own without legislative oversight can implement a program to tax cows or to tax the hay that cows eat?" (JA 0814 at 12:22.) "Any bill of this size and significance that gives an unlimited ability to the California Air Resources Board to charge fees and taxes and anything else they want should be a no on the merits." (JA 0814 at 50:32.)

The Speaker (who also was the bill author) replied to these concerns by assuring legislators that AB 32 only authorized narrow charges sufficient to pay program administration costs:

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[12] This is a DVD of the Assembly Floor Debate.

> Let me just say in closing, on the question that was raised by several of my colleagues, I want to encourage them to vote for this bill and I want to say to them, **I apologize if there is language in this bill which you are interpreting in a different way.** The **intent of the fee is for program administration and costs only**, and I have a letter to The Journal to specify that.

(JA 0814 at 1:09:35, emphasis added.) The Speaker's floor statement plainly refers to all language in the bill, and is not limited to just section 38597; and the bill was passed immediately after the Speaker finished speaking.

It defies logic to believe that the Legislature, which expressed concerns over and sharply limited the ARB's authority to impose a few million dollars in fees on emissions sources in section 38597, nonetheless silently intended with a vague phrase in section 38562(b)(1) to authorize ARB to impose tens of billions of dollars of charges on those same emissions sources. [13]

The Speaker's quote broadly refers to all language in AB 32, and his remarks on the Assembly floor immediately preceding the vote should be given their fair meaning.[14] Those remarks squelched

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[13] Section 38562 directs the ARB to adopt GHG limits and reduction measures by regulation. Subdivision (b) provides, "... to the extent feasible and in furtherance of achieving the statewide greenhouse gas emissions limit, the [ARB] shall . . . . (1) Design the regulations, including distribution of emission allowances where appropriate, in a manner that is equitable, seeks to minimize costs and maximize total benefits to California, and encourages early action to reduce greenhouse gas emissions." ARB improperly claims this vague phrase authorizes its massive revenue program, conveniently ignoring that charging billions of dollars for allowances is antithetical to subsection (b)(1)'s directive to minimize costs and the burden of complying.

[14] The trial court said that the Speaker's letter to the Assembly Journal referred only to fees authorized by section 38597. (JA

the concerns of legislators by satisfying them that AB 32 did not authorize massive revenue-raising by the ARB. As pointed out above, if AB 32 was intended to allow the ARB to raise tens of billions of dollars of revenue on the backs of a small sector of the State's business community, there would have been more vigorous debate and opposition to the bill. After the Speaker's clarification, debate ended because it obviously was understood that AB 32 does not authorize the ARB to do so.

**5. The fact that section 38597 expressly granted the ARB authority to impose fees on the sources of GHG emissions shows that the Legislature knew how to make its intent clear when it intended to authorize ARB to raise revenue – the absence of such authorizing language for a multi-billion dollar revenue-raising program means the Legislature did not intend to grant such authority to the ARB.**

Section 38597 enacted by AB 32 authorizes the ARB to

> adopt by regulation, after a public workshop, a schedule of fees to be paid by the sources of greenhouse gas emissions. . . . The revenues collected pursuant to this section, shall be deposited into the Air Pollution Control Fund ... for purposes of carrying out this division.

This very specific authorizing provision demonstrates the Legislature knew how to authorize the ARB to adopt regulations imposing charges on the sources of GHG emissions when that is what it intended. In contrast, there is no similar language in AB 32 expressly authorizing the ARB to adopt regulations imposing massive charges on GHG sources to fund a massive revenue-raising

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1605.) But the Speaker's statement on the floor speaks for itself and is what was heard by the members immediately before voting.

program. "Where the [Legislature] has demonstrated the ability to make [its] intent clear, it is not the province of this court to imply an intent left unexpressed." (*Mutual Life Ins. Co. v. City of Los Angeles* (1990) 50 Cal.3d 402, 412.)

The fact that AB 32 contains an express authorization in section 38597 for the ARB to impose a few million dollars of charges for administrative costs, but contains no similar authorization for the ARB to impose tens of billions of dollars of charges for revenue-raising purposes, is strong evidence the Legislature intended no such thing. Common sense tells us that the Legislature does not hide elephants in mouseholes. (*Cal. Redevelopment Assn. v. Matosantos* (2011) 53 Cal.4th 231, 260-61.)

The entirety of AB 32 must be considered in construing its provisions. (*People v. Allen* (2007) 42 Cal.4th 91, 102.) The ARB claims, and the trial court ruled, that the phrase "including distribution of allowances where appropriate" in section 38562(b)(1) authorizes the ARB to adopt regulations imposing tens of billions of dollars of charges on GHG emitters. But this is inconsistent with, and cannot be harmonized with, section 38597. It makes no sense that the Legislature would carefully restrict charges on emissions sources in section 38597, but then silently grant the ARB *carte blanche* to impose billions of dollars of charges on those same emissions sources with the vague language of section 38562.

### 6. To interpret AB 32 otherwise violates canons of statutory construction.

In refusing to apply the taxpayer protections of Proposition 218 (1996) to local annexation areas, the Court of Appeal recently explained: "there is much in the very structure of Proposition 218 that, if it had been intended to apply to annexations, should have

been there, but isn't. Just as the silence of a dog trained to bark at intruders suggests the absence of intruders, this silence speaks loudly." (*Citizens Assoc. of Sunset Beach v. Orange Co. LAFCO* (2012) 209 Cal.App.4th 1182, 1191.)

So it is here. Just like in *Sunset Beach,* if the Legislature had intended to authorize the ARB to impose tens of billions of dollars in new charges on California businesses, there is "much in the very structure of" AB 32 that should have been in its text or legislative history, but it is not there. (See also, *Schmeer v. County of Los Angeles* (2013) 213 Cal.App.4th 1310 [declined to interpret constitutional amendment broadly when there was no indication in ballot argument or text of measure indicating the voters had such intent].)

The absence of any express authority in AB 32 for the ARB's massive revenue raising program speaks loudly, particularly so when section 38597 expressly authorizes the ARB to impose fees on GHG sources to pay for minor program administrative costs. The notion that authority for the ARB to impose billions of dollars of charges on those same GHG sources is concealed in vague language in AB 32 is totally contrary to established canons of construction. "A recognized rule of statutory construction is that the expression of certain things in a statute necessarily involves exclusion of other things not expressed—*expressio unius est exclusio alterius.*" (*Henderson v. Mann Theatres Corp.* (1976) 65 Cal.App.3d 397, 403.)

Furthermore, if the ARB's authority to utilize market-based mechanisms provided in section 38562(c), or its authority to "distribute" emissions allowances in section 38562(b)(1), were construed to grant to the ARB the authority to raise tens of billions of dollars through the sale of GHG allowances, such construction of

the statute would render surplusage the authorization in section 38597 to raise a few million dollars for program costs. (*In re Luke W.* (2001) 88 Cal.App.4th 650, 656 ["In construing a statute, every word thereof is, if possible, to be given meaning so as to avoid surplusage."])

**7. Because the ARB's massive revenue-raising program is not essential to the purpose of AB 32, the legislation cannot be interpreted to impliedly confer upon the ARB the power to implement that program; and no deference is accorded to the ARB's contrary self-serving interpretation of the scope of AB 32.**

"[I]t is well settled that administrative agencies have only the powers conferred upon them, either expressly or by implication, by Constitution or statute. An administrative agency must act within the powers conferred upon it by law and may not act in excess of those powers." (*American Federation of Labor v. Unemployment Ins. Appeals Bd.* (1996) 13 Cal.4th 1017, 1042; internal citations omitted.) "Actions exceeding express or implied delegated powers are void." (*Diageo-Guiness USA, Inc. v. Bd. of Equalization* (2012) 205 Cal.App.4th 907, 915.) The trial court concluded AB 32 did not explicitly authorize the ARB's revenue raising regulations (JA 1697) and such authority may not be implied.

Implied administrative powers must be narrowly construed, and any reasonable doubt as to the existence of the implied power is resolved against the agency. (*Addison v. Department of Motor Vehicles* (1977) 69 Cal.App.3d 486, 498 ("*Addison*") ["For a power to be justified under the [implied powers] doctrine, it must be essential to the declared objects and purpose of the enabling act—not simply convenient, but indispensable. Any reasonable doubt concerning the

existence of the power is to be resolved against the agency." Underscoring added.] See also 76 Ops.Cal.Atty.Gen. 11, 16 (1993).)

Here, it is undisputed that the ARB's massive revenue-raising program is not indispensable to achieving the GHG reductions goal of AB 32. During the regulatory comment period, the ARB responded to a question regarding its authority to sell emissions allowances. The ARB stated that in a cap and trade program, allowances can be "distributed free of charge, they can be sold at a predetermined price, they can be auctioned off with competitive bidding, or by another allocation method developed." (JA 0113, 0115.) The ARB also conceded that "Traditionally, cap and trade programs have favored freely allocating allowances to the covered entities." (JA 0235.) And both the nonpartisan LAO and the ARB's Economic and Allocation Advisory Committee independently confirmed that the GHG reduction goals of AB 32 can be achieved just as easily through cost-free allocation of GHG allowances, which are revenue neutral to the state.[15]

Because the ARB's massive revenue-raising is not essential to achieve the GHG reduction purpose of AB 32, it is wrong to conclude that the bill impliedly conferred upon the ARB the authority to undertake a program raising from taxpayers tens of billions of

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[15] JA 0238: Legislative Analyst's Office, "Letter to Hon. Henry T. Perea," Aug. 17, 2012 [noting that an auction is not "necessary" and allowances can be distributed entirely for free "because it is *the declining cap on emissions that will reduce the state's overall level of GHGs—not the manner in which allowances are introduced into the market* (emphasis added)]; and JA 0242-0244: Economic and Allocation Advisory Committee, "Allocating Emissions Allowances Under a Cap-and-Trade Program, Recommendations to the California Air Resources Board and the California Environmental Protection Agency," March 2010, p. 2, [noting that allowances can be freely allocated under a cap-and-trade program].

dollars of revenue for the State. (See *Addison, supra,* 69 Cal.App.3d at p. 498.)

### a. No deference is given to the ARB's contrary interpretation of the scope of AB 32.

In assessing a regulation to determine whether the agency has exceeded its statutory authority, courts apply their own independent judgment. (*Yamaha Corp. of America v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 7-8 ["*Yamaha*"].) The initial duty of the court is to determine whether the agency acted "within the bounds of the statutory mandate." (*Morris v. Williams* (1967) 67 Cal.2d 733, 748.) If not, the regulation is invalid.

In *Citizens to Save California, supra,* 145 Cal.App.4th 736, this Court rejected the FPPC's interpretation of a statute and struck down an FPPC regulation as *ultra vires*, citing *Yamaha* and reiterating, "We do not defer to an agency's view when deciding whether a regulation lies within the scope of the authority delegated by the Legislature." (*Id.* at pp. 747, 748-754; see also, *Schneider v. California Coastal Com.* (2006) 140 Cal.App.4th 1339, 1345.) The Supreme Court is in accord.

> A court does not ... defer to an agency's view when deciding whether a regulation lies within the scope of the authority delegated by the Legislature. The court, not the agency, 'has final responsibility for the interpretation of the law' under which the regulation was issued. [Citations.]

(*Yamaha, supra,* 19 Cal.4th at p. 11, fn. 4.)

Courts routinely invalidate administrative action that has, "in effect, 'altered or amended the statute or enlarged or impaired its scope.'" (*Assn. for Retarded Citizens v. Dept. of Devp. Svcs.* (1985) 38 Cal.3d 384, 391 [internal brackets omitted], quoting *Morris*,

*supra*, 67 Cal.2d at p. 748.) "[A] court cannot insert or omit words to cause the meaning of a statute to conform to a presumed intent that is not expressed." (*Citizens To Save California, supra*, 145 Cal.App.4th at p. 747.)

The ARB contended below, and the trial court ruled, that by authorizing a cap-and-trade program "including the distribution of emissions allowances where appropriate" (section 38562(b)(1)), the Legislature authorized the ARB to adopt the massive revenue-raising program at issue here. But that is incorrect.

As demonstrated above, there is nothing in the text of the bill or its legislative history that indicates any intent on the part of the Legislature to authorize such revenue-raising. If AB 32 intended to authorize the ARB to raise revenue, the Legislature surely would have established limits and guidelines on the ARB's exercise of such an extraordinary power. But the bill contains no safeguards or standards to guide that power's use or protect against misuse. No boundaries whatsoever are placed on the ARB's purported revenue raising authority; the burdens imposed on and the revenue generated from the State's business community could be $5 million or $500 billion, all left to the discretion of the ARB. This would have been plainly improper. (*Hess Collection Winery v. ALRB* (2006), 140 Cal.App.4th 1584, 1604.) The trial court viewed these omissions as immaterial and the regulations as merely "filling in the details" of AB 32. (JA 1662.) Not so, one of the largest revenue-raising programs in state history is not "detail-filling."

Also as explained above and in further detail below, if the Legislature intended to authorize the ARB to impose massive revenue-raising, without precedent in state history, there would have been some indication of such an intent in the statute itself, its

findings and declarations, its legislative history and/or the Legislative Counsel's digest. And it certainly would have been the subject of hot debate in the Legislature. The fact that there was none demonstrates that there was no such intent. (*Ailanto Properties, Inc. v. City of Half Moon Bay* (2006) 142 Cal.App.4th 572, 589 [court reasoned that a statute described in legislative history as "noncontroversial" would not result in major changes.] Similarly here, if AB 32 intended to authorize a huge revenue generating program on the backs of California businesses, it is implausible the Legislature would have authorized it in total silence. As aptly stated in *Ailanto Properties*, "[w]e think it highly unlikely that the Legislature would make such a significant change ... without so much as a passing reference to what it was doing. The Legislature 'does not, one might say, hide elephants in mouseholes.'" [Internal quotation marks omitted.] (*Id.* at 589.)

In addition, as noted above, the record of the floor debate in the Assembly makes plain that the Legislature did not intend to authorize the ARB to implement a scheme to impose billions of dollars of charges on industry. In response to concerns expressed by some legislators, the Speaker of the Assembly assured all the intent of AB 32 was to limit fees to program administration and costs only. This assurance immediately squelched what would have been vigorous debate and opposition to AB 32 if the bill was intended to authorize the ARB to raise tens of billions of dollars on the backs of a small sector of the State's business community.

Finally, consideration should be given to the consequences that will flow from interpreting AB 32 as authorizing *sub silentio* the ARB to impose massive and unbounded revenue raising. (*Dyna-*

*Med, Inc. v. Fair Employment & Housing Com.* (1987) 43 Cal.3d 1379, 1388.)

In *Dyna-Med,* the Court rejected the FEHC's interpretation of its governing statute as authorizing it to award punitive damages. While acknowledging that awarding punitive damages would serve to deter discrimination consistent with the statutory purpose, the Court nonetheless concluded that this was "insufficient to support an inference that the Legislature intended sub silentio to empower the commission to impose punitive damages" in light of "the extraordinary nature of punitive damages." (*Id.* at 1389.) The Court also expressed concern that the FEHC's argument, taken to its logical conclusion would authorize every administrative agency granted remedial powers to impose punitive damages.

So it is here. If the "extraordinary nature of punitive damages" was reason for the *Dyna-Med* Court not to infer an intent *sub silentio* into FEHA, the extraordinary -- unprecedented power -- to impose a multi-billion dollar revenue raising program is reason for this Court not to infer an intent *sub silentio* into AB 32. And, like the *Dyna-Med* Court, this Court should also be concerned about the consequences that will flow from interpreting AB 32 as silently authorizing the ARB to impose massive revenue raising to ostensibly assist a regulatory program. If the ARB regulations are allowed to stand, there would be no end to the charges that creative minds could invent as part of the myriad regulatory programs in this state.

### 8. Statutes enacted in 2012 do not purport to construe or amend AB 32 and provide no guidance as to the intent of the 2006 Legislature.

The trial court ruled that four statutes enacted in 2012 "reflect a legislative understanding" that the 2006 Legislature intended AB

32 to authorize the ARB to auction emissions allowances and raise tens of billions of dollars. (JA 1698.) Not so. Those 2012 statutes merely establish the 2012 Legislature's decision that, if the government is to receive billions of dollars of new revenue, the Legislature itself will decide how to spend the money. None of the statutes attempts to declare the "intent" of the 2006 Legislature in enacting AB 32. Even if they did, however, it would be totally speculative: of the 120 members of the Legislature in 2006, only 23 remained in office in 2012.[16] Furthermore, "[t]he declaration of a later Legislature is of little weight in determining the relevant intent of the Legislature that enacted the law." (*Peralta Community College Dist. v. Fair Employment & Housing Com.* (1990) 52 Cal.3d 40, 52; *see also People v. Cruz* (1996) 13 Cal.4th 764, 775.) Any attempted reliance on statutes enacted in 2012 to interpret the intent of AB 32 enacted in 2006, falls flat. And finally, the fact that the Legislature appropriates auction revenues in no way validates the auction regulations challenged in this appeal. (See *Shaw v. Chiang* (2009) 175 Cal.App.4th 577 [this Court invalidated the Legislature's method of appropriating billions of dollars in transportation revenues as inconsistent with two voter initiatives despite the fact that the appropriations had been occurring for five consecutive fiscal years.].)

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[16] Compare 2005-06 and 2011-12 California state Legislature rosters: http://clerk.assembly.ca.gov//clerk/billslegislature/documents/Asm_Handbook_2005-06.pdf) and http://www.leginfo.ca.gov/pdf/2011_12_Legi_HandBook.pdf.

### 9. The legislative history of AB 32 does not support the ARB's claim that the Legislature intended the vague phrase "distribution of emission allowances" to authorize a multi-billion dollar revenue raising program.

As previously demonstrated, the legislative record is bereft of any indication that the 2006 Legislature thought it was authorizing the ARB to adopt an unprecedented revenue raising program in passing AB 32. What the Legislature understood in the summer of 2006 is controlling: "[t]he words of a statute are to be interpreted in the sense in which they would have been understood [by the Legislature] at the time of the enactment." (*People v. Cruz* (1996) 13 Cal.4th 764, 775.) Had the Legislature intended AB 32 to authorize massive revenue raising, it would have provoked a battle royal in the Legislature.

The ARB and the trial court ignored this obvious truth, and instead assert that, by using the vague phrase "distribution of emission allowances," the Legislature gave unbridled and unlimited authorization to the ARB to concoct a revenue raising program unlike any seen previously. But "[C]onstruing statutory language is not merely an exercise in ascertaining 'the outer limits of [a word's] definitional possibilities.'" (*FCC v. AT&T, Inc.* (2011) 131 S.Ct. 1177, 179 L. Ed. 2d 132, 136; *Dolan v. Postal Service* (2006) 546 U.S. 481, 486; 58 Cal.Jur.3d 564 (Statutes § 135).) Statutes are to be construed in accordance with the plain and commonsense or usual and ordinary meaning of the language used and construction should be practical rather than technical. (*Ste. Marie v. Riverside County Regional Park and Open-Space District* (2009) 46 Cal.4th 282, 288; *Moran v. Murtaugh Miller Meyer & Nelson, LLP* (2007) 40 Cal.4th 780, 783.)

Contrary to these principles, the ruling below is grounded on the erroneous premise that the phrase "distribution of emissions allowances" has a "technical meaning" and that it was "reasonable to assume" the Legislature considered that phrase to "potentially encompass both giving away allowances and selling them via auction or direct sales." (JA 1698.) This rationale was based on the trial court's incorrect premise that in 2006 auctions to raise massive revenue were a common method of distributing allowances, and the trial court's mistaken assertion that "petitioners admit" there were two cap and trade programs existing in 2006 which "authorized allowances to be sold or auctioned." (*Ibid.*, referring to the Federal Government's acid rain program and the European Union's Emissions Trading Scheme ("ETS").) (*Id.* at 1664.)[17] These conclusions of the trial court were wrong. Further, there is no support for the trial court's assertion as to what the 2006 Legislature understood the phrase "distribution of emission allowances" to mean.

First, the legislative history contains no mention whatever of these other cap-and-trade programs. Nor does it mention the self-allocation and auctioning of allowances to raise massive revenue.

Second, the federal government's acid rain reduction program under the Clean Air Act is as different from AB 32 as night is from day. Had the 2006 Legislature actually considered the Clean Air Act (and there is no indication in the legislative record that it did),

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[17] The trial court also cited a 2003 EPA document as support that allowances can be sold. (JA 1664.) However, that EPA report states, "To date, existing cap and trade programs have allocated allowances at no cost to sources." (*Emphasis added.*) Moreover, the EPA document was nowhere mentioned in AB 32's legislative history.

nothing in that Act would have informed the Legislature the "distribution of emissions allowances" language in AB 32 would authorize the ARB to implement a multi-billion dollar revenue-generating program.

In complete contrast to AB 32's ultra vague language, the Clean Air Act explicitly authorized the EPA to

> conduct auctions at which the allowances ... shall be offered for sale.... A person wishing to bid for such allowances shall submit ... to the [U.S. EPA] Administrator ... offers to purchase specified numbers of allowances at specified prices.

(42 U.S.C. § 76510(d)(2).) Furthermore, the Clean Air Act auctions are revenue-neutral and raise no government revenue. Under that Act, the auction proceeds are transferred back to the entities from whom the allowances sold at the auction were originally withheld, and **"[n]o funds transferred from a purchaser to a seller of allowances ... shall be ... treated for any purpose as revenue to the United States or the [U.S. EPA] Administrator**." (42 U.S.C. § 76510(d)(3).) Thus, if the Legislature in 2006 did have the Clean Air Act in mind when it passed AB 32, it would have understood that (i) explicit statutory authorization was needed for ARB to auction allowances, and (ii) auctions were not for revenue-raising.

Third, the European Union's ETS likewise was not mentioned in AB 32's legislative history, and nothing indicates the 2006 Legislature considered it in any way. Furthermore, the ETS in 2006 provided no precedent for the massive revenue-raising program created by the ARB. The ETS was embryonic in 2006, and the years 2005 – 2007 were its "'pilot' or 'trial' period." (Pricing Carbon at

1.)[18] In fact, during this trial period, only four of 25 member countries auctioned any allowances (Denmark, Hungary, Lithuania and Ireland); and the total percentage of allowances auctioned during the 2005 – 2007 was a microscopic 0.13%. (Pricing Carbon at 43, 62.) Thus, when the Legislature passed AB 32 in August 2006, it would have no reason to believe that the bill authorized the ARB to undertake a massive revenue-raising program. Furthermore, it would have understood that auctions required express authorization, which was absent from AB 32.

Fourth, there was no discussion in AB 32's legislative history regarding RGGI, a group of northeastern states who in late December 2005 signed a GHG reduction Memorandum of Understanding. (JA 1140-1159.) That MOU nowhere mentions the self-allocation and sale of allowances to generate revenue, nor does it mention "auctions." When AB 32 was passed in August 2006 there had not been a single auction of allowances by any RGGI state, and the first RGGI auction occurred September 25, 2008, a full two years after AB 32 passed. (http://www.rggi.org/docs/rggi_press_9_29_2008.pdf) (last accessed: August 6, 2013; JA 1448-1449.)

Finally, the trial court below referenced a March 2006 report of the California Climate Action Team to the Governor and Legislature as supporting its belief that the Legislature was aware the distribution of allowances included auctions to raise government revenues. (JA 1664.) But this report nowhere appears in AB 32's legislative history and is nowhere discussed in that history. Thus, there is no basis to say the Legislature considered this report in

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[18] ARB's AR cites the book "Pricing Carbon" at AR 063974-5, and includes a hard copy of this book.

passing AB 32. And even if it had, there is nothing in the report's Executive Summary (AR 006027-006044) or anywhere else that discusses auctioning of allowances for a massive government revenue generating program. (AR 006025-006281.) Thus, the report is not part of the legislative history, sheds no light on the "collegial view of the Legislature *as a whole*," and provides no evidence of the Legislature's corporate knowledge and purpose in enacting AB 32. (*Kaufman & Broad Communities, Inc. v. Performance Plastering, Inc.* (2005) 133 Cal.App.4th 26, 30 [emphasis in original]; *In-Home Supportive Services v. Workers' Comp. Appeals Bd.* (1984) 152 Cal.App.3d 720, 739.)

In sum, it defies common sense to conclude that information buried deep in matters not included in the legislative history and thus not discussed during debate (information of technical nature not commonly understood by person other than experts in the field) constitutes a basis to construe the vague term "distribution of emissions allowances" in AB 32 as a knowing and intentional legislative authorization of the ARB to implement a multi-billion dollar revenue-generating program – authorization that surely would have generated heated debate and opposition by legislators.

Simply stated, there is no basis for the ARB's claim and the trial court's ruling that the ARB's auction of emissions allowances to generate billions of dollars of state revenue was anticipated and authorized by the Legislature when it passed AB 32 in August 2006.[19]

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[19] The ARB also claimed below there were many "tradable permit" programs around the globe when AB 32 was passed. (JA 1008.) But none of this is in the legislative history of AB 32. Moreover, the great majority of these programs governed totally

And as explained next, there is another reason why AB 32 cannot be read to authorize the ARB to raise billions of dollars of State revenue by withholding for itself and then auctioning to the highest bidders a percentage of the GHG emissions allowances. Such a charge for emission allowances constitutes a tax that is unconstitutional because it was not passed by a two-thirds vote in each house of the Legislature. (See *Harrott v. County of Kings, supra*, at p. 1153 [courts must presume the Legislature did not intend to violate the Constitution; thus courts must construe a statute in a way that makes it constitutional].)

### B. The Challenged Regulations Impose An Illegal Tax.

#### 1. The trial court correctly recognized that *Sinclair Paint* controls, but failed to properly apply the *Sinclair Paint* test.

The trial court properly recognized that the *Sinclair Paint* line of cases controls this dispute. The *Sinclair Paint* test is straightforward: If an environmental mitigation charge (1) bears a reasonable relationship between the amount charged and the burdens imposed by the fee payer's operations, (2) the charge is not used for unrelated revenue purposes, and (3) the remedial measures funded with the charge have a causal connection or nexus to the fee payer's operations, then the charge is a regulatory fee. If the charge is lacking in any of those respects, it is a special tax. (*Sinclair Paint, supra*, 15 Cal.4th at pp. 876-879, 881.)[20]

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unrelated things like fishing and hunting licenses, and none involved government revenue-raising programs.

[20] Both the LAO and Legislative Counsel agree that the auction revenues are subject to and must satisfy the *Sinclair Paint* test. (JA 0060.)

Having correctly identified the controlling law, however, the trial court misapplied both the sequencing of the law as well as the tests. The ARB's auction constitutes the imposition of a special tax under *Sinclair Paint*. Because neither the auction regulations nor AB 32 were adopted by a two-thirds vote in the Legislature, the regulations are invalid under article XIIIA, section 3 of the California Constitution.

### 2. The trial court erred by concluding the auction revenues were regulatory fees *before* applying the *Sinclair Paint* test.

The trial court discussed whether the auction and reserve sale generated "taxes" or "fees." (JA 1667-1672.) It briefly summarized cases dealing with the historic definition of a "tax," then identified typical categories of fees (special assessment, business improvement district, development, user, and regulatory) and concluded that the auction and reserve sale constitute regulatory fees instead of taxes; albeit calling it a "close question." (JA 1670.)

This was itself a sequencing error. The whole purpose of the *Sinclair Paint* analysis is to determine whether a specific government charge or exaction is a "special tax" or a "regulatory fee." This inquiry was especially appropriate as the ARB conceded that the auction regulations were imposed pursuant to its regulatory powers. The *Sinclair Paint* analysis results in a "fee or tax" *conclusion*; the trial court *started* by concluding the auction proceeds were regulatory fees, and *then* attempted to apply *Sinclair Paint*. This was backwards.

At oral argument the trial court expressed uncertainty whether *Sinclair Paint* controls, but conceded if it did control the auction

regulations would be invalid: "**I would agree if *Sinclair Paint* is the test the state loses.**" (RT at p. 25, emphasis added.) By the time it ruled several months later, the court acknowledged this case is controlled by *Sinclair Paint*, stating: for a "mitigation fee to be a valid regulatory fee and not a tax, the [*Sinclair Paint*] requirements must be met." (JA 1672.) But because *Sinclair Paint* is the *only* legal framework for making the regulatory fee/special tax distinction, the trial court was in the impossible position of trying to apply the *Sinclair Paint* test in a way that would be consistent with its earlier conclusion that the auction proceeds were *regulatory fees*. As explained below, this is impossible to do, and led to the erroneous trial court ruling.

### 3. The trial court misstated and misapplied the *Sinclair Paint* test.

Having already prematurely concluded that the auction proceeds were regulatory fees, the court nonetheless said that their validity depended upon compliance with the three-prong *Sinclair Paint* test, which it characterized as follows:

> [F]or 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 the 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 payer's products or operations.

(JA 1672.)

The trial court's formulation of the *Sinclair Paint* test is simply wrong. When the three-part test is correctly stated, and the facts correctly applied, it is clear that the auction proceeds are "special taxes" and *not* "regulatory fees."

### 4. Proper description and application of the *Sinclair Paint* test demonstrates that the auction of GHG allowances results in an illegal tax.

#### a. The charges for the purchase of the GHG allowances bear *no* relationship to the burdens imposed by the purchasers' operations.

The trial court's ruling simply ignored the first *Sinclair Paint* requirement that the charge for the GHG allowances must "bear a reasonable relationship between the *amount charged* and the burdens imposed by the fee payer's operations" in order to escape characterization as a special tax. The auction regulations plainly fail this requirement. For any given period of time, the burden imposed by the fee payer's operations is a fixed number. For example, if the period covered by the auction is a year, the amount of GHG the fee payer will emit is fixed and determinable. However, the very nature of an auction is that the price paid for the allowance is not related to the burden of the fee payer's operations, but will fluctuate based on factors affecting the competitive demand for the limited number of allowances available. Thus, the price the fee payer will pay is not fixed by the burdens imposed by his or her business operations, but is related to fluctuating factors such as the marketplace, the relative profitability of the various bidders, and the cost and availability of means to otherwise reduce the amount of GHGs the bidder is producing.

A valid regulatory fee under the first prong of the *Sinclair* Paint test requires a "reasonable" relationship between the amount charged and the burden of the fee payer's operations. Here, the amount charged has no such relationship, and as a result the auction

charges are "special taxes" which are illegally imposed as they were not adopted by a two-thirds vote of both houses of the Legislature.

### b. Auction proceeds are being impermissibly used for "general government purposes."

The auction regulations violate the second prong of the *Sinclair Paint* test — that the charge is not levied for "unrelated revenue purposes." (*Sinclair Paint*, *supra*, 15 Cal.4th at 876; *Calif. Farm Bureau Federation v. State Water Resources Control Bd.* (2011) 51 Cal.4th 421, 437 ("*Calif. Farm Bureau*").)[21]

The trial court acknowledged that "*[t]he essence of a tax is that it raises revenue for general government purposes.*" (JA 1667; emphasis added.) It further reasoned that "since every aspect of life has some impact on GHG emissions, it is difficult to conceive a regulatory activity that will not have at least some impact on GHG emissions... *Thus, in practice, allowance proceeds can likely be used for general government purposes.*" (JA 1671; emphasis added.) It necessarily follows that the charges imposed through the auction regulations were levied for general government purposes—a violation of the second prong of the *Sinclair Paint* test.[22]

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[21] This Court has also recognized that the proper evaluation is whether the charge is imposed for "unrelated revenue purposes." (See *Townzen v. El Dorado County* (1998) 64 Cal.App.4th 1350, 1359 ["Plaintiff has not established that filing fees such as those imposed by section 26826(a) are levied for revenue purposes unrelated to the activity for which the fees are charged..."].)

[22] The trial court sidestepped this test and erred by asking a different question: whether the primary purpose was regulation or revenue generation. Having misstated the second prong of the *Sinclair Paint* test, the court below concluded "the primary purpose of the charges is regulatory." (JA 1673.) The court based this conclusion on the ARB's argument that the sale of allowances helps achieve regulatory goals. (*Id.*) There are two problems with this.

There is no question that the auction regulations have resulted in one of the largest net increases in state revenues in the state's history – dwarfing any regulatory fee ever approved by any court. (See JA 1667 ["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"].) The trial court acknowledged these revenues "can be reinvested for public benefit." (JA 1673.)

So it is: the revenues are being spent on a wide array of general government purposes. In the current 2014-15 Budget Act, proceeds from the sale of GHG allowances are appropriated for the high speed bullet train construction project ($250 million), transit and intercity rail ($25 million), transit operations ($25 million), affordable housing ($129 million), weatherization projects ($75 million), agricultural energy and operational efficiency ($15 million), energy conservation assistance for public buildings ($20 million), wetland and watershed restoration ($22 million), fire risk reduction and forest health ($24 million), urban forestry ($18 million), solid waste diversion ($20 million), and support of the Department of Fish and Wildlife ($3 million). (Stats. 2014, ch. 25 [SB 852].) Water efficiency programs received another $40 million in cap and trade

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First, the trial court's decision fails to explain how the generation of tens of billions of dollars for general government programs comports with the second prong of *Sinclair Paint*. Second, the trial court's conclusion conflicts with its own characterization of what constitutes a charge imposed for "the purpose of increasing revenues" in Cal. Const., art. XIIIA ["The phrase ['for the purpose of increasing revenues'] simply requires ... that the changes ... result in a cumulative net increase in state tax revenues"].) (JA 1667.) As the trial court acknowledged, the "essence of a tax is that it raises revenue for general government programs." (JA 1667.) The auction and reserve sale operate in exactly that fashion.

auction profits. (Stats. 2014, ch. 2 [SB 103].) In addition, the 2014-15 cap and trade budget trailer bill *continuously* appropriates beginning in Fiscal Year 2015-16 60 percent of all future cap and trade auction profits to the high speed bullet train (25%), affordable housing (20%), transit and intercity rail (10%), and low carbon transit (5%). The cap and trade trailer bill also takes $400 million of the $500 million in cap and trade profits loaned to the General Fund in the 2013-14 Budget Act and redirects it to the high speed bullet train project. (Stats. 2014, ch. 36 [SB 862].)[23]

**i. The trial court's "primary purpose" test completely eviscerates *Sinclair Paint's* second prong: does the revenue program raise more money than necessary to pay the costs of a fixed and determinable regulatory program?**

In every case where a mitigation charge has been found to be a valid regulatory fee and not for "general governmental purposes," the amount of the charge has been based on the size of the regulatory program it supported. For example, in *Sinclair Paint*, the Legislature established the Childhood Lead Poisoning Prevention Act to evaluate and screen children deemed to be potential victims of lead poisoning. The annual cost of the program was $16 million, so the total amount of annual fees collected from lead product manufacturers was $16 million. (*Sinclair Paint, supra,* 15 Cal.4th at

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[23] Ironically, the LAO states that use of auction proceeds for bullet train construction "would not help achieve AB 32's primary goal" and "construction and operation of the [bullet train] system would emit more GHG emissions than it would reduce for approximately the first 30 years." [See LAO 4/17/12 Report, "The 2012-13 Budget: Funding Requests for High Speed Rail: http://www.lao.ca.gov/analysis/2012/transportation/high-speed-rail-041712.aspx.] (Last visited 10/14/14.)

869-70; Stats. 1991, ch. 799, § 3 (then-Health & Saf. Code, § 372.7(f); now § 105310(f)).) The same was true in *Calif. Farm Bureau, supra,* 51 Cal.4th at 432 [fee was strictly limited to the costs of supporting the State Water Resources Control Board's Water Rights Division] and *Collier v. City and County of San Francisco* (2007) 151 Cal.App.4th 1326, 1346 [building inspection fee transfers to planning and fire departments were limited to the amounts necessary to support functions performed by those departments].)

Conversely, the auction charges do not support a fixed or determinable environmental mitigation program, the costs of which the Legislature sought to recover from those who caused the damage (i.e., emitters of GHGs). Rather, the auction charges imposed by the disputed regulations are amorphous, and raise vast amounts of money by selling *future* rights to emit GHGs and the spending program expands or contracts based on that revenue.

The trial court opinion eviscerates the very simple second prong of the *Sinclair Paint* test: does the program raise more revenue than that needed to fund a fixed and defined government regulatory program? The trial court stated, "[t]he proceeds of the sales will be used to pay for a wide range of *(as-yet-undetermined) regulatory programs (ostensibly) related to AB 32.*" (JA 1669, parentheticals in original; emphasis added) Nonetheless, the trial court concluded the auction proceeds will not exceed the activities they support because they will fund "additional regulatory programs that further the emissions reduction goals of AB 32." (JA 1670.) The trial court conceded that "*neither the ARB nor this court currently know what those programs might be.*" (*Id.*, emphasis added.)

This eviscerates *Sinclair Paint.* Unlike *Sinclair Paint, Calif. Farm Bureau,* and *Collier*, the scope and cost of the AB 32

regulatory program to be supported by the government-imposed charges is not specified *upfront*. To the contrary, it is essentially a pay-as-you-go regulatory program where the size of the program is determined only *after* revenues are collected and a calculation can be made regarding the level of spending that can be sustained.

Never before has a mitigation fee that did not contain a fixed and identifiable fee structure been found to be a valid regulatory fee. (See, e.g., *Sinclair Paint, supra,* 14 Cal.4th 866; *Calif. Farm Bureau, supra,* 51 Cal.4th 421; *Calif. Building Industry Assn. v. San Joaquin Valley Air Pollution Control District* (2009) 178 Cal.App.4th 120; *Calif. Assn. of Prof. Scientists v. Dept. of Fish & Game* (2000) 79 Cal.App.4th 935; *Equilon Enterprises v. Bd. of Equalization* (2010) 189 Cal.App.4th 865; *Collier, supra,* 151 Cal.App.4th 1326.) In all of those cases, the fees charged were subject to a statutory or regulatory framework that fixed the total amount of fees collected, and identified a method of calculating each fee payer's liability. This is because it would make it impossible to determine whether a charge is a regulatory fee or a tax. The answer would always be in constant flux depending on *future* spending decisions made by the legislative and executive branches.[24]

This charge-first-regulate-second approach results in exactly what the Supreme Court in *Calif. Farm Bureau* warned against. As expressed there, "permissible fees must be related to the overall cost of the government regulation... What a fee cannot do is exceed the reasonable cost of regulation with the generated surplus used for general revenue collection. An excessive fee that is used to generate

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[24] This is particularly true if spending programs span multiple auction periods which is currently the case. Identifying exactly which programs were paid for by a particularly auction would be impossible.

general revenue becomes a tax." (*Calif. Farm Bureau, supra,* 51 Cal.4th at 438.)

Under the trial court's decision in this case, the government can get away with overcharging fee payers by simply overspending the money collected; *i.e.,* through a never-ending expansion of the regulatory program. For example, under the trial court's rationale, in *Sinclair Paint* the government could have charged lead manufacturers $32 million in fees despite the fact that the cost of the Childhood Lead Poisoning Prevent Act was $16 million. Then *after* that action was challenged in court for collecting twice as much as necessary, the government could simply have started a new $16 million lead poisoning prevention public education and outreach program so that the total charges would end up not exceeding the total cost of all regulatory activities. Subsequently, the government could charge lead manufacturers $64 million. Once that action was challenged in court for collecting twice as much as necessary, the government could establish a $32 million lead-alternatives research and development program so that the total charges again would end up not exceeding the total cost of all regulatory activities. Thus, under the trial court's theory, the government could avoid converting the original fee into a tax by perpetually adding on new regulatory components, limited only by the government's imagination.

Second, the situation is exacerbated by the fact that, as the trial court acknowledged, "*nearly every aspect of life has some impact on GHG emissions.*" (JA 1671, emphasis added.) This means the government would almost always be able to come up with an after-the-fact regulatory add-on to justify the collection of auction revenues. If the government is not required to specify the regulatory program *upfront*, fee payers would be constantly forced to challenge

whether a new use of GHG allowance auction proceeds complies with *Sinclair Paint*, forcing payers to chase a moving target in perpetuity.

The trial court's "primary purpose" test effectively guts *Sinclair Paint's* "unrelated revenue purposes" test that has stood for years, and as shown above, really is no "test" at all. Any revenue program could be characterized as a "regulatory fee" by simply delegating an administrative agency broad authority to spend money on any program which could in the most remote way be tied to the actions of the payer.

Because the auction regulations fail the second prong of the *Sinclair Paint* test, the proceeds are special taxes requiring a two-thirds vote of both houses of the Legislature.

**c. The auction and reserve sale charges have no "causal connection or nexus to the fee payer's operations."**

The final requirement of *Sinclair Paint* is that there must be a causal connection or nexus between the fee payer's activities or products and the adverse effects that the regulatory program is mitigating. (*Sinclair Paint, supra,* 15 Cal.4th at 877-78 ["the police power is broad enough to include mandatory remedial measures to mitigate past, present, or future adverse impacts of the fee payer's operations, *at least where, as here, the measure requires a causal connection or nexus between the product and its adverse effects*"], emphasis added.) Accordingly, the regulatory program must therefore be aimed at mitigating the damage done by the *fee payer* and not the damage caused by others.

The trial court conflated this third prong with some aspects of the first prong of the *Sinclair Paint* test, holding that in order to be a

regulatory fee, there must be a "*reasonable relationship* between the charge and the payers' burdens on or benefits received from the regulatory program." [25] (Emphasis added; JA 1668.) In so doing, however, the trial court obliterated the heart of the *Sinclair Paint* regulatory fee/special tax distinction: that there must be a causal linkage between what the fee payer did and the remedial measure funded by the charge.

The auction charges lack the nexus required by *Sinclair Paint* and its progeny.[26] The charges are imposed on one group—certain GHG emitters covered by the ARB's regulations—while revenues generated are used to fund programs that either benefit society at large *or benefit other groups of GHG emitters.*

Furthermore, these uses of GHG allowance sale proceeds do not reduce GHG emissions. Rather, as stated by the trial court, *it is the declining cap on GHG allowances rather than the auction that reduces GHG emissions.* (JA 1656 ["Over time, ARB lowers the cap, reducing the total number of allowances available to regulated sources, *thereby guaranteeing a reduction in overall emissions*"],

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[25] As discussed above, *Sinclair*'s first prong requires that there be a reasonable relationship between the amount of the fee charged and the burdens imposed by the fee payer's operations.

[26] In 2011, for example, California produced less than 1% of GHG worldwide emissions. Global GHG emissions were approximately 45,720.46 terragrams of CO2 equivalent (Tg $CO_2$ Eq.) EPA, Sources of Greenhouse Gas Emissions, Land Use, Land-Use Change, and Forestry Sector Emissions (avail. at http://www.epa.gov/climatechange/ghgemissions/sources/lulucf.html). California's GHG emissions were 450.94 Tg of $CO_2$ Eq. California Greenhouse Gas Inventory for 2000-2012, California Environmental Protection Agency Air Resources Board (last updated Mar. 24, 2014) (avail. at http://www.arb.ca.gov/cc/inventory/data/tables/ghg_inventory_scopingplan_00-12_2014-03-24.pdf).

emphasis added.) Hence, the regulatory program that mitigates the adverse effects of the regulated sources' activities is the declining cap, not the auction and reserve sale. The auction proceeds simply finance billions of dollars of general government programs. (JA 1671.) Even assuming *arguendo* that the funded programs are not general government programs (which they assuredly are), the proceeds are still being used to assist other preferred groups reduce their own carbon footprint instead of regulating the activities of those paying the charge. Either way, the auctions fail the "causal connection or nexus" test of *Sinclair Paint*.

The trial court skirted this entire issue by asserting that the auctions were not intended to "shift the costs of any particular regulatory program" but instead to "support additional regulatory programs that further the emissions reduction goals of AB 32." (JA 1674.) However, the trial court in doing so incorrectly disregarded the nexus analysis required under *Sinclair Paint*. This is because all of the programs cited by the trial court – energy efficiency, weatherization retrofits, rail modernization, transit-oriented development, livable community strategies, water system efficiency, ecosystem management, recycling, waste diversion, and conservation easements – are aimed at reducing the GHG emissions of persons *other than the those paying the auction proceeds.*[27] Indeed, the trial court conceded that "[i]n practice the allowance proceeds likely can be used for "general governmental purposes." (JA 1671.) This stands *Sinclair Paint* on its head.

For these reasons, the auction regulations fail the third and final prong of the *Sinclair Paint* test.

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[27] The massive bullet train construction project is an example of this, and in any event can hardly be called a "regulatory program."

### 5. *Sinclair Paint*'s 3-prong test, properly applied, controls this case and invalidates the auction regulations.

In its discussion on nexus and whether the amount of the auction charge is "reasonably related" to the adverse effects addressed by the regulatory activities for which the charge is levied, the trial court struggled to reconcile three decisions of this Court: *Morning Star Co. v. Bd. of Equalization* (2011) 201 Cal.App.4th 737 ("*Morning Star*"); *Equilon Enterprises v. Bd. of Equalization* (2010) 189 Cal.App.4th 865 (*Equilon*); and *Calif. Assn. of Prof. Scientists v. Dept. of Fish & Game* (2000) 79 Cal.App.4th 935 (*Calif. Assn. of Prof. Scientists*). (JA 1674.) This difficulty came from the trial court's misstatement of the *Sinclair Paint* test (discussed above at pp. 36-38), and the application of the misstated test to the *Sinclair Paint* cases. However, when the proper *Sinclair Paint* test is applied, two of the cases (*Equilon* and *Calif. Assn. of Prof. Scientists*) are not relevant to this case,[28] and the third (*Morning Star*) confirms that proper application of *Sinclair Paint* results in the conclusion that the auction charge is a tax.

*Morning Star* involved a charge imposed on businesses with more than 50 employees that "use, generate, store, or conduct activities" in the state related to hazardous materials. (201 Cal.App.4th at 743.) The revenues raised were ultimately used to pay for a wide range of hazardous waste control services and

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[28] *Equilon* did not dispute the validity of the Childhood Lead Poisoning Prevention Act, but rather only the allocation of the fee amongst fee payers. *Calif. Assn. of Prof. Scientists* dealt only with the narrow issue of whether the state could charge a flat fee to review an administrative application, or whether the fee had to be graduated based on the complexity of the application. Neither case is relevant here.

programs that were unrelated to the activity for which the charge was imposed—the use, generation, or storage of hazardous materials. (*Id.* at 755.) More pointedly, the revenues raised were used to pay for remediation, cleanup, disposal, and control of hazardous wastes of others generally rather than for the regulation of the *fee payers'* business activities in using, generating, or storing hazardous materials. (*Id.*) This Court concluded:

> Thus, the section 25205.6 charge to the Company is not regulatory because it does not seek to regulate the Company's use, generation or storage of hazardous materials but to raise money for the control of hazardous materials generally. The charge is therefore a tax. (*Id.*)

As in *Morning Star*, the auction charges here do not regulate the payer's generation of GHG — indeed the payers are allowed to continue to operate essentially unchanged. Instead, the auction proceeds pay for broad programs to *generally* reduce GHG emissions societally by changing others' behavior. The application of *Sinclair Paint* and *Morning Star* to these facts compel the conclusion that the auction and reserve sale proceeds are "special taxes" enacted without the requisite two-thirds vote of both houses of the Legislature, and are therefore invalid.

**a. Although correctly finding *Sinclair Paint* controls, the trial court's misapplication of *Sinclair Paint* effectively guts that unanimous Supreme Court decision, and must be overturned.**

The trial court correctly determined that *Sinclair Paint* controls this case, but erred by misapplying *Sinclair's* 3-prong test. If upheld, the decision below would render *Sinclair Paint* meaningless by re-writing its three-part test. Under the trial court's

reasoning, there would be no need for a reasonable relationship between the amount charged and the burdens imposed by the fee payer's operations, the charge may be used for unrelated revenue purposes, and the remedial measures funded with the charge need not have a causal connection or nexus to the fee payer's operations. Thus, any unelected regulatory body charged with regulating particular activities would have the power to impose charges in any amount on regulated persons and entities so long as the revenues were "reinvested for public benefit" having some remote or attenuated link with the regulated activity. This is irreconcilable with *Sinclair Paint*.

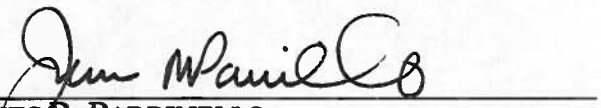
## V. CONCLUSION

For these reasons, the judgment below should be reversed.

Dated: October 17, 2014

Respectfully submitted,

NIELSEN MERKSAMER PARRINELLO GROSS & LEONI LLP



JAMES R. PARRINELLO
*Attorneys For Appellants and Petitioners*
California Chamber of Commerce and Larry Dicke

## DECLARATION OF JAMES R. PARRINELLO IN CERTIFICATION OF BRIEF LENGTH

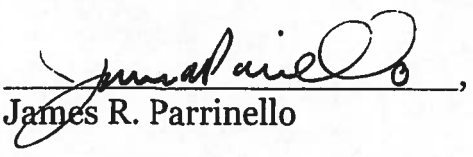
James R. Parrinello, Esq., declares:

1. I am licensed to practice law in the state of California, and am the attorney of record for Appellants in this action. I make this declaration to certify the word length of Appellants' Opening Brief.

2. I am familiar with the word count function within the Microsoft Word software program by which the Opening Brief was prepared. Applying the word count function to the Opening Brief, I determined and hereby certify pursuant to California Rules of Court Rule 8.204(c) that Appellants' Opening Brief contains 13,866 words, and is within the word count limit imposed by Rule 8.204(c).

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct and of my own personal knowledge except for those matters stated on information and belief and, as to those matters, I believe them to be true. If called as a witness, I could competently testify thereto.

Executed on October 17, 2014, at San Rafael, California.



James R. Parrinello

Cal Chamber v. California Air Resources Board
Morning Star v. California Air Resources Board
CA Court of Appeal, 3rd Appellate District
Case Nos. C075930 and C075954

**PROOF OF SERVICE**

I, the undersigned, declare under penalty of perjury that:

I am a citizen of the United States employed in the County of Marin. I am over the age of 18 and not a party to the within cause of action. My business address is 2350 Kerner Blvd., Suite 250, San Rafael, California. I am readily familiar with my employer's practices for collection and processing of correspondence for mailing with the United States Postal Service and for pickup by Federal Express.

On October 17, 2014, I served a true copy of the foregoing **CALIFORNIA CHAMBER OF COMMERCE, et al., APPELLANTS' OPENING BRIEF** on the following parties in said action, by serving the parties on the attached "Service List"

X **BY U.S. MAIL:** By following ordinary business practices and placing for collection and mailing at 2350 Kerner Blvd., Suite 250, California 94901 a true copy of the above-referenced document(s), enclosed in a sealed envelope; in the ordinary course of business, the above documents would have been deposited for first-class delivery with the United States Postal Service the same day they were placed for deposit, with postage thereon fully prepaid.

Executed in San Rafael, California, on October 17, 2014.

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

Paula Scott

Paula Scott

# SERVICE LIST

| | |
|---|---|
| Roger R. Martella (pro hac vice)<br>*Paul J. Zidlicky (pro hac vice)<br>Eric McArthur (pro hac vice)<br>Sidley Austin LLP<br>1501 K Street NW<br>Washington, DC 20005<br>pzidlicky@sidley.com<br><br>Attorneys for Intervener & Appellant<br>*National Association of Manufacturers* | *Theodore Hadzi-Antich (SBN 264663)<br>James S. Burling (SBN 113013)<br>Pacific Legal Foundation<br>930 G Street<br>Sacramento, CA 95814<br>Tel.: (916) 419-7111<br>tha@pacificlegal.org<br><br>Attorneys for Plaintiffs & Appellants<br>*Morning Star Packing Company, et al.* |
| *Sean A. Commons (SBN 217603)<br>Sidley Austin LLP<br>555 West Fifth Street<br>Los Angeles, CA 90013<br>Tel: (213) 896-6600<br>scommons@sidley.com<br><br>Attorneys for Intervener & Appellant<br>*National Association of Manufacturers* | Robert E. Asperger (SBN 116319)<br>Deputy Attorney General<br>1300 I Street<br>Sacramento, CA 95814<br>Tel. (916) 327-7582<br>Bob.Asperger@doj.ca.gov<br><br>Attorneys for Defendants & Respondents<br>*California Air Resources Board, et al* |
| *David A. Zonana (SBN 196029)<br>M. Elaine Meckenstock (SBN 268861)<br>Bryant B. Cannon (SB N 284496)<br>Deputy Attorneys General<br>California Department of Justice<br>1515 Clay Street, Suite 2000<br>P.O. Box 70550<br>Oakland, CA 94612-0550<br>Tel.: (510) 622-2145<br>David.Zonana@doj.ca.gov<br><br>Attorneys for Defendants & Respondents<br>*California Air Resources Board, et al.* | *Matthew D. Zinn (SBN 214587)<br>Joseph D. Petta (SBN 286665)<br>Shute, Mihaly & Weinberger, LLP<br>396 Hayes Street<br>San Francisco, CA 94102<br>Tel.: (415) 552-7272<br>Zinn@smwlaw.com<br><br>Attorneys for Interveners & Respondents<br>*Environmental Defense Fund* |
| *Erica Morehouse Martin (SBN 274988)<br>Timothy J. O'Connor (SBN 250490)<br>Environmental Defense Fund<br>1107 9th Street, Suite 1070<br>Sacramento, CA 95814<br>Tel.: (916) 492-4680<br>emorehouse@edf.org<br><br>Attorneys for Interveners & Respondents<br>*Environmental Defense Fund* | David Pettit (SBN 067128)<br>*Alexander L. Jackson (SBN 267099)<br>Natural Resources Defense Council<br>1314 2nd Street<br>Santa Monica, CA 90401<br>Tel.: (310) 434-2300<br>ajackson@nrdc.org<br><br>Attorneys for Interveners & Respondents<br>*Natural Resources Defense Council* |

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| California Supreme Court<br>Clerk of the Court<br>350 McAllister Street<br>San Francisco, CA 94102<br><br>***Via E-Submission*** | Sacramento County Superior Court<br>Hon. Timothy M. Frawley<br>720 Ninth Street<br>Sacramento, CA 95814 |