UPDATE: CALIFORNIA'S CAP-AND-TRADE PROGRAM UPHELD BY THE CALIFORNIA COURT OF APPEAL

Date: 7 April 2017

Energy Alert

Just yesterday, we issued an alert that discussed among other things the uncertainty surrounding California's cap-and-trade program under Assembly Bill 32 ("AB 32"). Today, that uncertainty has been lessened considerably, thanks to a state Court of Appeal decision holding that the California Air Resources Board's ("CARB") auction program is not an unconstitutional tax on California businesses.

In 2012, the California Chamber of Commerce ("Cal. Chamber") and others filed two lawsuits alleging that CARB's cap-and-trade program was unconstitutional because the agency collected auction proceeds that far outweighed AB 32's administrative costs and spent those monies on climate-friendly infrastructure projects. Describing cap-and-trade as a "tax," Cal. Chamber argued that such a tax was unconstitutional because it lacked approval by two-thirds majorities in both houses of the California State Legislature. While cap-and-trade opponents lost at the superior court, they appealed to the court of appeal, which held oral arguments earlier this year.

That appeal has now been resolved in favor of cap-and-trade. On the afternoon of April 6, the California Court of Appeal, Third Appellate District, upheld CARB's cap-and-trade regulations in a 2-1 decision, ruling that the purchase of emissions allowances is a "business-driven decision" that "conveys a valuable property interest—the privilege to pollute California's air—that may be freely sold or traded on the secondary market."[1] Unlike a tax, participation in CARB's auction process is "voluntary," and the allowances received are valuable.[2]

While there are still bills pending in the California legislature to explicitly extend cap-and-trade beyond 2020, the pressure to pass such an extension with a supermajority has likely been lessened. We expect that cap-and-trade will continue to play a large role in CARB's AB 32 Scoping Plan, and this recent decision may also spark renewed interest in CARB's quarterly allowance auctions, the next of which is scheduled for May 16, 2017. Environmental justice advocates who favor more stringent programs to reduce actual emissions may argue for stricter caps rather than opposing the entire auction process.

Cap-and-trade opponents had previously promised to press their fight to the California Supreme Court, if their bid at the court of appeal was unsuccessful. But it is looking increasingly likely that cap-and-trade will continue to be California's signature program to reduce greenhouse gas emissions at stationary sources, and CARB's interim victory will likely embolden the agency's broader efforts to fight climate change.

Notes:

[1] Cal. Chamber of Commerce v. State Air Resources Bd., No. C075930, Slip. Op. at 29 (Cal. Ct. App. Apr. 6, 2017).

©2005-2026 K&L Gates LLP. All Rights Reserved.

[2] *Id.*

This publication/newsletter is for informational purposes and does not contain or convey legal advice. The information herein should not be used or relied upon in regard to any particular facts or circumstances without first consulting a lawyer. Any views expressed herein are those of the author(s) and not necessarily those of the law firm's clients.

©2005-2026 K&L Gates LLP. All Rights Reserved.