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Exempt from Filing Fees
Government Code § 6103

IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA

Citizens for Fair REU Rates, et al.
Plaintiffs and Appellants
vs.
City of Redding, et al.
Defendants and Respondents.

Fee Fighter LLC, et al.
Plaintiffs and Appellants
vs.
City of Redding, et al.
Defendants and Respondents.

MOTION FOR JUDICIAL NOTICE IN SUPPORT OF PETITION FOR REVIEW

VOLUME I OF III

Of a Published Decision of the
Third Appellate District, Case No. C071906

Reversing a Judgment of the Superior Court of
the State of California for the County of Shasta,
Case No. 171377 (Consolidated with Case No. 172960)
Honorable William D. Gallagher, Judge Presiding

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TABLE OF AUTHORITIES

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To the Honorable Chief Justice and Associate Justices of the Supreme Court of the State of California:

Pursuant to California Rules of Court, rule 8.252, California Evidence Code section 452, subds. (d) and (h), and section 459; Petitioner City of Redding hereby moves this Court to take judicial notice of the documents attached hereto as Exhibits A through H:

A. Appellant's Opening Brief in *California Chamber of Commerce v. California Air Resources Board,* Third District Court of Appeal Case No. C075930

B. Appellant's Opening Brief in *Morning Star Packing Co. v. California Air Resources Control Board,* Third District Court of Appeal Case No. C075954

C. 2nd Amended Complaint in *Bauer v. Harris,* E.D. Cal. Case No. 11 CV 01440

D. Appellant's Opening Brief in *Capistrano Taxpayers Assn. v. City of San Juan Capistrano,* Fourth District Court of Appeal Case No. G048969

E. Complaint in *Glendale Coalition for Better Government v. City of Glendale,* Los Angeles County Superior Court Case No. BS153253

F. Complaint in *Sweetwater Authority Ratepayers Association, Inc. v. Sweetwater Authority,* San Diego Superior Court Case No. 37-2014-00029611-CM-MC-CTL

G. Respondent's Brief in *City of San Buenaventura v. United Water Conservation District*, Second District Court of Appeal Case No. B251810

H. Amicus Brief in *Great Oaks Water Co. v. Santa Clara Valley Water District*, Sixth District Court of Appeal Case No. H035260

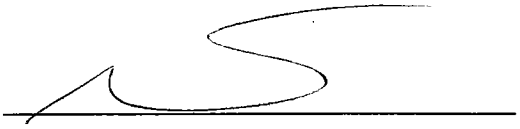
These materials are relevant to the Petition because they demonstrate the statewide significance of the issues presented in this case. Exhibits A through H show that lower courts are grappling with the very questions raised here, and will look to the Court of Appeal's published Opinion in this case for guidance. These materials also demonstrate that this Court should grant review to provide such guidance.

The above-listed materials were not presented to the trial court because they are relevant only to the unique questions presented in the Petition for Review.

This motion is based on the attached Memorandum of Points and Authorities, Declaration of Michael R. Cobden, and Exhibits A through H attached thereto, the complete records and files of this Court, and the accompanying proposed order granting this motion.

DATED: March 2, 2015

COLANTUONO HIGHSMITH & WHATLEY, PC



MICHAEL G. COLANTUONO
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MICHAEL R. COBDEN
Attorneys for Respondent
City of Redding

MEMORANDUM OF POINTS AND AUTHORITIES

I. JUDICIAL NOTICE OF BRIEFS AND PLEADINGS IN CASES PENDING IN LOWER COURTS IS APPROPRIATE TO ESTABLISH THE SIGNIFICANCE OF A LEGAL QUESTION PRESENTED FOR REVIEW

A. General Principles of Judicial Notice

A reviewing court may take judicial notice of any matter specified in Evidence Code section 452. (Evid. Code § 459.) Pursuant to Evidence Code section 452, subdivision (d) this Court may notice "[r]ecords of (1) any court of this state or (2) any court of record of the United States or of any state of the United States." The Court may also notice "facts ... that are not reasonably subject to dispute." (Evid. Code § 452, subd. (h).) Judicial notice of such facts are mandatory in the trial court upon request where the opposing party is permitted to raise objections and the court has enough information about the facts to make a determination that they come within a category subject to notice. (Evid. Code § 453, subd. (b). A reviewing court is permitted to notice facts just as is a trial court. (Evid. Code § 459, subd. (a).)

"Judicial notice is the recognition and acceptance by the court, for use ... by the court, of the existence of a matter of law or fact that is relevant to an issue in the action without requiring formal proof of the matter." (*Lockley v. Law Office of Cantrell, Green, et al.* (2001) 91 Cal.App.4th 875, 882, citations and quotations omitted.) "The

underlying theory of judicial notice is that the matter being judicially noticed is a law or fact that is **not reasonably subject to dispute.**" (*Ibid.*, original emphasis; Evid. Code § 452, subd. (h).)

B. The Court Should Notice Pleadings and Briefings from Pending State and Federal Cases

The Court should judicially notice Exhibits A through H of the Colantuono Declaration as documents duly filed in California Superior Courts, the Court of Appeal, or the United States District Court for the Eastern District of California. These documents are court records falling directly within subdivision (d) of Evidence Code section 452. Furthermore, they are documents not reasonably subject to dispute. (Evid. Code § 452, subd. (h).)

Respondent does not ask this Court to notice these documents for the truth of any fact stated within them, but for the proposition that the litigants and courts involved in those cases are grappling with the same or similar issues raised in this case. These documents are therefore relevant to the issues raised in the Petition for Review, and should be noticed in consideration of that Petition.

CONCLUSION

The City respectfully requests this Court grant Respondent's motion to notice Exhibits A–H and consider them in support of its Petition for Review.

DATED: March 2, 2015

COLANTUONO, HIGHSMITH & WHATLEY, PC

MICHAEL G. COLANTUONO
AMY C. SPARROW
MICHAEL R. COBDEN
Attorneys for Respondent
City of Redding

DECLARATION OF MICHAEL R. COBDEN

[Cal. Rules of Court, rule 8.54, subdivision (a)(2)]

1. I am an attorney in good standing licensed to practice before the courts of this state and counsel of record for Petitioner City of Redding in this matter.

2. Attached hereto as Exhibit A is a true and correct copy of the Opening Brief of Appellant National Association of Manufacturers in *California Chamber of Commerce v. California Air Resources Board,* Third District Court of Appeal Case No. C075930. I obtained this document from the Appellant's website on February 27, 2015 at the following address: http://www.nam.org/Advocacy/The-Center-for-Legal-Action/Briefs-Online/2014/NAM-Opening-Brief-in-California-Chamber-of-Commerce-v-California-Air-Resources-Board-(Cal-Ct-App)/

3. Attached hereto as Exhibit B is a true and correct copy of the Appellant's Opening Brief in *Morning Star Packing Co. v. California Air Resources Control Board,* Third District Court of Appeal Case No. C075954. I obtained this document from the Pacific Legal Foundation's website on February 27, 2015 at the following address: http://www.pacificlegal.org/document.doc?id=1689

4. Attached hereto as Exhibit C is a true and correct copy of the Second Amended Complaint in *Bauer v. Harris,* E.D. Cal. Case No. 11 CV 01440. I obtained this document from Plaintiffs' counsel's

website on February 27, 2015 at the following address: http://michellawyers.com/wp-content/uploads/2011/08/Bauer-v.-Harris_Conformed-Second-Amended-Complaint-for-Declaratory-and-Injunctive-Relief.pdf.

5. Attached hereto as Exhibit D is a true and correct copy of Appellant's Opening Brief in *Capistrano Taxpayers Assn. v. City of San Juan Capistrano,* Fourth District Court of Appeal Case No. G048969, which I obtained from my firms' files as we are Appellant's counsel there.

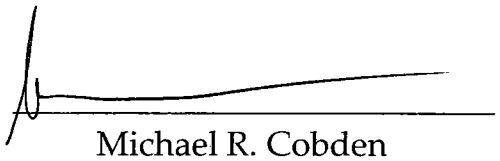
6. Attached hereto as Exhibit E is a true and correct copy of Complaint in *Glendale Coalition for Better Government v. City of Glendale,* Los Angeles County Superior Court Case No. BS153253, which I obtained from my firm's files as we are Respondent's counsel there.

7. Attached hereto as Exhibit F is a true and correct copy of the Complaint in *Sweetwater Authority Ratepayers Association, Inc. v. Sweetwater Authority,* San Diego County Superior Court Case No. 37-2014-00029611-CM-MC-CTL, which I obtained via the San Diego Superior Court's website.

8. Attached hereto as Exhibit G is a true and correct copy of Respondent's Brief in *City of San Buenaventura v. United Water Conservation District,* Second District Court of Appeal Case No. B251810, which I obtained from my firm's files as we are counsel for Respondent there.

9. Attached hereto as Exhibit H is a true and correct copy of Amicus Brief in *Great Oaks Water Co. v. Santa Clara Valley Water District*, Sixth District Court of Appeal Case No. H035260, which I obtained from my firm's files, as we obtained it from counsel for Amici there.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct. Executed this 2nd day of March 2015.



Michael R. Cobden

[Proposed]

ORDER TAKING JUDICIAL NOTICE OF DOCUMENTS

Good cause appearing, IT IS HEREBY ORDERED that Respondent City of Redding's Motion Requesting Judicial Notice is granted. IT IS ORDERED that this Court shall take judicial notice of the following:

A. Appellant National Association of Manufacturers' Opening Brief in *California Chamber of Commerce v. California Air Resources Board,* Third District Court of Appeal Case No. C075930

B. Appellant's Opening Brief in *Morning Star Packing Co. v. California Air Resources Control Board,* Third District Court of Appeal Case No. C075954

C. 2nd Amended Complaint in *Bauer v. Harris,* E.D. Cal. Case No. 11 CV 01440

D. Appellant's Opening Brief in *Capistrano Taxpayers Assn. v. City of San Juan Capistrano,* Fourth District Court of Appeal Case No. G048969

E. Complaint in *Glendale Coalition for Better Government v. City of Glendale,* Los Angeles County Superior Court Case No. BS153253

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G. Respondent's Brief in *City of San Buenaventura v. United Water Conservation District,* Second District Court of Appeal Case No. B251810

H. Amicus Brief in *Great Oaks Water Co. v. Santa Clara Valley Water District,* Sixth District Court of Appeal Case No. H035260.

DATED: _____ By:_____
Chief Justice Tani Cantil-Sakauye

EXHIBIT A

Nos. C075930, C075954

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA
THIRD APPELLATE DISTRICT

CALIFORNIA CHAMBER OF COMMERCE, *et al.*,

Appellants,

v.

CALIFORNIA AIR RESOURCES BOARD, *et al.*,

Respondents.

On Appeal from the Superior Court of California
County of Sacramento, Hon. Timothy M. Frawley
Nos. 34-2012-80001313, 34-2012-80001464

OPENING BRIEF OF APPELLANT THE NATIONAL ASSOCIATION OF MANUFACTURERS

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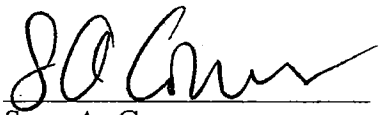
Counsel for The National Association of Manufacturers

CERTIFICATE OF INTERESTED ENTITES OR PERSONS

Pursuant to Rule 8.208, I certify that no party or entity has a 10% or greater ownership interest in The National Association of Manufacturers, and no other person or entity has a financial or other interest in the outcome of the proceeding within the meaning of Rule 8.208(e)(2).



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INTRODUCTION

The National Association of Manufacturers ("the NAM") submits this brief challenging the decision of the Superior Court (Frawley, J.) upholding regulations adopted by the California Air Resources Board ("ARB" or "Board"), establishing auctions and reserve sales for greenhouse gas ("GHG") emission allowances that are projected to generate revenues of between $12 and $70 billion over and above the regulatory fees separately collected to implement and enforce Assembly Bill 32 ("AB 32").

The issues presented are:

(i) Whether AB 32 authorizes the Board's regulations providing for the sale of GHG allowances at auctions and reserve sales to generate billions of dollars in revenues for the State; and

(ii) If AB 32 provides that authorization, whether AB 32 violates the California Constitution because it imposes a tax that was not adopted by a two-thirds supermajority of the California Legislature.

I. AB 32 does not authorize the Board to generate billions of dollars in revenues over and above the regulatory fees separately authorized and collected to implement and enforce AB 32. The language, structure, purpose, and legislative history of AB 32 all confirm that the Board is not authorized to generate such extraordinary revenues—the largest of any environmental program in the United States. AB 32 nowhere grants such

wide-ranging authority, but is instead structured to grant the Board carefully circumscribed authority to collect regulatory fees that are necessary to implement and enforce AB 32. Given that express, but limited, grant of authority to collect regulatory fees, the authorization to collect billions in additional revenues is not, as the court below concluded, a "detail" that the Legislature implicitly intended the Board to "fill up." (JA 1573, 1575.) As the California Supreme Court has explained, the "'drafters of legislation do not ... hide elephants in mouseholes.'" (*Cal. Redevelopment Ass'n v. Matosantos* (2011) 53 Cal.4th 231, 260–61.) Contrary to the Superior Court's conclusion, the Legislature would not "have silently, or at best obscurely, decided so important ... a public policy matter and created a significant departure from the existing law." (*In re Christian S.* (1994) 7 Cal.4th 768, 782.) Indeed, even if AB 32 could be viewed as ambiguous on this issue, California law *requires* the statute to be construed to *avoid* the need to resolve serious constitutional questions presented by the lower court's construction of AB 32.

II. The Superior Court's construction of AB 32 to authorize the Board to generate billions in revenues through auctions and reserve sales renders AB 32 unconstitutional because the collection of such revenues is an unlawful tax adopted under a statute passed without the necessary two-thirds supermajority of the Legislature. Under the three-part test set forth by

the Supreme Court in *Sinclair Paint Co. v. State Board of Equalization* (1997) 15 Cal.4th 866—which respondents did not even attempt to satisfy below—the allowance revenues are unconstitutional taxes. *First*, the allowance revenues vastly exceed the amount necessary to implement and enforce AB 32, which is already fully funded through a separate statutory provision expressly authorizing the collection of regulatory fees. *Second*, there has been *no* showing that the relationship between the revenues generated and the regulatory burden imposed by the regulated parties' operations is reasonable. *Third*, the primary purpose of a program projected to generate tens of billions in revenues is undoubtedly revenue generation. That conclusion is inescapable where, as here, those revenues (i) are not necessary to meet the GHG reduction goals of the Cap-and-Trade Program or to implement or enforce AB 32, and (ii) have been set aside to fund programs that have not yet been identified.

STATEMENT OF THE CASE

A. The California Constitution

In 1978, California voters adopted Proposition 13, which provides that "any changes in State taxes enacted for the purpose of increasing revenues collected pursuant thereto ... must be imposed by an Act passed by not less than two-thirds of all members elected to each of the two houses of the Legislature." (Cal. Const., art. XIIIA, § 3.) Under Proposition 13, the

California Constitution requires a supermajority vote of each house of the Legislature before a new tax can take effect. This constitutional provision was in effect when the Legislature enacted AB 32.[1]

B. The Global Warming Solutions Act of 2006 ("AB 32")

In 2006, the Legislature enacted AB 32, which was passed by 59% of the Assembly and 58% of the Senate, less than two-thirds of all the members of either house of the Legislature. (JA 1578.)

AB 32 designates ARB as the "state agency charged with monitoring and regulating sources of emissions of greenhouse gases that cause global warming in order to reduce emissions of greenhouse gases." (Health & Safety Code § 38510.) It further directs ARB to "adopt regulations to require the reporting and verification of statewide greenhouse gas emissions and to monitor and enforce compliance with this program," (*id.* § 38530(a)), and requires ARB to "determine what the statewide greenhouse gas emissions level was in 1990, and approve ... a statewide

[1] In 2010, California voters amended Article XIIIA of the California Constitution by approving Proposition 26. Proposition 26 provides that, after January 1, 2010, subject to certain exceptions, "[a]ny change in state statute which results in any taxpayer paying a higher tax must be imposed by an act passed by not less than two-thirds of all members elected to each of the two houses of the Legislature." Under Proposition 26, the definition of "tax" includes "any levy, charge, or exaction of any kind imposed by the State," with specified exceptions. (Cal. Const., art. XIIIA, § 3(a)–(b).)

greenhouse gas emissions limit that is equivalent to that level, to be achieved by 2020." (*Id.* § 38550.)

AB 32 states that ARB may "adopt rules and regulations ... to achieve the maximum technologically feasible and cost-effective greenhouse gas emission reductions from sources or categories of sources, subject to the criteria and schedules set forth in this part." (*Id.* § 38560.) Further, AB 32 authorizes ARB to include "market-based compliance mechanisms to comply with the regulations." (*Id.* § 38570.) AB 32 *limits* that authority, however, by requiring that ARB "[d]esign the regulations, including distribution of emissions allowances where appropriate, in a manner that is equitable, seeks to minimize costs and maximize the total benefits to California, and encourages early action to reduce greenhouse gas emissions." (*Id.* § 38562(b)(1).)

Finally, AB 32 requires ARB to "adopt by regulation, after a public workshop, a schedule of fees to be paid by the sources of greenhouse gas emissions regulated pursuant to [AB 32], consistent with Section 57001." (*Id.* § 38597.) Section 57001, in turn, ensures that "that the amount of each fee is not more than is reasonably necessary to fund the efficient operation of the activities or programs for which the fee is assessed." (*Id.* § 57001(a).) The "revenues collected" under § 38597 must be "deposited into the Air

Pollution Control Fund and are available upon appropriation, by the Legislature, for purposes of carrying out [AB 32]." (*Id.*)

C. The Board's Cap-and-Trade Regulation Proposal

On October 28, 2010, ARB issued a proposed regulation to establish a Cap-and-Trade Program. The proposed Cap-and-Trade Program would require certain industrial and utility sources of GHGs to acquire, and later surrender to ARB, an "allowance" for every metric ton of CO_2e they emitted during multi-year compliance periods. (*See* ARB, Staff Report: Initial Statement of Reasons, Proposed Regulation to Implement the California Cap-and-Trade Program ("ISOR") ES-2.) ARB proposed to reduce, over time, the total number of allowances available for each compliance period, thereby reducing the total level of GHGs that could be lawfully emitted in California by these regulated industries. (*Id.* at ES-3.) ARB acknowledged that the method of allocating allowances does not affect the amount of GHG reductions achieved because "[t]he limit on GHG emissions—the program 'cap'—determines the environmental effectiveness of the cap-and-trade program." (*Id.*) ARB's analysis was confirmed by the Legislative Analyst's Office ("LAO"). "[A]n allowance auction is not necessary to meet the AB 32 goal of reducing GHG emissions statewide to 1990 levels by 2020," the LAO concluded, "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." (JA 499.)

Under its proposal, ARB would grant, without charge, some allowances to entities regulated by Cap-and-Trade, and sell some allowances at public auctions and set-price reserve sales payable to the State of California. *Id.* ARB did not propose that the revenues collected be used to implement or enforce AB 32. Instead, ARB proposed that auction revenues be appropriated by the Legislature to "use the revenue for public benefit" by, for example, (i) redistributing allowance proceeds from fuel suppliers directly to consumers to help offset the higher fuel costs that would be passed along to consumers, (ii) funding a "Community Benefit Fund," and (iii) establishing a competitive grant program to invest in projects like research into low-GHG technologies or workforce training. (*Id.* at II-29–II-30.[2])

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[2] In Board Resolution 10-42, adopted on December 16, 2010, ARB recommended the use of "allowance value," *i.e.*, revenue generated from the auction and sale of allowances, to finance public and private investments oriented toward (i) "green job training," (ii) "economic opportunities and environmental improvements in disadvantaged communities," (iii) "adaptation to climate change," and (iv) "low-cost GHG emissions reductions, including investments in energy efficiency, public transit, transportation and land-use planning, and research, development, and deployment." (JA 419–20.) ARB also recommended that allowance revenues be "[r]eturn[ed] ... to households either through lump-sum rebates ... or through cuts or avoided increases in the State's individual income or sales tax rates." (JA 420.)

D. Cap-and-Trade Final Statement of Reasons

Commenters objected that ARB's "proposal to raise funds via an auction for reasons outside of administrative fee purposes is beyond [ARB]'s regulatory authority." (ARB, Final Statement of Reasons for Rulemaking, California's Cap-and-Trade Program ("FSOR") 731.) Commenters explained that the auction revenue proposals were "contrary to the legislative intent of AB 32," (*id.*), and that "an auction and its proceeds are not only unauthorized by AB 32, but equate to a tax that will require 2/3 vote of the legislature." (*Id.* at 723.) In response, ARB admitted that AB 32 "does not direct ARB to use any particular method to distribute allowances, and does not specify that some methods are allowed and others are not," but insisted that "the Legislature did not intend to forbid ARB from choosing this widely recognized distribution method." (*Id.* at 732.)

Further, ARB stated that while "[t]here are a variety of ways to allocate allowances," auctioning is "the method that has been recommended by the Market Advisory Committee and many other economists." (*Id.*) The Market Advisory Committee explained that "[t]he method by which emission allowances are distributed under a cap-and-trade program does not affect the total greenhouse gas emissions under the program, but will affect the distribution of economic costs associated with meeting California's greenhouse gas emission targets." (ISOR, App. H, at H-9.) The Committee

recommended that revenues from auctions, *i.e.*, "allowance value," be "utilized to provide transition assistance for workers and industries subject to strong market pressures from competitors operating in jurisdictions that lack similar caps on greenhouse gas emissions." (*Id.* at H-9–H-10.[3]) The Committee recognized that "[s]ome observers have suggested that [ARB] may not have the authority to auction and that auctioning might require further legislative action." (*Id.* at H-70.)

ARB did not directly address the argument that the sale of allowances constituted a tax that required a two-thirds supermajority vote of the Legislature. Instead, ARB responded that it believes "that in authorizing ARB to distribute allowances, and requiring that market-based compliance mechanisms must meet certain criteria, the Legislature did not intend to forbid ARB from choosing this widely recognized distribution method. In other words, as the administrating agency charged with interpreting AB 32, ARB believes that AB 32 provides ARB with the authority to include auctions as a feature of a cap-and-trade program." (FSOR 732, 2190.)

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[3] The Committee recommended that the "state could also offset the economic impact of the program by using auction revenues to finance reductions in income taxes or other taxes that distort economic decisions." (ISOR, App. H, at H-68.) Thus, "[i]f allowances are auctioned, some of the revenue from the auction can be used to finance reductions in State tax rates, or can be returned to taxpayers directly through rebate checks, perhaps on a per-capita basis." (*Id.*)

E. The Cap-and-Trade Regulation

On October 20, 2011, ARB adopted the Cap-and-Trade Regulation, which went into effect on December 22, 2011. Under the regulation, ARB grants some allowances without charge and sells others to generate revenues through auctions and reserve sales, with increasing reliance upon auctions and reserve sales in later compliance periods. (17 CCR §§ 95870, 95910–95914.) The NAM's lawsuit challenges the regulations through which ARB auctions and sells increasing percentages of emission allowances each year to generate revenues for the State.

On June 28, 2012, ARB approved amendments to the Cap-and-Trade Regulation, which went into effect on September 1, 2012. The Cap-and-Trade Regulation, as amended, requires certain "covered entities" responsible for annual GHG emissions greater than or equal to 25,000 metric tons CO_2e to acquire a "compliance instrument," *i.e.*, an allowance, for every metric ton of CO_2e they emit, and then surrender these compliance instruments to ARB annually. (*Id.* §§ 95811–12, 95850, 95855–56.) This requirement is known as a covered entity's "compliance obligation." (*Id.* § 95802(54).)

Failure to meet a compliance obligation, or other violations under the Cap-and-Trade Regulation, subjects regulated entities to potential penalties, including civil fines and criminal penalties up to and including

incarceration. (*Id.* §§ 96013–14; Health & Safety Code § 38580.) ARB decreases the number of GHG emission allowances each year. (17 CCR § 95841.) This declining "cap" on total permissible emissions is the mechanism by which the Cap-and-Trade Program reduces GHG emissions.[4]

The Cap-and-Trade Regulation provides that a portion of the GHG allowances ARB creates each year will be allocated directly to certain utilities and other industrial covered entities. (*Id.* §§ 95890–92.) Within the utility and industrial sectors eligible for direct allocation of allowances, ARB distributes GHG allowances to individual entities based upon industrial output. (*Id.* §§ 95891, 95892 & tbls. 9-1 & 9-3.) The proportion of allowances designated for free direct allocation diminishes each year. (*See, e.g.*, *id.* §§ 95870, 95891 & tbl. 9-2.) By 2020, ARB plans to allocate directly approximately 50% of GHG allowances. (JA 457.) Allowances that are not directly allocated by ARB are sold in 1,000-allowance bundles through public auctions and reserve sales. (17 CCR §§ 95910–14.)

[4] The Cap-and-Trade Regulation phases in participation in the Cap-and-Trade Program over three successive "compliance periods." (17 CCR §§ 95840, 95851.) The first period, from January 1, 2013, to December 31, 2014, requires participation from specified utility and heavy industry sectors. (*Id.*) The second and third compliance periods, from January 1, 2015, to December 31, 2017, and from January 1, 2018, to December 31, 2020, respectively, expand participation to other industries that account for mobile GHG emissions. (*Id.*)

The initial GHG allowance auction took place on November 14, 2012. (*Id.* § 95910(a)(1).) Subsequent auctions are scheduled on a quarterly basis. (*Id.* § 95910(a)(2).) The first reserve sale was on March 8, 2013. Future reserve sales are scheduled to occur six weeks after each quarterly auction. (*Id.* § 95913(d).) The auctions "consist of a single round of bidding." (*Id.* § 95911.) "No allowances will be sold at bids lower than" a minimum "auction reserve price." (*Id.*) "The Auction Reserve Price for ... allowances auctioned in 2012 will be $10 per allowance." (*Id.*) For future auctions, "the Auction Reserve Price" will be "increased annually by 5 percent plus the rate of inflation." (*Id.*)

At the November 14, 2012 quarterly auction, ARB offered 23,126,110 allowances for the 2013 compliance period. (JA 503.) ARB sold all the allowances offered at auction at a settlement price of $10.09 per allowance, for a total of over $233 million dollars in revenue generated. (*Id.*) ARB also sold 5,576,000 allowances for the 2015 compliance period at a cost of $10.00 per allowance. (*Id.*) At the November 14, 2012 auction, ARB raised nearly $289 million dollars for the State of California. (*Id.*) The LAO estimated that in fiscal year 2012–13, ARB's auctions would "generate roughly $660 million to upwards of $3 billion." (JA 485.) Over the life of the program, the LAO estimated that ARB would raise as much as $12 billion to $70 billion in additional revenue for the State. (JA 1566.)

For each compliance period, ARB withholds a percentage of the GHG allowances it creates for "reserve sales." (17 CCR § 95870(a).) At reserve sales, ARB sells GHG allowances at specific tiers of escalating prices. The reserve sale prices for the initial March 8, 2013 reserve sale ranged from $40 to $50 per allowance. Each year, the price of allowances at reserve sales is "increased by five percent plus the rate of inflation." (*Id.* § 95913(e).) Like the allowances sold at auction, the proportion of allowances designated for reserve sales increases each compliance period. (*Id.* § 95870(a).)

F. The Cap-and-Trade Fee Regulation

Pursuant to Health and Safety Code § 38597, ARB also promulgated an "AB 32 Cost of Implementation Fee" regulation ("Fee Regulation"). As explained by ARB, "[t]he purpose of [the Fee Regulation] is to collect fees to be used to carry out [AB 32] as provided in Health and Safety Code section 38597." (*Id.* § 95200 [citations omitted].) The Fee Regulation assesses fees on utility and industry sectors based on the amount of fuel combusted or distributed, the amount of CO_2 released, or the amount of electricity generated or imported by a regulated party, depending upon the sector. (*Id.* § 95201.) Under the Fee Regulation, the revenue collected "shall be the total amount of funds necessary to recover the costs of implementation of AB 32 program expenditures for each fiscal year," as

well as "payments required to be made by [ARB] on the Debt incurred," and "any amounts required to be expended by [ARB] in defense of [the Fee Regulation] in court." (*Id.* § 95203(a).) "If there is any excess or shortfall in the actual revenue collected for any fiscal year, such excess or shortfall shall be carried over to the next year's calculation of the Total Revenue Requirement." (*Id.*)

The total required revenue under the Fee Regulation for fiscal year 2010–11 was $62.1 million. (JA 509.) For fiscal year 2012–13, ARB concluded that the total revenue required to implement and enforce AB 32 was $62 million. (*Id.*) These annual fee estimates are dwarfed by the nearly $290 million in revenues generated at the first quarterly auction in November 2012.

G. Post-AB 32 Legislation

Since the enactment of AB 32, the Legislature has enacted additional laws—SB 1018, AB 1532, SB 535, and AB 383—providing that the auction and reserve sale revenues must be deposited into a Greenhouse Gas Reduction Fund and used to facilitate reduction of GHG emissions. (Gov't Code § 16428.8; Health & Safety Code §§ 39711–12.) In addition, in 2014, the Legislature enacted SB 862, which provides for the expenditure of the allowance revenues on a wide variety of projects unrelated to the regulation of the payers' activities, such as the construction of high-speed rail.

H. The Decision Below

Below, the Superior Court upheld ARB's regulations authorizing revenue-generating auctions and reserve sales. The court acknowledged that "over the life of the program" the auctions and reserves sales "will raise as much as $12 to $70 billion in revenues for the State." (JA 1566, 1570.) And the court acknowledged that these additional revenues were separate from and in addition to the regulatory fees collected under AB 32's express authorization for "ARB to collect a fee to recover the administrative costs of carrying out AB 32." (JA 1570.)

The court acknowledged that California law prohibits the delegation of "legislative power" to unelected state agencies and that any delegation must be circumscribed with "suitable standards" to guide the delegation and "to protect against misuse." (JA 1572.[5]) Nevertheless, the court believed that an "agency is authorized to 'fill up the details' of the statutory scheme." (JA 1573.) The court correctly acknowledged that "AB 32 does not explicitly authorize the sale of allowances," but concluded that by "broadly delegat[ing] the choice of distribution methods to ARB, if the Legislature had meant to exclude the sale of allowances, it would have done

[5] According to the court, "allowance allocation" has "financial consequences" that create "'winners' and 'losers'" among participants, and therefore allocation involves "a 'tough political decision' about who is to be the recipient of the value created by the [allowances]." (JA 1573.)

so" but "did not." (JA 1574–75.) The court failed to apply California law requiring that courts interpret statutes to *avoid* addressing serious constitutional questions, (*cf.* JA 1574 n.5]), even though it later ruled that the constitutionality of AB 32 under the Court's interpretation presented a "close question." (JA 1581.)

The court next addressed whether AB 32, if interpreted to authorize ARB to generate billions in excess revenues through the sale of allowances, imposes an unconstitutional tax in violation of Proposition 13. (JA 1576.) The court acknowledged that under Proposition 13, "'any changes in State taxes enacted for the purpose of increasing revenues' must be approved by a supermajority (two-thirds) vote of each house of the Legislature." (*Id.*) Because AB 32 was not passed by a two-thirds supermajority of the Legislature, the court explained that "if the auction provisions of AB 32 are 'changes in State taxes enacted for the purpose of increasing revenues,'" then "the auction provisions are invalid." (JA 1578.)

On that issue, the court noted that the "auction provisions of AB 32 will result in a cumulative net increase in state revenues" of "as much as $12 to $70 billion." (*Id.*) Nevertheless, the court concluded that "the charges" for allowances "are more like traditional regulatory fees than taxes, but it is a close question." (JA 1581.) *First*, notwithstanding that (i) ARB's auctions were estimated to generate staggering revenues, and

(ii) selling allowances was not necessary to meet the emissions targets of AB 32, the court ruled that the "primary purpose of the charges was regulatory." (JA 1584.) *Second*, the court acknowledged that (i) "the costs of the cap and trade program will be recovered by fees collected under § 38597," and (ii) the "proceeds of the sales of allowances will not be used to offset the costs of the cap-and-trade program," but then ruled that "the total amount of fees collected will not exceed the costs of the regulatory activities they support" because "the proceeds can only be used to advance the regulatory purposes of AB 32." (JA 1585.) *Finally*, the court noted that "[u]nlike a traditional *Sinclair*-type fee, the allowance charges are not intended to shift the costs of a particular regulatory program to those responsible for the problem that the program was designed to address." (JA 1586.) Nevertheless, the court ruled that "[u]nder the unique circumstances of this case, the court is not persuaded that the amounts charged for allowances must be closely linked to the payers' burdens on the specific regulatory programs that will be funded by them." (JA 1587.) The Court entered a final judgment based on this ruling, and NAM timely appealed pursuant to Code of Civil Procedure § 904.1(a)(1).

STANDARD OF REVIEW

The legal issues presented are reviewed de novo: (i) whether AB 32 authorizes ARB to raise billions of dollars in new revenue for the State by

auctioning and selling allowances, and (ii) if so, whether such authorization is an unconstitutional tax. (*Citizens to Save Cal. v. FPPC* (2006) 145 Cal.App.4th 736, 747 ["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"]; *Cal. Farm Bureau Fed'n v. State Water Res. Control Bd.* (2011) 51 Cal.4th 421, 436 ["Whether [a statute] imposes a tax or a fee is a question of law decided upon an independent review of the record."].)

ARGUMENT

I. AB 32 Does Not Authorize The Board To Raise Billions In Excess Revenue By Auctioning And Selling Allowances.

The text, structure, purpose, and history of AB 32 establish that the Board's regulations for raising billions in excess revenues through the auction and sale of allowances were not authorized by AB 32. Nothing in AB 32 empowers the Board to collect billions of dollars over and above the regulatory fees that are expressly authorized by the Legislature to implement and enforce AB 32. The contrary reading adopted by the court below—that the Legislature, *implicitly*, granted ARB authority to collect a second stream of regulatory fees that dwarf the regulatory fees expressly authorized by the Legislature—is unsupported by the text, contrary to the structure, and unnecessary to the purpose of AB 32. It is implausible that the Legislature implicitly would have delegated to ARB the authority in AB 32 to collect billions in excess revenues that were not needed to implement

and enforce AB 32. And, even if AB 32 *could* plausibly be read to authorize ARB to generate these massive revenues, California law *requires* that such a reading be rejected to avoid the serious questions that would arise about AB 32's constitutionality.

A. AB 32's Text, Structure, Purpose, and Legislative History Show That ARB Lacks Authority To Raise Revenue By Auctioning And Selling Allowances.

When construing AB 32, the Court's task is "is to ascertain the intent of the Legislature so as to effectuate the purpose of the law." (*Dyna-Med, Inc. v. Fair Emp't & Hous. Comm'n* (1987) 43 Cal.3d 1379, 1386.) The Court "must look first to the words of the statute themselves, giving to the language its usual, ordinary import and according significance, if possible, to every word, phrase and sentence in pursuance of the legislative purpose." (*Id.* at 1386–87.) "'Statutes must be harmonized, both internally and with each other, to the extent possible,'" to avoid "'[i]nterpretive constructions which render some words surplusage.'" (*Peralta Cmty. Coll. Dist. v. Fair Emp't & Hous. Comm'n* (1990) 52 Cal.3d 40, 51; *see also, e.g., Dyna-Med*, 43 Cal.3d at 1387.) Courts apply these structural canons with particular force where, as here, an agency asserts a power that is not expressly articulated by the statute. (*See, e.g., Peralta*, 52 Cal.3d at 51; *Dyna-Med* Cal.3d at 1387.)

1. No provision of AB 32 expressly authorizes the Board to raise billions of dollars in revenue through the auction and sale of emission allowances. That omission is critical because "administrative agencies have only the powers conferred on them" by the Legislature. (*AFL v. Unemployment Ins. Appeals Bd.* (1996) 13 Cal.4th 1017, 1042.) An "'agency cannot by its own regulations create a [power] which the Legislature has withheld,'" (*id.* at 1035 [quoting *Dyna-Med*, 43 Cal.3d at 1389]), and therefore "[a]dministrative regulations that alter or amend the statute or enlarge or impair its scope are void." (*Dyna-Med*, 43 Cal.3d at 1389 [internal quotation marks omitted].) Here, the court below acknowledged that "AB 32 does not explicitly authorize the sale of allowances." (JA 1574.)

The absence of express authority to collect billions in revenues is particularly stark because "'the power to collect ... the revenue of the State is one peculiarly within the discretion of the Legislature.'" (*In re Att'y Discipline Sys.* (1998) 19 Cal.4th 582, 595 [quoting *Myers v. English* (1858) 9 Cal. 341, 349].) The omission of express authority to generate massive excess revenues is likewise probative given that AB 32 establishes a comprehensive regulatory regime. Nowhere within that regime, however, does AB 32 expressly empower the Board to raise excess revenues by auctioning and selling allowances as part of the Cap-and-Trade Regulation.

(*See AFL*, 13 Cal.4th at 1034 [refusing to imply a power where the Legislature "could have easily" granted the power expressly "as it has in other administrative contexts"].)

The decision below erroneously converts this omission (or silence) into an express authorization by concluding that "if the Legislature had meant to exclude the sale of allowances, it would have said so." (JA 1575.) This precise form of argument was rejected in *Diageo-Guinness USA, Inc. v. State Board of Equalization* (2012) 205 Cal.App.4th 907, where the Court of Appeal ruled that "the existence of a regulatory power" cannot be "based on the absence of a prohibition against the exercise of such a power." (*Id.* at 915.) Rather, a state agency may only exercise regulatory powers the Legislature actually grants to it. (*Id.*)

2. The structure of AB 32 confirms that the Legislature's failure to authorize ARB to generate billions in excess revenues was not inadvertent, but was by design. Section 38597 of AB 32 demonstrates that when the Legislature intended to authorize the Board to raise revenues, it said so explicitly. (*Id.* § 38597.) In detailed terms, § 38597 grants the Board the power to adopt "a schedule of fees," from particular entities, to be deposited in a specific fund, to be "available upon appropriation, by the Legislature," according to established procedures, and in amounts not more than "reasonably necessary to fund" AB 32's operations. (*Id.* [cross-

referencing § 57001(a), which governs administrative fees and caps them to "reasonably necessary" amounts].) This clear expression that the Board may raise revenue through § 38597's carefully circumscribed procedures precludes the inference that AB 32 *implicitly* grants ARB limitless authority to generate a distinct, much larger, revenue stream through the auction and sale of emission allowances. As the California Supreme Court has explained, "[i]n the grants of powers and in the regulation of the mode of exercise, there is an implied negative; an implication that no other than the expressly granted power passes by the grant; that it is to be exercised only in the prescribed mode." (*Wildlife Alive v. Chickering* (1976) 17 Cal.3d 190, 196 [internal quotation marks and alteration omitted]; *see also Peralta*, 52 Cal.3d at 51 ["Statutes must be harmonized, both internally and with each other, to the extent possible"]; *United Farm Workers of Am. v. Agric. Labor Relations Bd.* (1995) 41 Cal.App.4th 303, 317; *B.C. Cotton, Inc. v. Voss* (1995) 33 Cal.App.4th 929, 955–56.[6]) Indeed, the provisions

[6] Section 38597 does not authorize the generation of revenues through the sale of allowances at auctions or reserve sales. Contrary to the language of § 38597, the auctions and reserve sales are not conducted pursuant to a "schedule of fees," and are not intended to cover AB 32's "reasonably necessary" implementation costs. (Health & Safety Code §§ 38597, 57001(a).) ARB has adopted an entirely separate, detailed Fee Regulation, with a schedule of fees that covered entities must pay to fund "the costs of implementation of AB 32 program expenditures" and related costs. (17 CCR § 95203(a).) ARB's adoption of this Fee Regulation confirms that it does not, and could not, invoke § 38597 as authority to raise additional revenue by auctioning and selling allowances.

authorizing ARB to establish Cap-and-Trade include none of § 38597's detailed terms—no mention of "fees," no identification of the payers or the funds into which revenue would be deposited, no limitation on the amounts to be collected, and no limits on how such revenues are to be used.

The Superior Court recognized that the Legislature's inclusion of the administrative fee provision "does ... aid Petitioners' interpretation," (JA 1576 n.6), but nevertheless reasoned that "the agency is not limited to the exact provisions of the statute in adopting regulations to enforce its mandate" and is "authorized to 'fill up the details of the statutory scheme.'" (JA 1573.) According to the court, (i) AB 32 authorized ARB to adopt a cap-and-trade system, (*id.*), (ii) a cap-and-trade system requires the distribution of allowances, (*id.*), and (iii) AB 32 "authorized ARB to '[d]esign the regulations, including distribution of emissions allowances.'" (JA 1574 [quoting § 38562(b)(1)].) The authority to design regulations for the distribution of allowances is not blanket authority for ARB to generate billions in excess revenues.[7]

[7] To be precise, § 38561(b) grants ARB generic rulemaking authority to implement "Market-Based Compliance Mechanisms" under AB 32. The court, however, relied on different statutory language, in subsection 38561(b)(1), which requires that ARB "[d]esign the regulations, including distribution of emissions allowances where appropriate, *in a manner that is equitable, seeks to minimize costs and maximize the total benefits to California, and encourages early action to reduce greenhouse gas emission.*" (Health & Safety Code § 38561(b)(1) [emphasis added].) This language does not *grant* ARB additional authority, but instead imposes

The court's contrary conclusion ignores the healthy "skepticism" with which California courts view claims that the Legislature has "alter[ed] the fundamental details of a regulatory scheme in vague terms or ancillary provisions." (*Clayworth v. Pfizer, Inc.* (2008) 165 Cal.App.4th 209, 240.) California courts repeatedly have rejected arguments that "'the Legislature would have silently, or at best obscurely, decided so important ... a public policy matter and created a significant departure from the existing law.'" (*Garcia v. McCutchen* (1997) 16 Cal.4th 469, 482 [quoting *In re Christian S.* (1994) 7 Cal.4th 768, 782].[8]) Put plainly, California courts presume that "the drafters of legislation 'd[o] not ... hide elephants in mouseholes.'" (*Cal. Redevelopment Ass'n*, 53 Cal.4th at 260–61; *accord Whitman v. Am. Trucking Ass'ns, Inc.* (2001) 531 U.S. 457, 468 [the legislature "does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions"].)

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limitations (including limitations on the "distribution of emissions allowances") on ARB's generic rulemaking authority.

[8] (*See State Bldg. & Constr. Trades Council v. Duncan* (2008) 162 Cal.App.4th 289, 323 ["Courts do not lightly conclude that substantial statutory changes are intended or accomplished by legislative misdirection"]; *Ailanto Props., Inc. v. City of Half Moon Bay* (2006) 142 Cal.App.4th 572, 589 ["we 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"].)

Nor can the delegation of Legislative authority to generate billions in excess revenues be deemed a "detai[l]" that ARB is "authorized to fill up." (JA 1573.) That conclusion is inescapable in this context because "the power to collect and appropriate the revenue of the State is one peculiarly within the discretion of the Legislature." (*In re Att'y Discipline*, 19 Cal.4th at 595.) The legislative power to collect revenue has long been understood as "'a very delicate and responsible trust, and if not used properly by the Legislature at one session, the people will be certain to send to the next more discreet and faithful servants.'" (*Estate of Cirone v. Corey* (1987) 189 Cal.App.3d 1280, 1288 [quoting *Myers*, 9 Cal. at 349].) It is implausible that the Legislature would delegate to the Board, *by implication*, the authority to generate billions in excess revenues for the government "without so much as a passing reference to what it was doing." (*Ailanto Props., Inc. v. City of Half Moon Bay* (2006) 142 Cal.App.4th 572, 589.) To the contrary, the Legislature cannot be presumed so easily to "divest itself of its constitutionally granted powers." (*Cal. State Employees' Ass'n. v. State* (1973) 32 Cal.App.3d 103, 108.)

Nor does the authority to adopt regulations governing the distribution of allowances necessarily imply authorization to generate billions in excess revenues. As the Court and the Board have acknowledged, "[m]any different methods can be used to distribute

allowances free of charge." (JA 1573; FSOR 732; ISOR, App. H, at H-66–H-67.) To be sure, the sale of allowances is one form of distribution. But even the "sale" of allowances does not imply authority to generate revenues for California. Indeed, the federal cap-and-trade program referenced by the Board and the court below, which expressly authorizes the sale of allowances, does so in a revenue-neutral manner, *i.e.*, the money collected was redistributed, pro rata, back to industry participants.[9] Under the federal model identified by the court, "[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 Administrator." (42 U.S.C. § 7651o(d)(3).)

Here, the Legislature would not have delegated authority to ARB to raise billions of dollars without saying so expressly and without specifying how those revenues were to be used. Indeed, inferring from AB 32's silence an open-ended authority to raise unlimited revenues would render § 38597's circumscribed fee provisions surplusage. The Legislature's imposition of strict constraints on the amount of regulatory fees collected by the Board from regulated parties under § 38597 would be meaningless if the Board were authorized to generate vastly greater revenue streams from

[9] Under that program, EPA allocates 97.2% of allowances without charge and reserves 2.8% for sale or auction, directing that all proceeds of the sales and auctions be returned to covered entities in a prescribed formula (and not retained as revenue for the federal government). (42 U.S.C. § 7651o(b), (c)(6); *see* 40 C.F.R. § 73.27.)

these same parties through the auction and sale of emission allowances. (*See Peralta,* 52 Cal.3d at 51 [rejecting the agency's claim to "a legislative grant by implication of unbridled power ... to make monetary awards without guidelines or limitations"].) Construing § 38597 to be the Board's exclusive revenue-raising power under AB 32 preserves § 38597's independent meaning and harmonizes the entirety of AB 32.[10]

Applying similar principles, the California Supreme Court twice rejected claims by the Fair Employment and Housing Commission that statutory language empowering it to "take such action, including but not limited to" specified remedial actions on behalf of victims of discrimination, implied the additional powers to impose punitive and compensatory damages, respectively. (*See Dyna-Med*, 43 Cal.3d at 1387–88; *Peralta*, 52 Cal.3d at 51.) In both cases, the Supreme Court noted that the Legislature demonstrated its ability expressly to authorize damages remedies in other statutes, and therefore refused to "infe[r] that the

[10] Other statutes, too, confirm that the Legislature must speak with precision when it intends to grant an unelected agency authority to impose charges on private parties. For example, elsewhere, the Legislature has expressly authorized ARB to collect revenues by imposing particular fees. (*See* Health & Safety Code §§ 39612(f)(1), 39613.) Like § 38597 of AB 32, both of these provisions clearly circumscribe the Board's fee authority. (*See id.* § 39612(f)(1) [authorizing ARB to impose permit fees on nonvehicular sources of air pollution, up to $13 million, to be used for specific purposes]; *id.* § 39613 [authorizing ARB to impose a fee for certain consumer products or architectural coatings, to be used for specified purposes].)

Legislature intended *sub silentio* to empower the commission to impose punitive damages." (*Dyna-Med*, 43 Cal.3d at 1389; *see Peralta*, 52 Cal.3d at 51 [refusing to "infer that through the expansive language ... the Legislature intended by implication to grant the Commission the authority not only to award compensatory damages, but to award such damages without limit"].) Here, the express grant to ARB of limited authority to collect regulatory fees refutes the conclusion that the Legislature implicitly granted ARB a much broader authority to generate excess revenues through auctions and reserve sales. (*See Peralta*, 52 Cal.3d at 50 ["'Where the [Legislature] has demonstrated the ability to make [its] intent clear, it is not the province of ... court[s] to imply an intent left unexpressed'"].)

3. Implication of authority to generate excess revenues would be inappropriate because such authority is not necessary to serve the purpose of AB 32. As the court acknowledged, the generation of revenue through the sale of allowances is not needed to satisfy the legislative purpose of AB 32, *i.e.*, to reduce GHG emissions in California. (JA 1573 ["under certain idealized conditions, the allocation choices will have no effect on the supply and demand for ... [GHG] emissions"].)

Indeed, ARB likewise has acknowledged that the method of allocating GHG allowances does not affect the amount of GHG reductions the Cap-and-Trade Program achieves because "[t]he limit on GHG

emissions—the program 'cap'—determines the environmental effectiveness of the cap-and-trade program." (ISOR ES-3.) ARB adopted the Market Advisory Committee's conclusion that "the method of initial allowance distribution has no effect on the environmental outcome, that is, the achievement of the emissions cap." (ISOR, App. H, at H-66; *see also id.* at H-9 ["[t]he method by which emission allowances are distributed under a cap-and-trade program does not affect total greenhouse gas emissions under the program"].)

4. Finally, AB 32's legislative history confirms that the Legislature did not authorize the Board to raise billions in revenues over and above the strictly limited fees expressly authorized in § 38597.

Of the seven legislative reports and analyses prepared for AB 32, only one discusses a grant of revenue-raising powers. (*See* JA 363–64.) Consistent with AB 32's text, this report discusses only the Board's authority to "adopt a schedule of fees to pay for the costs of implementing the program established pursuant to the bill's provisions." (JA 363.)

Given the circumstances surrounding AB 32's enactment, this "silence" is telling. (*See Dyna-Med*, 43 Cal.3d at 1387 ["wider historical circumstances of [a statute's] enactment may be considered in ascertaining the legislative intent"].) AB 32 was a highly visible and closely scrutinized bill, as its provisions affect numerous sectors of California's economy and

raise the profile of California's climate change regulation program nationally. Indeed, the legislative history reflects that AB 32's opponents *did* voice concerns about giving the Board "carte blanche authority to collect fees," but they focused those efforts on AB 32's fee provision, § 38597. (*See* JA 376.) If legislators thought that AB 32 could be interpreted to give ARB unprecedented revenue-raising authority in addition to the express fee provision, then surely the legislative history would reflect vigorous debate about that possibility. (*See United Farm Workers*, 41 Cal.App.4th at 316 [refusing to imply agency authorization where "there is nothing in the legislative history to show any contemplation of any involvement" by the agency in the proposed action].

The decision below does not address this omission from the legislative record, but instead points to "[p]ost-AB 32 legislation pertaining to the use of auction proceeds" to support its conclusion that "AB 32 authorized the sale of allowances." (JA 1575.) That is wrong because "[t]he declaration of a later Legislature is of little weight in determining the relevant intent of the Legislature that enacted the law." (*Peralta*, 52 Cal.3d at 52; *see also People ex rel. Lockyer v. R.J. Reynolds Tobacco Co.* (2005) 37 Cal.4th 707, 724 ["'subsequent legislation interpreting [a] statute ... [cannot] change the meaning" of the earlier enactment'"] [alteration in original]; *Del Costello v. State* (1982) 135 Cal.App.3d 887, 893 n.8 [a

legislature "has no legislative authority simply to say what it did mean"].) The statutes adopted in 2012 and 2014 do not reflect the intent of a prior legislative body as to the meaning of AB 32 adopted in 2006.

B. AB 32 Must Be Construed To Avoid Constitutional Doubt.

Even if the question whether AB 32 authorized the auction and sale of allowances to generate billions in revenues were debatable, California law requires that the Court adopt a construction of AB 32 that would avoid the necessity of resolving serious constitutional questions. That canon of construction applies here because a construction of AB 32 that authorizes ARB to generate billions in excess revenues would require the court to address whether AB 32 is an unconstitutional tax enacted without a supermajority vote of the Legislature.

In California, "[a] statute should be construed whenever possible so as to preserve its constitutionality." (*Dyna-Med*, 43 Cal.3d at 1387.) That is because courts presume "'that the Legislature intended, not to violate the Constitution, but to enact a valid statute within the scope of its constitutional powers.'" (*Harrott v. Cnty. of Kings* (2001) 25 Cal.4th 1138, 1153 [quoting *People v. Superior Court* (1996) 13 Cal.4th 497, 509].) Accordingly, "'[i]f a statute is susceptible of two constructions, one of which will render it constitutional and the other unconstitutional in whole or in part, *or raise serious and doubtful constitutional questions*, the court

will adopt the construction which, without doing violence to the reasonable meaning of the language used, will render it valid in its entirety, or free from doubt as to its constitutionality.'" (*Id.*) This canon favoring the construction that avoids constitutional questions applies even when "'the other construction is equally reasonable.'" (*Id.*[11])

Although the court below acknowledged that the issue whether the revenues generated through ARB's Cap-and-Trade Regulation were an illegal "tax" presented a "close question," (JA 1581), it ignored that California law requires that statutes such as AB 32 must be interpreted to avoid the need to resolve such serious constitutional questions. (JA 1574 & n.5.) Contrary to that requirement, the court interpreted the meaning of AB 32 without regard to the canon of constitutional avoidance and thereafter unnecessarily purported to resolve the constitutionality of AB 32. (*Id.*) That approach is fundamentally flawed.

In describing the operation of this canon of constitutional avoidance, the United States Supreme Court explained long ago:

> [U]nless this rule be considered as meaning that our duty is to first decide that a statute is unconstitutional and then proceed to hold that such ruling was unnecessary because the statute is

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[11] (*Accord Crowell v. Benson* (1932) 285 U.S. 22, 62 ["When the validity of [an] act of Congress is drawn in question, and even if a serious doubt of constitutionality is raised, it is a cardinal principle that this Court will first ascertain whether a construction of the statute is fairly possible by which the question may be avoided."].)

> susceptible of a meaning, which causes it not to be repugnant to the Constitution, *the rule plainly must mean that where a statute is susceptible of two constructions, by one of which grave and doubtful constitutional questions arise and by the other of which such questions are avoided, our duty is to adopt the latter.*

(*United States ex rel. Att'y Gen. v. Delaware & Hudson Co.* (1909) 213 U.S. 366, 407–08 [emphasis added].) California courts apply this same standard. (*See, e.g., Myers v. Philip Morris Cos.* (2002) 28 Cal.4th 828, 847 [following *Delaware & Hudson*]; *Perkey v. Dep't of Motor Vehicles* (1986) 42 Cal.3d 185, 194 ["statutes are to be construed, if possible, so as to avoid potential constitutional problems"] [emphasis added].)

Indeed, in *Association for Retarded Citizens v. Department of Developmental Services* (1985) 38 Cal.3d 384, the Supreme Court addressed a California agency's adoption of spending "priorities" which qualified as "quasi-legislative act[ion]." (*Id.* at 391 n.4.) The Court rejected the agency's reading of a statute to "authoriz[e] the issuance of the Priorities," and held that "[e]ven if this [statutory] language were ambiguous, we would not read it in any other way" because "[w]hen faced with a statute reasonably susceptible of two or more interpretations, of which at least one raises constitutional questions, we should construe it in a manner that avoids any doubt about its validity." (*Id.* at 394 [citing *Delaware & Hudson*, 213 U.S. at 407–08; *Carlos v. Superior Court* (1983)

35 Cal.3d 131, 147; *Cal. Housing Fin. Agency v. Elliott* (1976) 17 Cal.3d 575, 594].) Because the agency's proposed interpretation "would raise serious constitutional questions," the Supreme Court rejected that interpretation "to avoid any doubt about the validity of the [statute]." (*Id.*)

As discussed above, the language, structure, purpose, and history of AB 32 confirm that the Legislature did not authorize ARB to generate billions in excess revenues. At the very minimum, it would be *reasonable* to conclude that the Legislature did not authorize ARB to generate these revenues. That conclusion is dispositive because California law requires courts to adopt the construction that avoids difficult constitutional questions. As shown in Part II, if AB 32 were construed to allow ARB to raise revenue by auctioning and selling allowances, the statute would levy an unconstitutional tax.

II. If AB 32 Is Construed To Authorize ARB To Raise Revenue By Auctioning And Selling GHG Emission Allowances, Then It Imposes An Unconstitutional Tax.

Because AB 32, properly construed, does not grant ARB authority to raise billions of dollars in revenue by auctioning and selling GHG emission allowances, the decision below should be reversed on that basis, and this Court need not decide any constitutional question. If, however, AB 32 is construed to grant such authority, then it imposes an unconstitutional tax, and any such grant of authority must be severed from the statute, because

AB 32 was not passed by the two-thirds supermajority required to enact new taxes under the California Constitution.

"The California Constitution provides that any act to increase taxes must be passed by a two-thirds vote of the Legislature." (*Cal. Farm Bureau*, 51 Cal.4th at 428 & n.1 [citing art. XIIIA, § 3].) Added to the Constitution in 1978 by Proposition 13, Article XIIIA "impos[es] important limitations upon the assessment and taxing power of state and local governments." (*Amador Valley Joint Union High Sch. Dist. v. State Bd. of Equalization* (1978) 22 Cal.3d 208, 218.[12]) A tax that fails to garner the requisite two-thirds supermajority vote is unconstitutional and "may not be enforced." (*Beaumont Investors v. Beaumont-Cherry Valley Water Dist.* (1985) 165 Cal.App.3d 227, 238.)

The supermajority requirement cannot be evaded by labeling what is in substance a tax as a "fee" or some other kind of charge. (*See, e.g., Nw. Energetic Servs., LLC v. Cal. Franchise Tax Bd.* (2008) 159 Cal.App.4th 841, 855 ["Labeling the Levy a fee is not determinative of its nature."].) As a result, when the Legislature enacts a new fee or other revenue-raising measure by a simple majority vote, courts must determine whether "th[e]

[12] As noted above, in November 2010, California voters amended Article XIIIA by approving Proposition 26. (*See supra,* n.1.) Because Proposition 26 does not apply retroactively, the constitutionality of AB 32 turns on the pre-Proposition 26 version of Article XIIIA.

fees [are] in legal effect 'taxes' required to be enacted by a two-thirds vote of the Legislature." (*Sinclair Paint*, 15 Cal.4th at 870.) "Whether [a statute] imposes a tax or a fee is a question of law decided upon an independent review of the record." (*Cal. Farm Bureau*, 51 Cal.4th at 436.)

A. A Regulatory Charge That Fails To Satisfy The Requirements Of *Sinclair Paint* Is A Tax.

Although "the distinction between taxes and fees is frequently 'blurred'" (*Sinclair Paint*, 15 Cal.4th at 874), courts have identified certain kinds of fees that may be imposed without a two-thirds supermajority vote, provided that specified requirements are met. Among them are "regulatory fees, imposed under the police power." (*Id.*[13]) "The California Supreme Court has ... set out guidelines for determining whether a denominated fee is, in fact, a bona fide regulatory fee and not a disguised tax." (*Tomra Pac., Inc. v. Chiang* (2011) 199 Cal.App.4th 463, 487.) The leading case is *Sinclair Paint*. There the Court ruled that a fee claimed to serve a regulatory purpose must satisfy three requirements to be deemed

[13] Other fees include "special assessments, based on the value of benefits conferred on property" and "development fees, exacted in return for permits or other government privileges." (*Sinclair Paint*, 15 Cal.4th at 874.) Respondents have not attempted to defend the allowance charges as special assessments or development fees. Nor could they, as the allowance charges do not "reflec[t] the value of the benefits conferred by improvements," or "bea[r] a reasonable relation to [any] development's probable costs to the community and benefits to the developer." (*Id.* at 874–75.)

constitutional. (JA 1583 [citing, *inter alia*, *Cal. Farm Bureau*, 51 Cal.4th at 437–42; *Sinclair Paint*, 15 Cal.4th at 876–80].)

First, a regulatory fee may not "excee[d] the reasonable cost of providing the ... services for which the fees were charged." (15 Cal.4th at 880.) Thus, "'to show a fee is a regulatory fee and not a special tax, the government should prove ... the estimated costs of the service or regulatory activity.'" (*Id.* at 878 [quoting *San Diego Gas & Elec. Co. v. San Diego Cnty. Air Pollution Control Dist.* (1988) 203 Cal.App.3d 1132, 1146].) The amount of revenue generated by the fee "cannot ... exceed the reasonable cost of regulation with the generated surplus used for general revenue collection." (*Cal. Farm Bureau*, 51 Cal.4th at 438.) "An excessive fee that is used to generate general revenue becomes a tax." (*Id.*)

Second, the amount of the fee also must bear a "reasonable relationship to the social or economic 'burdens' [the payers'] operations generat[e]." (*Sinclair Paint*, 15 Cal.4th at 881.) While a regulatory fee may be imposed to "mitigat[e] [the payers'] operations' adverse effects," (*id.* at 880), the government must show that the amount of the fee "'bear[s] a fair or reasonable relationship to the payor's burdens on or benefits from the regulatory activity.'" (*Id.* at 878 [quoting *San Diego Gas & Elec.*, 203 Cal.App.3d at 1146].)

Third, and finally, a regulatory fee may not be "levied for unrelated revenue purposes." (*Id.* at 877 [citing *Pennell v. City of San Jose* (1986) 42 Cal.3d 365, 375].) The *Sinclair Paint* Court recognized that "if regulation is the primary purpose of the fee measure, the mere fact that the measure also generates revenue does not make the imposition a tax." (*Id.* at 880.) But at the same time, the Court made clear that the fee must be imposed for purposes that are related to the regulation of the payer's activities "and not for general revenue purposes." (*Id.* at 881.)

B. Under *Sinclair Paint*, The Allowance Charges Are An Unconstitutional Tax.

Notwithstanding that *Sinclair Paint* sets forth the controlling standard, respondents did not attempt below to defend the allowance charges under the established framework for assessing regulatory fees set forth in *Sinclair Paint*. Instead, they argued that the allowance charges were a *sui generis* kind of regulatory fee that did not need to satisfy *Sinclair Paint*'s requirements because the charges were not intended to fund a regulatory program. (JA 1580; *see* JA 1837 ["We're not claiming to be a Sinclair-type fee so that analysis ... just doesn't apply here."].) The Superior Court correctly rejected that argument, holding that the charges must be reviewed "using the regulatory fee framework." (JA 1583.)

The allowance auction and reserve sale charges do not meet any of the three independent requirements set forth by the Supreme Court in

Sinclair Paint for qualifying as a regulatory fee exempt from Proposition 13. *First*, the allowance revenues vastly exceed the amount necessary to fund the Cap-and-Trade Program (or even the broader implementation of AB 32). Indeed, AB 32 contains a separate regulatory fee provision to fund the implementation of AB 32. *Second*, ARB has made no showing that the billions in revenues to be generated bear a reasonable relationship to any burdens imposed by the payers' operations. *Third*, given that ARB acknowledged that the generation of revenues is unnecessary to serve the environmental goal of reducing GHG emissions, there can be no serious question that the primary purpose of the auction and reserve sale provisions is the generation of billions in revenues that the Legislature can use for a grab-bag of programs unrelated to regulation of the payers' activities. Accordingly, if AB 32 were construed to authorize ARB to raise billions of dollars in revenue by auctioning and selling GHG emissions allowances, it would constitute an unconstitutional "chang[e] in State taxes enacted for the purpose of increasing revenues." (Cal. Const., art. XIIIA, § 3 [2006].)

1. The allowance charges fail the *Sinclair Paint* test, first, because the billions of dollars in revenues they generate vastly "exceed the reasonable cost of regulation." (*Cal. Farm Bureau*, 51 Cal.4th at 438.)

The amount of money ARB proposes to raise through its auctions and reserve sales is staggering. At the first quarterly auction alone, ARB

raised nearly $289 million dollars (JA 503.) The LAO estimated that in fiscal year 2012–13, the auctions would "generate roughly $660 million to upwards of $3 billion," and that these numbers would only increase in subsequent years as ARB shifted to greater reliance on auctions and reserve sales. (JA 503.) The LAO projected that, by 2015, ARB would be raising between $2 and $14 billion per year from the sale of allowances, meaning that over the life of the program ARB would raise as much as $12 to $70 billion in additional revenue for the State. (JA 460.) Thus, "[b]illions of dollars in revenues from the auction of allowances will become available as a result of the ARB's cap-and-trade program." (*Id.*)

These amounts dwarf not only the cost of the Cap-and-Trade Program, but the entire cost of implementing AB 32. According to ARB, the cost of implementing AB 32 in its entirety is approximately $35 million a year, plus about $27 million a year in repayment of start-up loans that will be paid off by fiscal year 2013–14. (JA 509.) In a single quarterly auction, therefore, ARB raised almost five times more in revenues from selling allowances than it needs to fund AB 32 for an entire year.

Moreover, the cost of AB 32 is already fully funded by AB 32's separate cost-of-implementation fee (17 CCR § 95203(a) [providing that revenue collected under the Fee Regulation "shall be the total amount of funds necessary to recover the costs of implementation of AB 32 program

expenditures for each fiscal year"].) The allowance revenues are *over and above* the fees already collected for implementation and are thus by definition more than necessary to fund the Cap-and-Trade Program or to implement AB 32. (*See* JA 1585 ["The costs of the cap-and-trade program will be recovered by the fees collected under § 38597."].)

By any measure, the revenues ARB generates from auctioning and selling allowances far "exceed the reasonable cost of regulation." (*Cal. Farm Bureau*, 51 Cal.4th at 438.) The allowance charges are therefore an unconstitutional tax. (*See id.* ["permissible fees must be related to the overall cost of the governmental regulation"]; *Sinclair Paint*, 15 Cal.4th at 876 [a regulatory fee must "'not exceed the reasonable cost of providing services necessary to the activity for which the fee is charged"]; *Nw. Energetic Servs.*, 159 Cal.App.4th at 859 [charge was a tax because the revenue it generated "far exceed[ed] any reasonable cost of regulating or providing services" under the regulatory program]; *Beaumont Investors*, 165 Cal.App.3d at 234–38 [charge was a tax because government failed to show it did not "'exceed the reasonable cost'" of regulation]; *cf. Griffith v. City of Santa Cruz* (2012) 207 Cal.App.4th 982, 996 [charge was not a tax because the amounts collected were "'no more than necessary to cover the reasonable costs of the governmental activity'"].)

The Superior Court found that the allowance charges satisfied this prong of *Sinclair Paint*, but it was able to do so only by redefining the relevant regulatory program to be, not the Cap-and-Trade Program or AB 32, but rather the "additional regulatory programs that further the emissions reduction goals of AB 32." (JA 1585.) Because those programs are not defined in AB 32, the court recognized that "neither ARB nor this court currently know[s] what those programs might be." (*Id.*) The court concluded, however, that "because the proceeds can only be used to advance the regulatory purposes of AB 32, by definition, the total amount of fees collected will not exceed the costs of the regulatory program they support." (*Id.*)

The Superior Court's reasoning nullifies this prong of the *Sinclair Paint* test, which requires the relevant regulatory program to be defined in advance. As the *Sinclair Paint* Court explained, "'to show a fee is a regulatory fee and not a special tax, the government should prove ... the estimated costs of the service or regulatory activity.'" (15 Cal.4th at 878.) The government cannot prove the estimated cost of the regulatory activity if the program to be funded has not yet been defined. Perhaps for that reason, respondents made no attempt below to meet their burden in this regard, which by itself is grounds for reversal. (*See, e.g., Beaumont Investors*, 165 Cal.App.3d at 237 [holding that a charge imposed to finance

capital improvements to water system facilities was an unconstitutional tax and not a valid fee because the record did not contain "the facts necessary to establish a reasonable relation between the estimated cost of the capital improvements and the facilities fee imposed on plaintiffs"].)

The Superior Court relieved respondents of their burden by inverting the *Sinclair Paint* analysis. *Sinclair Paint* allows the Legislature to create a regulatory program and then impose a fee to fund the program. The Superior Court's approach allows the Legislature to impose a fee and then create a program to spend the proceeds. In the former case, the estimated cost of the program sets an upper bound on the amount the Legislature can raise through the fee. In the latter case, no such constraint exists, and the amount raised simply becomes a rainy-day slush fund that the Legislature can expend at its discretion in the future, as long as the expenditures can be said to advance some broadly defined regulatory purpose. The ruling below thus eliminates a critical limitation on the Legislature's ability to impose regulatory fees without a two-thirds supermajority vote.

In this regard, the allowance auction and reserve sale charges differ sharply from charges that have been upheld as regulatory fees. Cases upholding regulatory fees invariably involve a statute that defines in advance the program to be funded such that the cost of the program can be estimated and the fee calibrated accordingly. In *Sinclair Paint*, for example,

the fee was imposed to fund a program for the evaluation, screening, and follow-up services for children deemed potential victims of lead poisoning. (15 Cal.4th at 871–72.) The program was described in detail in the applicable chapter of the Health and Safety Code, and the provision authorizing the fee expressly provided that "[t]he department shall not collect fees pursuant to this section in excess of the amount reasonably anticipated by the department to fully implement this chapter." (Health & Safety Code § 105310(f).) Citing that provision, the Court explained that "the state must use the funds it collects under [the statute] *exclusively* for mitigating the adverse effects of lead poisoning of children" pursuant to the program the Legislature had established. (15 Cal.4th at 881.)

Likewise, in *California Farm Bureau*, the regulatory activities to be funded were spelled out in the statute, which instructed the agency to "'set the fee schedule authorized by this section so that the total amount of fees collected pursuant to this section equals the amount necessary to recover costs incurred in connection with'" those activities. (51 Cal.4th at 431 n.11 [quoting Water Code § 1525].) In upholding the fee, the Court emphasized that the statute "described the purposes for which the money [raised by the fee] may be expended" and "permit[ted] the imposition of fees only for the costs of the functions or activities described." (*Id.* at 438–39.)

Other cases are in accord. (*See, e.g., Pennell*, 42 Cal.3d at 374–75 & n.10 [upholding fee in amounts necessary to fund dispute mediation and arbitration hearing process]; *Griffith*, 207 Cal.App.4th at 987–88, 996–97 [upholding fee in amounts necessary to fund inspection of residential rental properties]; *Cal. Bldg. Indus. Ass'n v. San Joaquin Valley Air Pollution Control Dist.* (2009) 178 Cal.App.4th 120, 127–28, 134 [upholding fee in amounts necessary to fund off-site emission reductions to offset emissions caused by new development]; *Collier v. City & Cnty. of San Francisco* (2007) 151 Cal.App.4th 1326, 1331–32, 1346–49 [upholding fee in amounts necessary to fund building permit and inspection services]; *Cal. Ass'n of Prof'l Scientists v. Dep't of Fish & Game* (2000) 79 Cal.App.4th 935, 939–40, 946 [upholding fee in amounts necessary to fund Fish and Game environmental review functions].)

Unlike in these cases, the Legislature in AB 32 did not define a regulatory program in advance (other than the AB 32 program) and then impose a fee in amounts necessary to fund the estimated costs of that program. Instead, ARB adopted the auctions and reserve sales and then the Legislature, in subsequent legislation, began to specify the purposes for which the proceeds could be used, with the intent to spend however many billions of dollars were raised on new programs to be created and defined in the future. This blank check does not satisfy *Sinclair Paint*'s requirement

that the amount of the fee must not exceed the estimated cost of the regulatory program. A contrary ruling would render the limitations set forth in *Sinclair Paint* wholly ineffective and allow the Legislature to end run the constitutional restrictions on new taxes.

2. The allowance charges further fail to meet the *Sinclair Paint* test because they do not bear a "reasonable relationship to the social or economic 'burdens' [the payers'] operations generat[e]." (*Sinclair Paint*, 15 Cal.4th at 881.) Here, too, respondents did not even argue below that the allowance charges are reasonably related to any burdens imposed by the payers' operations, let alone attempt to prove the "'estimated costs'" of mitigating the effects of the payers' GHG emissions or "'the basis for determining the manner in which the costs are apportioned, so that charges allocated to a payor bear a fair or reasonable relationship to the payor's burdens on or benefits from the regulatory activity.'" (*Id.* at 878.)

There is thus no basis in the record for the Superior Court's finding that there is a "reasonable relationship between the charges and the covered entities' (collective) responsibility for the harmful effects of GHG emissions." (JA 1587.) The amount of the charge for an allowance is not calculated based on any purported adverse effects attributable to the payers' operations. Rather, it is set based on a "market" price that is determined by the supply of allowances made available by ARB and the demand for those

allowances. There is no relationship between that price and any effects purportedly caused by the payers' operations.[14]

Nor is there any evidence that the total amount to be raised through the auctions and reserve sales is reasonably related to the cost of mitigating the effects of covered entities' GHG emissions. Respondents never presented any evidence of the amount or percentage of GHGs that covered entities emit or attempted to quantify the effects of their emissions. There is thus no basis for finding that covered entities' GHG emissions will impose between $12 and $70 billion (LAO's estimate of the total amount of revenues that will be raised over the life of the program) in costs on California. Indeed, given that the total amount of money that will be raised is unknown, with the estimated range varying by as much as $58 *billion*, the Superior Court's finding effectively amounts to a conclusion that *any* amount covered entities are compelled to pay would be reasonably related to the burdens they impose on California. Here again, the Superior Court's reasoning transforms a critical constraint on the Legislature's ability to impose regulatory fees into a blank check.

The Superior Court's decision also ignores an important difference between GHGs and activities that have previously been found to support

[14] Indeed, under the Cap-and-Trade Regulation, the payer may be a person or organization that conducts no GHG-emitting operations at all, but instead purchases allowances in order to retire them. (FSOR 449.)

"mitigation fees." Unlike the companies whose products contributed to lead contamination in *Sinclair Paint*, the covered entities under the Cap-and-Trade Program are not solely or even primarily responsible for any adverse effects in California from GHGs. Any harms to California would be based on the total level of GHGs in the global atmosphere and are thus caused by virtually every human activity everywhere in the world. There is no basis in the record for finding that the billions of dollars in new charges that ARB is seeking to impose on a subset of California industry are reasonably related to the covered entities' proportionate responsibility for any effects of global climate change in California. (*Cf. Equilon Enters. v. State Bd. of Equalization* (2010) 189 Cal.App.4th 865, 880–86 [upholding fee that was allocated "proportionally among those who are responsible for significantly contributing to such environmental lead contamination based on their 'market share' responsibility"].)

3. Finally, the allowance charges are not regulatory fees because their primary purpose is the generation of billions of dollars in revenues that are unnecessary to serve the environmental goals of the Cap-and-Trade Program and that can be spent for a wide variety of purposes unrelated to the regulation of the payers' activities under the Cap-and-Trade Program.

ARB designed the allowance auctions and reserve sales to raise billions in excess revenue that could be used for general public benefit

purposes. As ARB recognized during the administrative proceedings, raising revenue through allowance auctions and reserve sales is not necessary to achieve AB 32's environmental goal of reducing statewide GHG emissions to 1990 levels by 2020. (Health & Safety Code § 38550.) That is because, as ARB recognized, "[t]he limit on GHG emissions—the program 'cap'—determines the environmental effectiveness of the cap-and-trade program." (ISOR ES-3.) "The method by which emission allowances are distributed under a cap-and-trade program does not affect total greenhouse gas emissions under the program" and thus "has no effect on the environmental outcome." (*Id.*, App. H, at H-9, H-66.) Accordingly, "an allowance auction is not necessary to meet the AB 32 goal of reducing GHG emissions" because "it is the declining cap on emissions that will reduce the state's overall level of GHGs." (JA 499.)

At the same time, ARB repeatedly touted the revenue that would be raised as a principal advantage of its proposed auctions and reserve sales over free allocation. ARB explained that "[t]he value of allowances ... is represented by the money paid to the State, which would then have the opportunity to use the revenue for public benefit." (ISOR II-29; *see also, e.g.,* ISOR ES-4, II-24; FSOR 199.) In discussing the "advantages of auctioning as an allocation method," (ISOR, App. J, at J-62 [capitalization omitted]), ARB emphasized that the allowance revenues could be used for a

variety of purposes, including "tax-rate reduction." (*Id.* at J-64.) Thus, ARB observed, "[u]sing auction proceeds is like green tax reform," *i.e.*, "the substituting of environmental taxes such as carbon taxes or gasoline taxes for ordinary taxes." (*Id.* at J-65; *see also* JA 420 [ARB resolution recommending that allowance revenues be used to finance "cuts or avoided increases in the State's individual income or sales tax rates"].[15])

The Superior Court ignored these and many other statements in the record showing that ARB adopted the auctions and reserve sales for the purpose of raising revenues and that those revenues are not merely a multi-billion dollar "byproduct of the implementation of a regulatory program." (JA 1586.) ARB did not just "recogniz[e] that the sale of allowances will provide revenues that can be reinvested for public benefit." (JA 1584.) It

[15] The expert committees on which ARB relied likewise emphasized the many benefits that would flow from "the influx of revenue to the government." (ISOR, App. H, at H-70.) The Economic and Allocation Advisory Committee—whose recommendations ARB endorsed (*see, e.g.*, FSOR 1129, 1149, 1901, 1904)—explained that, "[i]n contrast with free provision, auctioning yields revenue and thereby can reduce the extent of the government's reliance on ordinary taxes for financing expenditures." (ISOR, App. L, at L-6; *see also id.* at L-18, L-37, L-62.) Similarly, in discussing the advantages of auctioning over free allocation, the Market Advisory Committee explained that "[s]ince free allocation does not bring in revenues, unlike auctioning it cannot be used to finance reductions in existing income or sales taxes, or to pay for consumer rebates." (ISOR, App. H, at H-69; *see also id.* at H-68–H-69.)

adopted the auctions and reserve sales *because* they would generate revenue that could be used by the State in lieu of ordinary taxes.

Moreover, even apart from ARB's revenue-raising purpose, the allowance charges fail *Sinclair Paint* because the proceeds can be used for general revenue purposes unrelated to the payers' activities. AB 32 nowhere provides that the revenues from the allowance auctions and reserve sales must be used exclusively for purposes related to the Cap-and-Trade Program, or even for purposes of implementing AB 32 generally. Nor does it link the revenues to any specified regulatory costs or burdens, require the allowance revenues to be deposited in a separate fund, or impose any other restrictions on the use of the revenues.[16] AB 32 thus resembles the statute that was held to impose a tax in *Northwest Energetic Services* because it did not "identify any connection between the Levy and th[e] regulatory activity or its costs or benefits." (159 Cal.App.4th at 855.)

[16] The Cap-and-Trade Regulation provides that "[t]he proceeds from the sale of th[e] allowances will be deposited into the Air Pollution Control Fund and will be available upon appropriation by the Legislature for the purposes designated in [AB 32]." (17 CCR § 95870(f).) But, as ARB recognized, this regulation does not constrain the Legislature's use of the allowance revenues because ARB lacks authority to direct the Legislature with respect to the expenditure of state funds. (*See* FSOR 724 ["All revenue collected through auction will be appropriated at the discretion of the Legislature, not ARB."]; *id.* at 1900 ["The Governor and Legislature have the ultimate authority on directing the use of auction revenue."].)

In failing to limit the purposes for which the allowance revenues may be used, AB 32 contrasts starkly with statutes that have been upheld as imposing valid regulatory fees. The statute upheld in *California Farm Bureau*, for example, "reveal[ed] a specific intention to avoid imposition of a tax," because it "permit[ted] the imposition of fees only for the costs of the functions or activities described, and not for general revenue purposes." (51 Cal.4th at 438.) The Court emphasized that the statute "carefully se[t] out that the fees imposed shall relate to costs linked to" the regulatory program; "direct[ed] that the fees collected be deposited in" a designated fund separate from the general fund; and "describ[ed] the purposes for which the money in [that fund] may be expended." (*Id.* at 438–39.) Likewise, the statute upheld in *Sinclair Paint* provided that "the state must use the funds it collects [thereunder] *exclusively* for mitigating the adverse effects of lead poisoning in children, and not for general revenue purposes." (15 Cal.4th at 881 [citing Health & Safety Code § 105310(f)].) AB 32, by contrast, imposes no restrictions on the use of the allowance revenues.

The court below nonetheless concluded that the allowance charges were not imposed for unrelated revenue purposes because "the post-AB 32 legislation restricts how the proceeds of sales will be used." (JA 1584.) But the spending limitations these statutes impose do not cure the constitutional defect in AB 32 because they permit the allowance revenues to be used for

general revenue purposes unrelated to regulation of the payers' activities under the Cap-and-Trade Program. The post-AB 32 legislation permits the allowance revenues to be used in any way "to facilitate the achievement of reductions of greenhouse gas emissions in this state." (Health & Safety Code § 39712(b).) This "limitation" does not satisfy *Sinclair Paint.*

As the Superior Court recognized, "since nearly every aspect of life has some impact on GHG emissions, it is difficult to conceive of a regulatory activity that will not have at least some impact on GHG emissions." (JA 1582.) Because GHGs are ubiquitous, an authorization to use the allowance revenues to facilitate GHG reductions is for all practical purposes a grant of general revenue authority. For example, the post-AB 32 legislation permits the allowance revenues to be used to fund public transportation initiatives such as the construction of high-speed rail; to develop advanced technology vehicles and biofuels; to invest in sustainable housing and infrastructure; to improve municipal solid waste disposal; and to fund land and natural resource conservation and management, forestry, and sustainable agriculture. (Health & Safety Code § 39712(c).)

The post-AB 32 statutes thus fail to satisfy *Sinclair Paint* because they permit the allowance revenues to be used for the "control of [GHGs] generally, rather than for the regulation of the [fee] payers' business activities." (*Morning Star Co. v. Bd. of Equalization* (2011) 201

Cal.App.4th 737, 755.) This Court's decision in *Morning Star* is directly on point. The statute there imposed a charge on businesses that used, generated, stored, or conducted activities in California related to hazardous materials. (*Id.* at 742.) The proceeds were used to fund "various programs relating to the control of hazardous materials." (*Id.* at 743.) This Court held that the charge was a tax because it was used "to pay for a wide range of governmental services and programs related to hazardous waste control," rather than for "the regulation of ... payers' business activities in using, generating or storing hazardous materials." (*Id.* at 755.)

Like the hazardous material charge in *Morning Star*, the allowance charges are a tax because they are used for purposes unrelated to regulation of the payers' activities. The programs funded by the allowance revenues, such as the construction of high-speed rail, are not designed to remediate any effects of the covered entities' operations.[17] They are designed to reduce GHG emissions from other sectors of the economy unrelated to the payers' operations. If this were enough to satisfy *Sinclair Paint*, then the Legislature could raise the revenue needed to fund high-speed rail (or any other ostensibly GHG-reducing project) by imposing, through a simple majority vote, a "GHG mitigation fee" on every business and person in the

[17] Covered entities include specified manufacturing, production, and utility operations that emit threshold amounts of GHGs. 17 CCR §§ 95811–12.

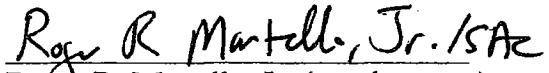
State based on the amount of GHGs they emit. Such a "fee" plainly would be an unconstitutional tax. So are the allowance charges.

Of course, the Legislature has authority to raise revenue to be spent on efforts to mitigate GHGs or to ameliorate any effects of global climate change in California. But that power must be exercised consistent with the requirement of the California Constitution that new taxes may be imposed only by a two-thirds supermajority vote of the Legislature. Because AB 32 was enacted by less than a two-thirds supermajority, and because the allowance charges do not satisfy *Sinclair Paint*'s criteria for regulatory fees, AB 32 is unconstitutional to the extent it authorizes ARB to raise revenue through allowance auctions and reserve sales.

CONCLUSION

For these reasons, the judgment below should be reversed.

Respectfully submitted,



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WORD COUNT CERTIFICATE

Pursuant to Rule 8.204(c)(1), I certify that this brief contains 13,064 words, excluding the portions of the brief listed in Rule 8.204(c)(3).

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PROOF OF SERVICE

Pursuant to Rules 8.25(a)-(b), 8.29(c), 8.44(b), and 8.212(c) of the California Rules of Court, I certify that on this 20th day of October, 2014, I served the foregoing Opening Brief of Appellant The National Association of Manufacturers in the following manner:

(1) one paper copy to each of the parties listed in the attached Service List (including the Attorney General) by placing each in sealed envelopes with the fees paid and depositing the envelopes with Federal Express for guaranteed next day delivery;

(2) one paper copy to the superior court clerk for delivery to the trial court by placing it in a sealed envelope with the fees paid and depositing the envelope with Federal Express for guaranteed next day delivery;

(3) one electronic copy on the Supreme Court by sending the copy to the Supreme Court's electronic service address as a single computer file in text-searchable PDF format; and

(4) one original and four papers copies on the Clerk of the Court of Appeal for State of California Third Appellate District by placing the original and four copies in a sealed envelope with the fees paid and depositing the envelope with Federal Express for guaranteed next day delivery.

I reside and am employed in the County of Los Angeles, am over the age of 18, and am not a party to this case. I declare under penalty of perjury that the foregoing is true and correct and that this declaration was executed this 20th day of October, 2014, at Los Angeles, California.

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EXHIBIT B

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

THIRD APPELLATE DISTRICT

No. C075954
(Consolidated with No. C075930)

MORNING STAR PACKING COMPANY, et al.,
Petitioners-Appellants,

v.

CALIFORNIA AIR RESOURCES BOARD, et al.,
Respondents-Appellees,

and

ENVIRONMENTAL DEFENSE FUND, et al.,
Intervenors and Respondents.

On Appeal from the Superior Court of Sacramento County
(Case No. 34-2013-80001464, Honorable Timothy M. Frawley, Judge)

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TO BE FILED IN THE COURT OF APPEAL APP-008

COURT OF APPEAL, THIRD APPELLATE DISTRICT, DIVISION	Court of Appeal Case Number: C075954 Consol. with C075930
ATTORNEY OR PARTY WITHOUT ATTORNEY (Name, State Bar number, and address): James S. Burling, No. 113013 / Theodore Hadzi-Antich, No. 264663 Harold E. Johnson, No. 200392 Pacific Legal Foundation 930 G Street, Sacramento, CA 95814 TELEPHONE NO.: (916) 419-7111 FAX NO. (Optional): (916) 419-7747 E-MAIL ADDRESS (Optional): jsb@pacificlegal.org / tha@pacificlegal.org ATTORNEY FOR (Name): Morning Star Packing Company, et al.	Superior Court Case Number: 34-2013-80001464 FOR COURT USE ONLY
APPELLANT/PETITIONER: Morning Star Packing Company, et al. RESPONDENT/REAL PARTY IN INTEREST: California Air Resources Board, et al.	
CERTIFICATE OF INTERESTED ENTITIES OR PERSONS (Check one): ☑ INITIAL CERTIFICATE ☐ SUPPLEMENTAL CERTIFICATE	

Notice: Please read rules 8.208 and 8.488 before completing this form. You may use this form for the initial certificate in an appeal when you file your brief or a prebriefing motion, application, or opposition to such a motion or application in the Court of Appeal, and when you file a petition for an extraordinary writ. You may also use this form as a supplemental certificate when you learn of changed or additional information that must be disclosed.

1. This form is being submitted on behalf of the following party (*name*): List of Parties on Attachment Number 1.

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

THEODORE HADZI-ANTICH
(TYPE OR PRINT NAME)

▶ [signature]
(SIGNATURE OF PARTY OR ATTORNEY)

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APP-008 [Rev. January 1, 2009]

CERTIFICATE OF INTERESTED ENTITIES OR PERSONS

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SHORT TITLE:	CASE NUMBER:
Morning Star Packing Co., et al. v. Cal. Air Resources Board, et al.	C075954 Consol. with C075930

ATTACHMENT *(Number):* 1

(This Attachment may be used with any Judicial Council form.)

Certificate of Interested Entities or Persons submitted on behalf of the following parties:

1. Morning Star Packing Company;
2. Dalton Trucking, Inc.;
3. California Construction Trucking Association;
4. Merit Oil Company;
5. Ron Cinquini Farming;
6. Construction Industry Air Quality Coalition;
7. Robinson Enterprises, Inc.
8. Loggers Association of Northern California, Inc.
9. Norman R. "Skip" Brown;
10. Joanne Brown;
11. Robert McClernon;
12. National Tax Limitation Committee

(If the item that this Attachment concerns is made under penalty of perjury, all statements in this Attachment are made under penalty of perjury.)

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INTRODUCTION

This appeal arises out of an effort by a state agency to collect billions of dollars of revenue from California enterprises in violation of the California Constitution and, in the alternative, without statutory authority. The Petitioners-Appellants (collectively, "Petitioners"), ask this Court to reverse the decision of the court below on legal grounds and to declare invalid, enjoin, and order the Respondents-Appellees (collectively, "CARB"), to rescind and refrain from enforcing a regulation governing emissions of carbon dioxide and related gases ("greenhouse gases").

The regulation at issue, Cap of Greenhouse Gas Emissions and Market-Based Compliance Mechanisms, 17 C.C.R. §§ 95801-96023 ("Cap and Trade Regulation"), was promulgated by CARB under the California Global Warming Solutions Act of 2006, Health & Safety Code § 38500, *et seq.* ("A.B. 32"), which mandates that California Covered Entities reduce greenhouse gas emissions to 1990 levels by the year 2020, under a statewide descending "cap" on such emissions. The specific portions of the Cap and Trade Regulation for which relief is sought are set forth in 17 C.C.R. §§ 95830-95834, 95870, and 95910-95914 (the "Auction Provisions"). On cross motions for summary judgment, the court below found that the Auction Provisions did not violate the California Constitution and were authorized by A.B. 32 (JA1595-1616). This appeal challenges that decision.

STATEMENT OF THE CASE

On April 16, 2013, Petitioners filed a Verified Petition for Writ of Mandate and Complaint for Declaratory Relief against CARB in the Superior Court of California for the County of Sacramento, asking the court to declare invalid, enjoin, and order CARB to rescind the Auction Provisions of the Cap and Trade Regulation. (JA0549).

The case was assigned Number 34-2013-80001464 by the Superior Court. On April 17, 2013, the Petitioners filed a Notice of Related Case, notifying the trial court and the parties that Case No. 34-2012-80001313, pending in the same court, was related to the instant case. (JA0575). On April 24, 2014, the trial court ordered that the two cases be designated as related. (JA0579).

On May 14, 2013, Environmental Defense Fund and Natural Resources Defense Council (the "Environmental Advocacy Group Intervenors"), were granted intervenor status as Respondents-Defendants (JA0597), and they filed their Complaint in Intervention on June 12, 2013 (JA0898).

After the briefing, on November 12, 2013, the trial court issued an Order After Hearing, ruling in favor of CARB on all issues in both cases. (JA-1566). Specifically, the trial court held that (1) the Auction Provisions, and therefore A.B. 32, did not violate California Constitution Article XIII A, Section 3 **(Proposition 13)**, (2) Neither the Auction Provisions nor four bills

enacted in 2012 violated California Constitution Article XIII A, Section 3 (**Proposition 26**), and (3) the Auction Provisions were authorized by A.B. 32. On December 20, 2013, the trial court issued its Judgment spelling (JA1618). Notice of Entry of Judgment was filed on January 9, 2014 (JA1681).

Notice of Appeal was timely filed in the trial court on February 28, 2014 (JA1742). The Petitioners filled their Notice Designating Record on Appeal on April 11, 2014 (JA1780).

On May 5, 2014, the trial spelling court filed its Clerk's Designation of Record on Appeal, attaching the original signed Reporter's Transcript of the hearing held on August 28, 2013, which was received by this Court on May 8, 2014. The Clerk's Designation stated that, although the Petitioners in the instant case requested the administrative record, that record was filed in the related case but not in the instant case; to avoid duplication. The parties have stipulated that the administrative record in the related case will serve as the record in that case and the instant case (JA1956-1957). On July 15, 2014, this Court approved a request by the parties to consolidate the instant appeal (CO75954), with the appeal in the related case (CO75930). JA1958.

STATEMENT OF APPEALABILITY

This appeal is from a final judgment after court trial on the Verified Petition for Writ of Mandate and Complaint for Declaratory Relief and is authorized by Code of Civil Procedure section 904.1, subdivision (a)(4).

STATEMENT OF FACTS

Under the Cap and Trade Regulation, Covered Entities, *i.e.*, those who are subject to the emissions limitations, may not emit greenhouse gases without possessing emissions allowances created by CARB, which distributes the allowances free of charge to certain Covered Entities and sells the remainder at auction, with the proceeds of auction sales to be used by California for purposes that are not specifically identified in either A.B. 32 or the Cap and Trade Regulation (JA-0693).[1] Annual revenues to be generated by CARB at such auctions have been estimated at between $1 billion and $14 billion, with total estimated revenues ranging from $7 billion to $75 billion, to be generated over a seven-year period from 2013-2020 (JA0697).

As of the date of the filing of Petitioners' Opening Brief in the lower court, CARB had held three auctions at which it had collected approximately $796 million in revenues, and CARB plans to hold auctions every three months for the next several years, as the state emissions cap decreases over time. (JA0721-0722, 0725).

At the end of each compliance period, Covered Entities must surrender their emission allowances and obtain new ones for the next compliance period. A declining emissions cap requires that CARB create fewer emissions

[1] *See* Petitioners' Request for Judicial Notice, Appendix of Exhibits, and Declaration of Ralph Kasarda, filed in the lower court (JA0677).

allowances for each succeeding compliance period (JA0695, 0743-0745). Accordingly, the price of allowances sold at auction will increase over time, as the supply of allowances decreases. (JA0738).

No provision in A.B. 32 specifically directs CARB to collect revenues pursuant to an auction of greenhouse gas emission allowances, and A.B. 32 is silent with regard to what, if anything, is to be done with any such revenues. In 2012, the California Legislature enacted four bills which together purport to allocate the revenues generated at CARB's auctions. First, Senate Bill 1018 ("S.B. 1018") provides that (1) "except for fines and penalties, all moneys collected by CARB from the auction or sale of allowances . . . shall be deposited in the [Greenhouse Gas Reduction] fund and [shall be] available for appropriation by the Legislature," Gov't Code § 16428.8(b), and (2) the State "Controller may use the moneys in the [Greenhouse Gas Reduction] fund for cash flow loans to the General Fund . . .." Gov't Code § 16428.8(d).

Second, Assembly Bill 1532 ("A.B. 1532"), provides that the uses of funds to be deposited in the Greenhouse Gas Reduction Fund may be determined after the revenues have been collected. Health & Safety Code §§ 39712(a)-(c), 39716(a)-(c), 39718(a)-(b).

Third, Senate Bill 535 ("S.B. 535") mandates that a minimum of 25% of CARB's auction revenues be spent for the benefit of certain "disadvantaged communities," and that a minimum of 10% of the available moneys in the

Greenhouse Gas Reduction Fund be allocated to projects located within such communities. Health & Safety Code §§ 39713(a)-(b).

Fourth, Assembly Bill 1464 ("A.B. 1464") provides that notwithstanding any other provision of law, the Director of Finance may allocate or "otherwise use" an amount of "at least" $500 million from moneys derived from the sale of greenhouse gas emission allowances deposited in the Greenhouse Gas Reduction Fund and make commensurate reductions to General Fund expenditure authority. 2012 Stats. Ch. 21 § 15.11(a).

In 2014, the Legislature allocated certain moneys in the Greenhouse Gas Reduction Fund to various projects. Sixty percent of future auction proceeds are allocated to an amalgam of programs, including affordable housing, high-speed rail, and public transit. S.B. 852, 862 (June 20, 2014). The Petitioners hereby request that this Court take judicial notice of those 2014 enactments. *Dailey v. City of San Diego*, 223 Cal. App. 4th 237, 244 n.1 (2013) (Courts may take judicial notice of post-judgment legislative changes relevant to an appeal.)

STANDARD OF REVIEW

A trial court's denial of a petition for writ of mandate is reviewed *de novo* where the decision does not involve any disputed facts. *Prof'l Eng'rs in Cal. Gov't v. Kempton*, 40 Cal. 4th 1016, 1032 (2007). The facts in this case are undisputed. Whether the Auction Provisions are unconstitutional or

unauthorized by statute are legal questions with regard to which an appellate court does not defer to the trial court's decision. *Gilbert v. City of Sunnyvale*, 130 Cal. App. 4th 1264, 1275 (2005) ("In resolving questions of law on appeal from a denial of a writ of mandate, an appellate court exercises its independent judgment."). *See Reid v. Google, Inc.*, 50 Cal. 4th 512, 527 (2010) (*de novo* review for statutory construction issues); *Apartment Ass'n of Los Angeles County, Inc. v. City of Los Angeles*, 24 Cal. 4th 830, 836 (2001) (*de novo* review for construction of constitutional amendments adopted by voter initiative).

Differing specific *de novo* review standards apply, however, depending upon whether the issue is one constitutional or statutory construction. On the issue of whether a revenue-generating imposition or levy is an unconstitutional "tax" or an allowable "regulatory fee," the standard of review depends on whether the imposition is controlled by Proposition 26 or by Proposition 13. Cal. Const. art. XIII A, § 3. For impositions mandated *after* November 3, 2010, the effective date of Proposition 26, CARB bears the burden of proving by a preponderance of the evidence that the imposition is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor's burdens on, or benefits received from, the governmental activity. Cal. Const., art. XIII A, § 3(d). On the other hand,

for impositions enacted *prior* to November 3, 2010, Proposition 13 applies. Under Proposition 13, the Petitioners are required to make a prima facie showing that the imposition is an unconstitutional tax. But once a prima facie showing is made, CARB bears the "burden of production and must show '(1) the estimated costs of the service or regulatory activity, and (2) the basis for determining the manner in which the costs are apportioned, so that charges allocated to a payor bear a fair or reasonable relationship to the payor's burdens on or benefits from the regulatory activity.' " *Cal. Farm Bureau Fed'n v. State Water Res. Control Bd.*, 51 Cal. 4th 421, 436-37 (2011) (quoting *Sinclair Paint Company v. State Bd. Of Equalization*, 15 Cal. 4th 866, 878 (1997).

Finally, on the issue of whether an administrative agency exceeded its authority, this Court gives no deference to the agency's interpretation of the statute at issue. *See Cal. Ass'n of Psychology Providers v. Rank*, 51 Cal. 3d. 1, 11-12 (1990) (government not entitled to deference if "the regulations transgress statutory power").

SUMMARY OF ARGUMENT

The revenues CARB has collected and intends to collect by auctioning emission allowances are unconstitutional, not authorized by statute, or both. They are illegal taxes in violation of California Constitution, Article XIII A, Section 3 (**Proposition 13**), because A.B. 32 was not enacted by at least a two-

thirds supermajority vote of the California Legislature. And the auction revenues cannot be characterized as valid regulatory fees under *Sinclair Paint* and its progeny because: (1) they are not limited to the reasonable costs of any regulatory program, (2) there is no reasonable relationship between the amounts bid at auction and the bidder's regulatory burdens or benefits, and (3) the Cap and Trade Regulation does not prohibit the revenue from being used for purposes that are unrelated to CARB's greenhouse gas emissions limitations program.

In the alternative, the Cap and Trade Regulation is ultra vires because A.B. 32 does not authorize CARB to generate billions of dollars of revenues for California by selling emission allowances at auction. If there is any ambiguity in A.B. 32's language regarding whether auctions are authorized, overwhelming evidence in the legislative history shows that the Legislature did not intend for CARB to generate billions from its implementation of A.B. 32.

Finally, if A.B. 32 does not authorize CARB to generate billions, then any effort by the Legislature to authorize the auctions after-the-fact in 2012, is unconstitutional because not one of the relevant 2012 legislative enactments was passed by at least a two-thirds supermajority of the Legislature. Cal. Const. art. XIII A, § 3 (**Proposition 26**). For the same reason, the relevant 2014 legislation cannot support the auctions.

ARGUMENT

I

THE REVENUE GENERATED BY THE AUCTION IS AN ILLEGAL TAX IN VIOLATION OF CALIFORNIA CONSTITUTION ARTICLE XIII A, SECTION 3 (PROPOSITION 13)

The People's Initiative to Limit Property Taxation, known as Proposition 13, amended the Constitution of California in 1978. Under Proposition 13, any legislation to increase state taxes "for the purpose of increasing revenues" must be passed by at least a two-thirds supermajority vote of the members of both houses of the Legislature. Cal. Const., art. XIII A, § 3. *See, Cal. Farm Bureau Fed'n*, 51 Cal. 4th 421 at 428.

A.B. 32 was not passed by two-thirds of the members of the Legislature and, therefore, it cannot be used to raise state taxes (JA0809-0810) (vote tally in Assembly and Senate). In construing Proposition 13, the California Supreme Court held in *Sinclair Paint* that if a revenue generating measure is a regulatory fee and not a tax, Proposition 13 does not require a supermajority vote. *See* 15 Cal. 4th at 876-78. The question in the instant case is whether CARB's revenue-generating auctions are unconstitutional taxes or valid regulatory fees.

A. The Revenues Generated by CARB's Auctions Are Unconstitutional Taxes Under Proposition 13 Because They Fail To Meet the Requirements of the California Supreme Court's *Sinclair Paint* Test

Under Proposition 13, any revenue generating measure related to a regulatory scheme is subject to a four-pronged test established in *Sinclair Paint* to determine whether it is a tax or a regulatory fee. Under the test, the following requirements all must be met:

(1) There must be "a causal connection or nexus between the product [or regulated activity] and its adverse effects," *Sinclair Paint*, 15 Cal. 4th at 878;

(2) The total amount of money raised by the program must be "limited to the reasonable costs of . . . [the] program," *id.*, as defined by "amounts necessary to carry out the regulation's purpose," *id.* at 876;

(3) The allocation of burdens among payors must reflect "a fair or reasonable relationship" between the charges allocated to a payor and "the payor's burdens on or benefits from the regulatory activity," *id.* at 878 (quoting *San Diego Gas & Elec. Co. v. San Diego Cnty. Air Pollution Control Dist.*, 203 Cal. App. 3d. 1132, 1146 (1988)); and

(4) The fees must not be used "for unrelated revenue purposes." *Id.*

The auctions under the Cap and Trade Regulation fail to meet the second, third, and fourth prongs of the *Sinclair Paint* test.

1. CARB's Auction Revenue Fails To Meet the Second Prong of the *Sinclair Paint* Test Because the Revenue Is Not Limited to the Reasonable Costs of the Regulatory Program

To constitute valid regulatory fees and not taxes, the revenues may not "exceed in amount the reasonable cost of providing the protective services for which [they were] charged," *Sinclair Paint*, 15 Cal. 4th at 876 (citing *Pennell v. City of San Jose*, 42 Cal. 3d. 365, 375 (1986)). For four reasons, CARB's auctions fail this prong of the *Sinclair Paint* test: (1) CARB cannot determine in advance of any auction the amount of revenues that will be generated, (2) CARB cannot provide any reasonable estimate of the regulatory costs because many of the specific programs to be funded by the auction revenues are either not identified or unauthorized, (3) there is no safeguard to authorize the lowering or reimbursement of auction payments if proceeds are found to exceed the cost of the regulatory program, and (4) the auction revenues are unnecessary to administer or implement the regulatory program. Each of these criteria is examined.

a. CARB Cannot Determine in Advance of Any Auction the Amount of Revenues That Will Be Generated

Each auction is conducted as a single round bidding process where "bids will be sealed," so that no bidder knows the amount of any other will bid, and CARB does not know in advance the amount of revenues that will be collected. 17 C.C.R. § 95911(a)(1)-(2). This makes it impossible for CARB

to determine whether auction revenues will be greater than, less than, or equal to the "reasonable costs" of the regulatory program. Auction revenues are a function of the "blind" bids made by bidders at each auction, which depends entirely on what individual bidders may be willing to bid at any particular time, based upon their own economic decisions. Rabo Decl. ¶¶ 2, 18 (JA0840,0842). Accordingly, the requisite alignment between the auction revenues and the "reasonable costs of providing" the regulatory service is missing. *Sinclair Paint*, 15 Cal. 4th at 876.

b. CARB Cannot Provide Any Reasonable Estimate of the Regulatory Costs Because Many of the Specific Programs To Be Funded by the Auction Revenues Are Either Not Identified or Unauthorized

Under *Sinclair Paint*, CARB must provide at least an estimate of the regulatory costs, yet none has been provided. "[T]o show a fee is a regulatory fee and not a special tax, the government should prove . . . the estimated costs of the service or regulatory activity." *Sinclair Paint*, 15 Cal. 4th at 878, (quoting *San Diego Gas & Elec. Co. v. San Diego Cnty. Air Pollution Control Dist.*, 203 Cal. App. 3d. at 1146). CARB's auctions fail to meet this requirement because CARB has made no findings in the Cap and Trade

Regulation or elsewhere[2], regarding the estimated costs of services or regulatory activities to be funded by auction revenue.

c. There Is No Safeguard To Authorize Reimbursement of Auction Payments If Proceeds Are Found To Exceed the Cost of the Regulatory Program

Regulatory safeguards are absent for ensuring that auction payments are reimbursed if auction revenue exceeds the cost of the regulatory program. The Cap and Trade Regulation does not provide for funds generated at auction to be returned to the successful auction bidders if it is determined, in retrospect, that they paid more than their *pro rata* share for the "service or regulatory activity." *Sinclair Paint*, 15 Cal 4th at 878. Accordingly, there is a built-in risk that bidders will pay more than is required to fund the regulatory program, something that is antithetical to *Sinclair Paint*.

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[2] California's recently issued "Cap-and-Trade Auction Proceeds Investment Plan: Fiscal Years 2013-14 through 2015-16" (the "Investment Plan") sets forth certain recommendations to the Legislature regarding "priority State investments to help achieve greenhouse gas reduction goals and yield valuable co-benefits," but the Investment Plan does not provide cost estimates of *actual* services or regulatory activity to be funded by auction revenues. Those depended entirely on future legislation. ("[I]nclusion of a recommended investment in this plan does not guarantee funding.") (JA0736). It is true that 2014 legislation allocates certain moneys in the Greenhouse Gas Reduction Fund to some specific projects, but several of them (e.g., affordable housing, high speed rail) have little if any relationship to compliance with A.B. 32's greenhouse gas emissions reduction goals and, therefore, do not provide funds for a relevant "government service or activity." 203 Cal. App. 3d. at 1146.

d. The Auction Revenues Are Unnecessary To Administer or Implement the Regulatory Program

CARB's costs of administering the A.B. 32 program are already funded under the Act's administrative fees provision, which authorizes CARB to promulgate regulations adopting "a schedule of fees to be paid by [regulated] sources of greenhouse gas emissions." Health & Safety Code § 38597. The, revenues must be used "for purposes of carrying out this division." *Id.* Thus, A.B. 32 section 38597 contemplates that the regulatory fees authorized therein *themselves* will pay for the costs associated with CARB's administration of A.B. 32. In fact, CARB has promulgated a detailed fee regulation implementing section 38597, the sole purpose which is to "collect fees to be used to carry out the California Global Warming Solutions Act of 2006, as provided in Health and Safety Code section 38597" (internal citations omitted). 17 C.C.R. § 95200. That fee regulation is separate from CARB's Cap and Trade Regulation. And the formula that must be used to calculate the amount of administrative fees provides explicitly for the full recovery of the total costs of implementing A.B. 32's regulatory program. "The Required Revenue [from the fee regulations] shall be the *total* amount of funds *necessary to recover the costs of implementation of A.B. 32 program expenditures for each fiscal year.*" 17 C.C.R. § 95203(a)(1). (Emphasis

added.) Accordingly, there is no need for proceeds from an auction to cover the "costs of implementation of A.B. 32's program." *Id.*

Indeed, the Cap and Trade Regulation states that "[t]he purpose of [the Cap and Trade Regulation] is to reduce emissions of greenhouse gases," 17 C.C.R. § 95801, while the administrative fee regulation states that the "total amount of funds necessary to recover the costs of implement[ing]" the Cap and Trade Regulation is provided by the administrative fee regulation. *See* 17 C.C.R. § 95203(a)(1). Applying the *Sinclair Paint* test, the "costs of the service or regulatory activity" implementing the Cap and Trade Regulation are fully recovered by CARB under the administrative fee regulation and, therefore, the auction revenues are not reasonably necessary to achieve the regulatory purpose, 15 Cal. 4th at 876.

Conceivably, one may posit that CARB's administrative fees may be insufficient to pay for the broader goals of A.B. 32, namely, to deal generally with problems posed by global warming. Such an argument fails under *Sinclair Paint,* because CARB has made no findings in the Cap and Trade Regulation or elsewhere regarding "the estimated costs" of addressing the issue of global warming, in or outside of California, and no "total budgeted cost" of dealing with global warming has been projected. *Sinclair Paint,* 15 Cal. 4th at 876. CARB has not even estimated the extent to which California's greenhouse gas emissions reductions, at whatever cost, may have

any beneficial effect on reducing global warming, thereby running afoul also of *Sinclair Paint's* reasonable alignment requirement. *See* 15 Cal. 4th at 876.

Accordingly, for the four reasons set forth in this Section I.A.1., CARB's auction revenues fail the second prong of the *Sinclair Paint* test.

2. CARB's Auction Revenue Generation Fails To Meet the Third Prong of the *Sinclair Paint* Test Because the Winning Bids at CARB's Auctions Bear No Relationship to Any Burdens Imposed or Benefits Received by the Bidders from the Regulatory Program

The third prong of the *Sinclair Paint* test requires that the allocation of charges among payors reflect "a fair or reasonable relationship" between the charges allocated to each payor and "the payor's burdens on or benefits from the regulatory activity," 15 Cal. 3d. at 878. Because the revenues generated by CARB's auction are determined by competitive bidding among prospective payors, the ultimate allocation of these charges among payors can bear no more than an accidental relationship to either the burdens imposed or the benefits received by any individual payor.

In the context of A.B. 32, the relevant "burden imposed" by Covered Entities could be reasonably construed as their contribution to global warming. Yet the Cap and Trade Regulation acknowledges that different types of greenhouse gas emissions have different "global warming potential," depending on whether the emissions are of carbon dioxide or other greenhouse gases. *See* in 17 C.C.R. § 95802 (43) (definition of "carbon dioxide

equivalent"). The auctions, however, do not distinguish between allowances for the emission of greenhouse gases with relatively higher or lower "global warming potential." Thus, the ultimate allocation of charges at the conclusion of an auction bears a completely unknown relationship to the burdens imposed by the bidders' relative contributions to global warming. The allowances may be purchased by Covered Entities emitting solely carbon dioxide; or they may be purchased by Covered Entities emitting greenhouses gases with lesser or greater "global warming potential," in a variety of combinations. Consequently, the ultimate allocation of charges under the auctions can bear no more than a random relationship to any actual burdens imposed on the atmosphere by the successful bidders. Accordingly, because CARB does not know how the charges from the auctions are distributed with respect to the actual burdens imposed by Covered Entities, CARB cannot establish a "reasonable relationship" between charges and burdens imposed by payors, as required by *Sinclair Paint.*

Similarly, the allocation of charges under CARB's auctions bears no systematic or predictable relationship to the *benefits* successful bidders receive from emitting greenhouse gases. The amount a Covered Entity bids for allowances is determined by each Covered Entity's opportunity costs—in this case, the cost of reducing emissions by upgrading the Entity's facility instead of purchasing CARB's allowances at auction. (JA0840,0842). This internal

economic calculation will be unique to each firm, and will vary according to the age, capacity, specific use, and technology employed in each facility. It will also vary by utilization rate and the ease with which each Covered Entity can shift its production activities to other facilities. Assuming that bidders calculate their costs accurately, CARB's auction results will distribute emissions allowances roughly in proportion to the bidders' relative costs of participating or not participating in the auctions. But this does not meet *Sinclair Paint's* requirement that the allocation of charges must be "fairly or reasonably related" to the benefits Covered Entities receive from the regulated activity (JA0842, JA0690). The only "benefit" successful bidders receive here is the requirement to pay for what they had been doing before for free, and then to surrender the allowances purchased without receiving the purchase price back, only to pay additional sums for allowances covering subsequent compliance periods. Surely this stretches the term "benefit" to the breaking point.

Because CARB's auction revenues are not related to the costs of government regulatory services, but rather to the economic forces operating within the auction, the auction prices bear no discernable relationship to either the burdens on global warming posed by Covered Entities or the benefits they derive by participating in the auctions. Accordingly, the government cannot meet its burden of demonstrating that the auction mechanism apportions costs

in a manner reasonably related to either the burdens or benefits of payors. *Sinclair Paint*, 15 Cal. 4th at 878; *see Cal. Ass'n of Prof'l Scientists v. Dep't of Fish & Game*, 79 Cal. App. 4th 935, 945 (2000) (citing *Beaumont Investors v. Beaumont-Cherry Valley Water Dist.*, 165 Cal. App. 3d. 227, 235 (1985)).

3. CARB's Auction Revenue Generation Fails To Meet the Fourth Prong of the *Sinclair Paint* Test Because the Cap and Trade Regulation Does Not Prohibit the Revenue from Being Used "For Unrelated Revenue Purposes"

CARB's Cap and Trade Regulation provides no indication regarding where or how the revenues from the auctions will be used. Neither does A.B. 32. Accordingly, neither prohibits the auction revenues from being used for "unrelated revenue purposes," which contravenes the fourth prong of the *Sinclair Paint* test. 15 Cal. 4th at 878. The sole question remaining is whether any combination of the bills enacted by the Legislature in 2012 or later, purporting to allocate the auction revenues, satisfies that fourth prong. The answer is no.

S.B. 1018, enacted in 2012, does not amend A.B. 32. Rather, it establishes the "Greenhouse Gas Reduction Fund" as a special fund in the State Treasury and requires that any money collected by CARB through its auction or sale of emissions allowances be deposited into that fund and made available for appropriation by the Legislature. Gov't Code § 16428.8 (a), (b). The statute explicitly provides: "Notwithstanding any other law, the

Controller may use the moneys in the fund for cash flow loans to the General Fund." *Id.* § 16428.8(d). The statute does not dedicate the cash flow loans for any specific purpose, and the Controller is free to use the loan proceeds for any purpose he may deem fit. Moreover, nothing in S.B. 1018 dedicates or limits the use of *any* amounts in the Greenhouse Gas Reduction Fund to any specific purpose.

Next, neither A.B. 1532 nor S.B. 535 amends A.B. 32. The two bills work in tandem to provide some general guidance on how monies located in the Greenhouse Gas Reduction Fund should be spent, but they fail to identify which projects will qualify for funding. A.B. 1532 directs California's Finance Department to develop a three-year investment plan to use the funds to reduce greenhouse gas emissions. Investments would target areas such as clean energy, low carbon transportation and infrastructure, natural resource protection, and research and development. As set forth in footnote 2, *supra*, on May 14, 2013, California issued a first version of the Investment Plan called for in A.B. 1532, but that document does not prohibit auction revenues from being used for "unrelated purposes." By its own terms the Investment Plan merely identifies and prioritizes a wish list for the utilization of auction revenues, subject to legislative approval (JA0736). ("[I]nclusion of a recommended investment in this plan does not guarantee funding.")

In turn, the 2012-enacted S.B. 535 requires the Finance Department to set aside 25% of the Greenhouse Gas Reduction Account to projects benefitting disadvantaged communities, and at least 10% of that fund must go toward projects actually located in such communities. Of course, S.B. 535 begs the question: What if any evidence is there to establish that the 25% or 10% set-asides for disadvantaged communities bear any "related purpose" to greenhouse gas emissions or, for that matter, to global warming? *See* 15 Cal. 4th at 878. Although it may be a good thing to benefit disadvantaged communities, and although A.B. 32 encourages CARB to ensure that such communities benefit from "statewide efforts to reduce global warming," CARB has not established any relationship between reducing greenhouse gas emissions and benefitting disadvantaged communities. And the fact that neither A.B. 1532 nor S.B. 535 actually sets forth how the funds will be used for specific greenhouse gas emissions reductions projects means that neither the Legislature, nor CARB, has dedicated either the 25% or, for that matter, the remaining 75% of the funds in a manner that meets the fourth prong of the *Sinclair* test.[3]

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[3] This issue is also relevant to the third prong of the *Sinclair Paint* test, namely, whether there is any "reasonable relationship" to the social or economic burdens generated by covered entities that emit carbon dioxide. *See Sinclair Paint*, 15 Cal. 4th at 878. No such relationship is evident in the Cap and Trade Regulation, A.B. 32, or any of the 2012 or 2014 enactments.

In turn, A.B. 1464, the last of the 2012 enactments, does not amend A.B. 32. Rather, it provides that, notwithstanding any other provision of law, the Director of Finance may allocate or otherwise use an amount of "at least" $500 million from moneys derived from the sale of greenhouse gas emission allowances, and make commensurate reductions to General Fund expenditure authority. 2012 Stats. Ch. 21, § 15.11(a). Although A.B. 1464 provides that the "funds shall be available to support the regulatory purposes of [A.B. 32]," section 15.11(a), the enactment does not define the criteria by which the Director of Finance shall decide whether any particular expenditure may "support the regulatory purposes" of A.B. 32. That glaring omission, when considered in light of the explicit authority to "make commensurate reductions to General Fund expenditure authority," provides the Director of Finance with more leeway than permitted under *Sinclair Paint* with regard to the "at least" $500 million he is authorized to siphon from the Greenhouse Gas Reduction Fund. Accordingly, for purposes of *Sinclair Paint*, A.B. 1464 does not sufficiently constrain the Director of Finance from using the funds for "unrelated purposes" and, therefore, fails the fourth prong of the *Sinclair Paint* test.

The 2014 bills fare no better, because they allocate auction revenues for purposes that on their face are "unrelated" to greenhouse gas reduction, such as affordable housing and high-speed rail. *See* Statement of Facts, *supra*.

B. The Trial Court Erred in Holding That the Auction Revenues Are Not Unconstitutional Taxes Under Proposition 13

The court below held that the billions of dollars to be generated by the auctions are not taxes under Proposition 13 because: (1) CARB did not have a predominantly revenue-generating purpose in rasing the billions; (2) successful auction bidders pay market prices for emissions allowances; (3) payments for the emissions allowances are voluntary, and (4) the auction revenues cannot be used for general government purposes. Opinion at 17-22 (JA1611-1616). The trial court was mistaken on all points.

The trial court acknowledged that:

> It is undisputed that the auction provisions of A.B. 32 will result in a cumulative net increase in state revenues [and that] if the cost of allowances are 'taxes,' A.B. 32 violates Proposition 13.

JA1607. While characterizing the Proposition 13 challenge as "a close question," the trial court held that the revenues were fees and not taxes (JA1609-1610).

The court did not try to address the burdens of proof or standards of review established by *Sinclair Paint* and its progeny. Rather, it cobbled together burdens and standards that are unrecognizable under the four-pronged analysis mandated by *Sinclair Paint.* "The decisions of [the California Supreme Court] are binding upon and must be followed by all the state courts

of California." *McClung v. Employment Dev. Dep't*, 34 Cal. 4th 467, 473 (2004).

Significantly, the California Legislature has recognized that the auction revenues are subject to the *Sinclair Paint* test. S.B. 957, the Budget Act of 2012-2013, states:

> The Legislature finds that . . . the funds generated by the [CARB auctions] are regulatory fees [under] *Sinclair Paint Co. v. State Board of Equalization* (1997) 15 Cal.4th 866.

S.B. 957, Section 15.11c. Thus, the Legislature has acknowledged that the *Sinclair Paint* test applies to any determination of whether the auction revenues at issue here are unconstitutional taxes under Proposition 13. On the other hand, the *substantive* finding of the 2012 Legislature that the auctions constitute regulatory fees need be given no weight because

> [a] legislative declaration of an existing statute's *meaning* is neither binding nor conclusive in construing the statute. Ultimately, the interpretation of a statute is an exercise of the judicial power the Constitution assigns to the courts.

Western Security Bank v. Superior Court, 15 Cal. 4th 232 (1997) (emphasis added). The same can be said for CARB's own views regarding whether the auctions are fees or taxes: "This is a question particularly suited for the judiciary as the final arbiter of the law, and does not invade the technical expertise of the agency." *Samantha C. v. State Dept. of Developmental Services*, 185 Cal. App. 4th 1462, 1482 (2010), (quoting *Aguiar v. Superior Court*, 170 Cal. App. 4th 313, 323 (2009)).

Giving short shrift to *Sinclair Paint,* the lower court opines that the enormous sums to be generated by the auctions are mere "byproducts" of the regulatory program to curb carbon dioxide emissions and revenue generation is not the "primary reason"for the auctions (JA1615). But neither *Sinclair Paint* nor its progeny suggest that, where the revenue generation is a "byproduct" of a regulatory program, *the Sinclair Paint* standards are inapplicable. To the contrary, *Sinclair Paint* itself is a case in which the Supreme Court decided whether the revenues generated as a "byproduct" of a regulatory program aimed at curbing lead poisoning constituted taxes subject to Proposition 13. 15 Cal. 4th at 874-76. Calling the auction revenues a "byproduct" of the regulation does not make them any less of a tax.

Moreover, the lower court's holding falls under the weight of its own analysis. Assuming arguendo the lower court's conclusion that raising revenues was a byproduct of the regulatory scheme and not the primary reason for the Auction Provisions, that is irrelevant to the issue of whether the auctions are constitutional. There is no dispute that A.B. 32 did not pass with the required two-thirds supermajority. There is no dispute that the auctions will raise billions of dollars for the state. And there is no dispute that CARB *intended* to raise those billions. It was not an accident. Accordingly, using the specific language of Proposition 13, the auctions came about "for the purpose of increasing revenues collected," regardless of whether that purpose was a

primary, secondary, or tertiary one. Cal. Const. art. XIII A, § 3. At the very least, CARB's "purpose of increasing revenues collected" *furthered* one or more of CARB's other purposes, making it *a* purpose of the auctions. Significantly, the lower court cited no case standing for the proposition that, where regulation is the primary purpose, revenues cannot be considered taxes.

The court's citation to *California Taxpayers' Ass'n v. Franchise Tax Bd.*, 190 Cal. App. 4th 1139 (2010), justifies neither the reasoning employed nor the result reached. *California Taxpayers* involved a statutory penalty imposed upon corporate taxpayers who underpaid their taxes by more than $1 million. The issue was whether the government should be required to show that the penalty was "reasonably necessary to the cost of providing [a] service or regulatory activity." *Id.* at 1145. The Fourth Appellate Division held that the government need not be put to that showing because, under the circumstances of that case, "[w]e do not deal with a situation in which *only the government has the information* to show the cost of the service or regulatory activity . . .. Instead we deal with a statutory '*penalty*' that applies only if a 'tax' has not been fully paid." *Id.* at 1146 (emphasis added). By contrast, this case *is* a situation in which, if anyone has information regarding the "cost of the service or regulatory activity" at issue, namely the costs of reducing greenhouse gas emissions sufficient to comply with the Cap and Trade Regulation or, more generally, the costs of dealing with global warming, *only*

the government could have such information. Auction bidders cannot be expected to divine those costs. Rabo Reply Decl. ¶¶ 17-18 (JA1399-1400). Moreover, here no one has asserted that the auction revenues constitute a "penalty."

The court's citation to *Schmeer v. County of Los Angeles*, 213 Cal. App. 4th 1310 (2013), also is not helpful. *Schmeer* involved Proposition 26, under which the distinction between a regulatory fee and a tax is irrelevant. *Id.* at 1323-25. That case held that a county ordinance enacted after the effective date of Proposition 26 requiring customers to pay 10 cents for each paper carryout bag provided by retail stores was not a tax because the money was paid to the stores and was not remittable to any level of government. *Id.* at 1326. By contrast, here billions are going to the state government. Under these circumstances, the instant case sets up "a clear, substantial, and irreconcilable conflict" between the auctions, on the one hand, and the California Constitution on the other hand. *Pajaro Valley Water Mgmt. Agency v. Amrhein*, 150 Cal. App. 4th 1364, 1380 (2007), (quoting *Orange County Water District v. Farnsworth*, 138 Cal. App. 2d 518, 530 (1956)). These are precisely the circumstances to which *Sinclair Paint* applies.

The lower court opines further that, because auction bidders get something of value that may be traded, auction revenues are not a tax. (JA1611). But value passes to a payor in many situations that have long been

recognized as taxes. For example, when a consumer purchases any tangible thing, a sales tax is paid. The fact that the tangible item has value does not make the sales tax any less of a tax. Although it is true that financial firms may benefit if they trade allowances profitably, Covered Entities are required to obtain emissions allowances in order to stay in business in California. The only "benefit" they receive is the ability to continue doing what they have always been doing, but they will be required to do less of it and pay for the "privilege."

The lower court observes that the auction differs from paying a tax because the amount of the payment is not determined by a tax rate, tax schedule, or other act of the government. That is not true. CARB has set a minimum price for all emissions allowances. The Cap and Trade Regulation states that "[e]ach auction will be conducted with an auction reserve price" established by CARB, 17 C.C.R. § 95911(b)(1), and "[n]o allowances will be sold at bids lower than the auction reserve price," 17 C.C.R. § 95911(b)(2). Thus, the minimum payment that must be paid at auction is determined by an act of government. For example, CARB established the auction reserve price, or floor price, at a minimum bid of $10 for the first auction and $10.71 for the following two auctions. Rabo Reply Decl. ¶ 13 (JA1399).

The court goes on to state that auction revenues are not taxes because participation in the auctions is voluntary and not mandatory. But Covered

Entities are required to have emissions allowances in order to emit carbon dioxide. It is true that they may choose to move out of the state and no longer be subject to the California emissions requirements. By the same token, a California resident may choose to move out of the state and no longer be subject to California income taxes. But that does not make the state income tax any less of a tax. One of the declarants stated it well: "Morning Star has absolutely no choice but to participate in the auctions if it wants to stay in business in California." *See* Rabo Reply Decl. ¶ 14 (JA1399). "The notion that, as a Covered Entity, Morning Star's participation in the CARB auctions is somehow 'voluntary' is both false and ridiculous." Rabo Reply Decl. ¶ 16 (JA1399). Significantly, any distinction between "voluntary" and "compulsory" payments played no role in the tax-versus-fee analysis in the *Sinclair Paint* and *Cal. Farm Bureau* decisions.

Next, the lower court states that auction revenues are not taxes because they cannot be used for the general support of the government (JA1614). But that is not true, either. Before the 2012 statutes were enacted, there were no limitations on expenditures of auction revenues. After the 2012 statutes were enacted, some limitations were imposed, but not in ways that support the lower court's holding. For example, S.B. 535 requires the Finance Department to set aside 25% of the Greenhouse Gas Reduction Account to projects benefitting "disadvantaged" communities, and at least 10% of that fund must go toward

projects actually located in such communities. Benefitting disadvantaged communities is an important function of general government, and 25% of many billions of dollars could go a long way toward providing the government with the means to discharge such a general obligation. Thus, not only can a good portion of the total auction revenues be used to support general government responsibilities, but it *must* be so used.

In addition, A.B. 1464 provides that the Director of Finance may allocate or otherwise use an amount of "at least" $500 million from moneys derived from the sale of emissions allowances and make commensurate reductions to *General Fund* expenditure authority. There is no limit to the amount of funds that actually can be used in this way. Finally, S.B. 1018 authorizes the Controller to borrow funds from the auction revenues "for cash flow loans to the General Fund." Gov't Code § 16428.8(d). Interestingly, the *entire amount* deposited into the Greenhouse Gas Reduction Fund from the first three auctions were immediately "borrowed" for use in the General Fund. (JA0759).

II

CARB'S AUCTION IS ULTRA VIRES BECAUSE A.B. 32 DOES NOT AUTHORIZE CARB TO GENERATE BILLIONS OF DOLLARS OF REVENUE

Statutes should be construed whenever possible so as to preserve constitutionality, based on the presumption that the Legislature intended not

to violate the Constitution. *Harrot v. County of Kings*, 25 Cal. 4th, 1138, 1153 (2001). Accordingly, courts will construe a statute so as to avoid addressing its constitutionality, even though another construction may also be reasonable. *Id.* Because A.B. 32 may be reasonably construed so as not to authorize the Auction Provisions, the principal of constitutional avoidance informs the judgment of this Court on the ultra vires issue. This Section addresses that issue.

A. No Deference Is Given to an Administrative Agency's Interpretation of a Statute When the Issue Is Whether an Agency's Regulation Transgresses Statutory Power

The Supreme Court has stated:

> [I]n finding that the challenged regulations contravened legislative intent, [we] rejected the agency's claim that the only issue for review was whether the regulations were arbitrary or capricious. . . . *Administrative regulations that alter or amend the statute or enlarge or impair its scope are void and courts not only may, but it is their obligation to strike down such regulations.*

Cal. Ass'n of Psychology Providers v. Rank, 51 Cal. 3d at 11 (emphasis added, internal quotation marks and citation omitted). The Supreme Court recently echoed these sentiments in *Western States Petroleum Ass'n v. Board of Equalization*, 57 Cal. 4th 401, 416 (2013) (courts exercise independent judgment on issues of whether a regulation exceeds statutory authority). Because the issue here is whether CARB transgressed its statutory power by

including the auctions as part of the Cap and Trade Regulation, deference to CARB's statutory interpretation is neither merited nor permitted.

B. A.B. 32 Does Not Authorize CARB To Generate Billions of Dollars From the Sale or Auction of Emissions Allowances

No provisions of A.B. 32, either individually or collectively, authorize the Auction Provisions promulgated by CARB.

1. A.B. 32's Only Fee Provision Does Not Authorize an Auction

A.B. 32's sole fee provision authorizes CARB to promulgate regulations adopting "a schedule of fees to be paid by [regulated] sources of greenhouse gas emissions." Health & Safety Code § 38597. The revenues are to be used "for purposes of carrying out this division." *Id.* Nothing in section 38597 authorizes CARB to auction the emissions allowances that it creates. By its own terms, section 38597 contemplates that regulatory fees will pay for the costs of CARB's implementation of A.B. 32.

CARB promulgated separate fee regulations implementing section 38597, whose purpose is to "collect fees to be used to carry out the California Global Warming Solutions Act of 2006, as provided in Health and Safety Code section 38597" (citations omitted). 17 C.C.R. § 95200. The formula to be used to calculate the amount of administrative fees provides for the recovery of the total costs of implementing A.B. 32. *Id.* § 95203. Because the fee regulations provide the funds needed by CARB to "carry out" A.B. 32's

mandates, there is no need for proceeds from an auction to cover CARB's costs of administering or implementing those mandates.

2. A.B. 32's "Market-based Compliance Mechanisms" Language Does Not Authorize CARB To Collect Auction Revenue

A.B. 32 permits but does not require CARB to regulate greenhouse gases by a market-based cap and trade program. Specifically, Part 5 of A.B. 32, sections 38570, 38571, and 38574, sets forth guidelines for rules should CARB establish "market-based compliance mechanisms." None of these provisions explicitly authorize CARB's auctions. CARB's auction scheme is a massive multi-billion dollar program that reaches into every nook and cranny of California's economy. It has the potential of creating huge alterations, and even dislocations, in the range of businesses operating in California. Its impact on jobs and the loss of jobs is poorly understood, at best. A court should not take lightly CARB's attempt to divine its authority to undertake such a massive and far-reaching program from a few snippets of A.B. 32—snippets that do not provide any clear authority for what has evolved into one of California's most intrusive regulatory schemes in its history.

Section 38570c states that CARB "shall adopt regulations governing how market-based compliance mechanisms may be used by regulated entities subject to greenhouse gas emission limits . . . to achieve compliance." (Emphasis added.) The plain language directs CARB to create "compliance

mechanisms" for the use of those who must meet greenhouse gas emissions limits. *Regents of Univ. of Cal. v. East Bay Mun. Util. Dist.*, 130 Cal. App. 4th 1361, 1372-73 (2005) (courts must give meaning and purpose to every word used by the Legislature). But CARB itself has no obligations to comply with emissions limitations. By becoming a direct participant in the market-based compliance mechanisms it has established, CARB has set the stage to be the recipient of billions of dollars of auction revenues, which the language of A.B. 32 does not support. *People v. McNamee*, 96 Cal. App. 4th 66, 72 (2002) (statutory interpretation leading to absurd results must be avoided).

In turn, section 38505(k) of AB 32 defines the term "market-based compliance mechanism" to mean either of the following:

> (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.

Health & Safety Code § 38505(k) (emphasis added). The language in subdivision 1 does not explicitly authorize an auction. Neither is there any indication that CARB's auction scheme is required or desired to implement the "system of market-based annual aggregate emissions limitations." Indeed,

subsection 1 states that market-based emissions limitations are for "sources that emit greenhouse gases," in other words, for Covered Entities. At most, subdivision 1 is silent regarding the appropriateness of an auction. *Dean v. Superior Court*, 62 Cal. App. 4th 1066, 641-42 (2002) (statute's silence not be interpreted as authorization).

Focusing on subdivision 2, there is nothing that expressly provides authority for CARB's Auction Provisions. Subdivision 2 speaks specifically to actions that are to be taken *by* Covered Entities under CARB-generated "rules and protocols," and conspicuously omits any use of the term "allowances," using instead the term "credits" when referring to transactions among Covered Entities, saving the term "allowances" for CARB's *creation* of compliance instruments. *Lungren v. Deukmejian*, 45 Cal. 3d. 727, 735 (1988) (use and omission of statutory terms must be construed in the context of the statute as a whole).

Further, the statutory terms that precede the term "other transactions" provide for "exchanges, banking [and] credits." Those terms imply business transactions *among* Covered Entities and not business transactions between Covered Entities and the regulator CARB. As one California appellate court stated, "a word takes meaning from the company it keeps." *People v. Jones*, 112 Cal. App. 4th 341, 354 (2003). In fact, the Supreme Court of California has long applied the statutory construction principle of *esjusdem generis*,

which "holds that where general words follow the enumeration of particular classes of persons or things, the general words will be construed as applicable only to persons or things of the same general nature or class as those enumerated." *Harris v. Capital Growth Investors XIV*, 52 Cal. 3d. 1142, 1160 (1991) (internal quotes and citations omitted).

Thus, nothing in Section 38505(k) can be fairly characterized as a grant of authority to CARB to establish an auction system by which CARB may generate billions of dollars of revenue for the state. Significantly, no provision of A.B. 32 sets forth or attempts to define even the most basic elements of an auction, such as a seller, an auctioneer, bidders, or the fate of the auction proceeds. Indeed, the term "auction" is an utter stranger to the statute, as well as to it's pre-enactment legislative history. If the Legislature had intended to authorize auctions of this magnitude in connection with the creation and distribution of allowances to Covered Entities it could have easily said so. But it did not.

It is true that the Cap and Trade Regulation itself defines the term "auction" as "the process of selling California Greenhouse Gas Allowances by offering them up for bid, taking bids, and then distributing the allowances to winning bidders." But this regulatory definition of a term that does not appear anywhere in the statute is more than a mere regulatory gap filler. It is CARB's attempt to arrogate power to itself. "An administrative agency must act within

the powers conferred upon it by law and may not act in excess of those powers." *Am. Fed'n of Labor and Congress of Indus. Org. v. Unemployment Ins. Appeals Bd.*, 13 Cal. 4th 1017, 1042 (1996).

Where a statute does not expressly grant a power to an administrative agency, it is sometimes necessary to construe the statute to imply such a power, but a long line of California cases, including cases decided by this Court, holds that implied powers must be narrowly construed, and powers will not be implied unless essential to effectuate the statutory purpose. *See Cox v. Kern Cnty. Civil Serv. Comm'n*, 156 Cal. App. 3d. 867, 873 (1984) ("[C]ourt would still look to Ordinance No. A-126 to determine whether the power to adopt such a rule was indispensable to effectuation of the objects and purposes of the civil service system."). *See also, Water Quality Ass'n v. Cnty. of Santa Barbara*, 44 Cal. App. 4th 732, 746 (1996) ("The only implied powers . . . are those essential to the limited declared powers provided by its enabling statute."); *Addison v. Dep't of Motor Vehicles*, 69 Cal. App. 3d. 486, 498 (1977) (implied power must be "indispensable").

CARB has acknowledged that the sale of emissions allowances is not essential to its implementation of A.B. 32 or to the Cap and Trade Regulations, and that allowances could just as well be "distributed free of charge." *See* CARB's *Final Statement of Reasons for Rulemaking, California Cap-and-Trade Program* (Oct. 2011), at 732 (JA0812) and 2190 (JA0813-JA0814).

Accordingly, because sale of emissions allowances is neither essential to the purposes of A.B. 32, nor is it indispensable to CARB's implementation of A.B. 32 or to the Cap and Trade Regulations, such a statutory power should not be implied.

When all is said and done, there is a conspicuous omission in A.B. 32: The statute is utterly silent regarding what, if anything, CARB could do with any revenues collected from the auction of emissions allowances. If the Legislature had contemplated that there would be an auction of allowances, surely it would have provided CARB with at least some direction as to how the funds from any such auction would be used, or at least how the funds would be stored for safekeeping before a use was found for them. But there is no such legislative direction in A.B. 32, further evidencing that the statute did not contemplate the auction scheme established by CARB's Cap and Trade Regulation.

3. The Trial Court Erred When It Held That The Auction Provisions Are Authorized Under A.B. 32

Without addressing the important details discussed in Sections II.A.1, and II.A.2, the lower court held that because the "design" of a cap-and-trade program requires choices concerning how to "distribute" allowances, CARB is necessarily authorized to sell emissions allowances at auction. Opinion at 9-10 (JA1603-1604). But neither A.B. 32 nor the Cap and Trade Regulation define "distribution" or "design" or any variants thereof. Nevertheless, the

lower court insisted that the use of the term "distribution" authorizes CARB to auction emission allowances.

The holding is at odds with precedent established in this Court. For example, in *Miller Brewing Co. v. Dep't of Alcoholic Beverage Control*, 204 Cal. App. 3d. 5, 1213 (1988), this Court stated:

> [T]he wide spectrum of accepted definitions of the term "distribution" . . . gives rise to ambiguity . . . . [To resolve ambiguity a court must] discern legislative intent [and] examine the legislative history and the statutory context of the act under scrutiny. . ..
>
> Furthermore, we are not bound to the Department's construction . . . . [N]o deference to an administrative interpretation of [a statute] is required [if] the meaning of the applicable statutory language and its legislative history is accessible.

Id. at 12-13. Moreover, the California Supreme Court addressed the meaning of the statutory term "distribution," found the meaning unclear, and consulted the "legislative history of the statute and the wider historical circumstances of its enactment." *California Mfrs. Ass'n v. Public Utilities Comm'n*, 24 Cal. 3d. 836, 844 (1979). For a discussion of A.B. 32's legislative history, *see* Section II.B, *infra.*

Next, the lower court offers a statement by the California Climate Action Team to support its finding that the Legislature understood the phrase "distribution of emissions allowances" to encompass both giving away allowances and selling them at auction. (JA1604). The self-serving statement made by the California Climate Action Team, which has responsibility for

implementing parts of A.B. 32 and other California greenhouse gas initiatives, provides no insight into legislative intent. The court could have submitted with equal probity a statement from CARB itself, opining that A.B. 32 authorizes auctions. *Ass'n for Retarded Citizens v. Dep't of Developmental Services*, 38 Cal. 3d. 384, 391 (1985) (self serving statements of administrative agency regarding its scope of authority are neither authoritative nor persuasive).

The lower court also observed that "if the Legislature had meant to exclude the sale of allowances, it would have said so. It did not." (JA1604). But that turns the law on its head. An administrative agency may only do that which it is authorized to do by statute. Cal. Gov't Code § 11342.1-2 (regulations must "be within the scope of authority conferred"); *Martinez v. Combs*, 49 Cal. 4th 35, 61 (2010) (agencies can do only what statutes authorize); *O'Grady v. Superior Court*, 139 Cal. App. 4th 1423, 1443 (2006) (a statute "is presumed to exclude things not mentioned"). It would be a startling proposition if CARB could do *anything* not explicitly prohibited by A.B. 32. *Dean*, 62 Cal. App. 4th at 641-42 (statute's silence does not constitute authorization).

The lower court goes on to observe that the Legislature was aware of the Cap and Trade program in the federal Clean Air Act, which authorizes auctions, concluding erroneously that the Legislature must have intended to

authorize any and all auctions in A.B. 32, even the budget-busting multi-billion dollar scheme before this Court. Yet contrasting the lack of any provision in A.B. 32 for auctions against the detailed auction provisions of the Clean Air Act underlines the fact that A.B. 32 does not include or authorize even the most basic elements of an auction found in the Clean Air Act. Title IV of the federal Clean Air Act governs the emission of sulfur oxides ("SOx"), and authorizes a maximum of 1% of the total allowable emissions to be set aside for auction. Even for that small percentage, the Clean Air Act provides explicit and detailed directions to the United States Environmental Protection Agency ("EPA") regarding how auctions must be conducted, by whom, when, and how auction revenues must be handled. *See* 42 U.S.C. § 7651o. Notwithstanding the availability of this federal model, the California Legislature did not even use the term "auction" in the statute, let alone define its parameters. The fact that the California Legislature was aware of the Clean Air Act's detailed provisions and, therefore, knew how auctions could be explicitly authorized, supports the conclusion that the Legislature did not intend for CARB to auction emissions allowances via the massive revenue-generating scheme that is before this Court.

The lower court opines further that an expansive reading of section 38562(b)(1) is appropriate because A.B. 32 generally provides broad delegation to CARB to implement the overall regulatory program without

detailed legislative guidance or constraint. That is not true. A.B. 32 requires CARB to take specific steps to implement the legislative goal of reaching 1990 emissions levels by 2020. For example, section 38562(b) requires CARB to do the following to achieve "the statewide greenhouse gas emissions limit:" (1) provide due credit to those who have made early voluntary emissions reductions, (2) make actions under A.B. 32 consistent with ambient air quality standards and toxic contaminant emissions requirements, (3) minimize the administrative burden of implementing and complying with the regulations, (4) minimize "leakage" (i.e., the flight of Covered Entities out of California resulting from the regulations), and (5) consider regulatory cost effectiveness, societal benefits, and "other benefits to the economy, environment, and public health." *Id.* And A.B. 32 has a smorgasbord of other specific requirements with which CARB must comply in designing the regulations, including, e.g., (1) "rely on the best available economic and scientific information . . . when adopting the regulations," Health & Safety Code § 38562(e); (2) achieve "real, permanent, quantifiable, and enforceable" emissions reductions, section 38562(d)(1); and (3) "consult with other states and the federal government, and other nations to identify the most effective strategies and methods to reduce greenhouse gases . . .." Section 38564. A.B. 32 also gives specific direction to CARB in connection with CARB's development of "market-based compliance mechanisms," including, e.g., (1) "prevent any increase in

emissions of toxic air contaminants and criteria pollutants," section 38570(b)(2); (2) "maximize additional environmental and economic benefits," section 38570(b)(3); and (3) "adopt regulations governing how market-based compliance mechanisms may be used *by regulated entities subject to greenhouse gas emission limits . . .* to achieve compliance with *their* greenhouse gas emissions limits." Section 38570c (emphasis added). The latter provision is especially informative, since it shows that the Legislature authorized CARB to develop "market-based compliance mechanisms" specifically so that "regulated entities" could "achieve compliance with their greenhouse gas emissions limits," and not so that CARB could generate billions for the state.

Given these explicit, specific, and detailed legislative directives, it would be odd indeed if the Legislature intended to authorize CARB's scheme of auctions by silence. It did not, as evidenced by the legislative history.

C. The Legislative History Makes Clear That The Legislature Did Not Intend To Authorize an Auction When It Enacted A.B. 32

1. The Legislative Floor Debate on A.B. 32 Shows a Legislative Intent for CARB *Not* To Sell Emissions Allowances

The Assembly floor debate on the enacted version of A.B. 32 occurred on August 31, 2006.[4] *See* DVD of Legislative Floor Debate on A.B. 32 (JA08340; *See also,* Francois Decl. ¶¶ 3, 4-5 (JA0834). During that debate, Assemblymember Fabian Nunez, the author of A.B. 32 and the then-Speaker of the Assembly, responded to claims made by opposing Assemblymembers that A.B. 32 constituted a tax that was being levied in California. Francois Decl. ¶ 11 (JA0835). For example, Assemblymember George A. Plescia said

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[4] DVD (JA0814) obtained on June 3, 2013, by Anthony L. Francois from the Office of Assembly Television. Mr. Francois' declaration setting forth the authenticity of the DVD, as well as the chain-of-custody, was filed in the lower court. Francois Decl. ¶¶ 4-8. (JA-0833-08356). All references to the Assembly Floor Debate are to the time stamps on the DVD (JA0814), a hard copy of which has been submitted to this Court as part of the hard copy of the JA. The time stamps reflect when the floor statements were made during the legislative debate leading to the vote on A.B. 32. The DVD can be played on a computer running the Windows operating system using the Windows Media Player. The DVD should automatically play. If it does not, please follow the following instructions. In Windows Media Player, click on the "Exit Full-Screen Mode" icon located on the lower right hand side of the window. A smaller window will appear on the screen. Then, click on the "Switch to Library" icon located in the upper right hand side of the window. In the window that appears next, make sure that the "Play" tab is activated. Then, double-click on the "Title 1" link located near the middle of the right-hand panel of that window. At that point the DVD should be fully functional and begin playing. Francois Decl. ¶ 8. Specific time stamps on the DVD can be accessed using Windows Media Player by dragging the progress bar to the time stamp desired. *Id.* The first 35 minutes and 20 seconds of Exhibit F do not relate to A.B. 32 but were included in the DVD as received by Mr. Francois from the Office of Assembly Television. Francois Decl. ¶ 9.

that A.B. 32 provides "an open checkbook for the air resources board." DVD at 1:38:03-06. (JA0814) He went on to say that anyone voting for A.B. 32 would be voting to make CARB "the largest taxing agency since the Board of Equalization." *Id.*, DVD at 1:38:06-14. He went on to assert: "If you vote for this, you're voting for an SUV tax." *Id.*, DVD at 1:38:37-45. Finally, he stated: "You're going to be voting for a cow tax with methane gas." *Id.*, DVD at 1:38:45-49.

In response to these and similar statements by others, Speaker Nunez stated on the floor, immediately before the vote, that the intent of A.B. 32 is to provide funds "for program administration and costs only." *Id.*, DVD at 1:45:13-19. He immediately went on to say, "I'll give you my word today that next year I'll introduce a bill if necessary to make sure that happens in order that I get your support on this bill." *Id.*, DVD at 1:45:20-34. Thus, the author of the bill urged the Assembly to vote in favor of passage specifically based upon his representation that the only funds A.B. 32 would generate are those for "program administration and costs." Sadly, the promise to introduce a bill "to make sure that happens" was never fulfilled. As stated by the California Supreme Court, "[d]ebates surrounding the enactment of a bill may illuminate its interpretation." *In Re Marriage of Bouquet*, 16 Cal. 3d. 583, 590 (1976).

Further, on the very day of the vote on A.B. 32, Speaker Nunez sent to the Legislature a "Letter of Legislative Intent," in which he confirmed that

"any funds provided by Health and Safety Code section 38597, are to be used solely for the direct costs incurred in administering [A.B. 32]." (JA0815). Indeed, Speaker Nunez referred directly to that letter on the floor immediately before the vote, as part of his effort to encourage the Legislature to enact the bill. DVD 1:45:18-22 (JA0814). *See* 16 Cal. 3d. at 590 ("letter of legislative intent" of Assemblyman Hayes commands respect on the issue of the Legislature's intent "through the light it sheds upon" the meaning of the bill as passed).

The lower court observes that the "Legislative Letter of Intent" submitted by the author of A.B. 32 is not dispositive. But the court ignored the floor debate in the Assembly that generated the letter. Petitioners submitted to the lower court a DVD containing the entire Assembly debate on A.B. 32, showing in detail the Assembly proceedings, yet the court did not mention the debate or the DVD in its opinion. "Debates surrounding the enactment of a bill may illuminate its interpretation." 16 Cal. 3d at 590.

2. A Legislative Effort in 2009 To Amend A.B. 32 To Authorize the Use of Auctions Died on the Floor of the Senate

After the enactment of A.B. 32, Senator Pavley introduced legislation, known as S.B. 31, that would have authorized CARB to conduct auctions. S.B. 31 never left the Senate, which was the house of origin, and died on the floor. (JA-0665). Thus, the Legislature had the opportunity in 2009, before

CARB's promulgation of the Cap and Trade Regulation, to authorize auctions but did not avail itself of that opportunity, further showing that the Legislature did not intend to authorize them. *See Seibert v. Sears Roebuck & Co.*, 45 Cal. App. 3d. 1, 19 (1975) (Legislature's failure to enact an amendment may shed light on legislative intent of prior enactment when the "full context of circumstances" is considered.).

Ignoring *Seibert*, the lower court observed that the Legislature's failure to enact S.B. 31 has "little value." (JA1604). Instead, it cited *Apple Inc., v. Superior Court*, 56 Cal. 4th 128, 146 (2013), which is inapposite. In *Apple*, the issue was whether failed legislation intended to *remove* authorization to act indicated that the existing statute contained such authorization. The Court stated that "the Legislature may have concluded that it was unnecessary to remove online transactions from the statute's coverage because such transactions were never covered by the statute in the first place." *Id.* That is the *opposite* of the situation here, where the issue is whether the 2009 failed legislation, which sought to *authorize* the auctions three years after the enactment of A.B. 32, evidences legislative intent *not* to authorize them. In any event, given the *Seibert* decision, failure to enact legislation authorizing the auctions is certainly relevant to the issue of legislative intent and should not have been given such short shrift by the lower court.

D. Because the Auctions Are Not Authorized by A.B. 32, CARB's Cap and Trade Regulation Is Ultra Vires Thereunder

The authority to sell carbon emissions credits at auction to generate billions of dollars of revenues for the state is a stunning power for an administrative agency to arrogate to itself. Taken together, the evidence provides overwhelming support for the conclusion that the Legislature did not intend to grant this kind of auction authority to CARB in A.B. 32. *Lungren*, 45 Cal. 3d. at 733-43 (all relevant evidence should be used to interpret a statutory provision). *See McGlothlen v. Dep't of Motor Vehicles*, 71 Cal. App. 3d. 1005, 1015 (1977) (courts may consider any appropriate material in construing statutes, including, legislative history, materials that contain economic, political or social facts, findings or opinions, and other relevant "extrinsic aides"). *See also, Seibert v. Sears Roebuck & Co.*, 45 Cal App. 3d. at 19 (appropriate to review "full context of circumstances" of legislative action or inaction to determine legislative intent).

In light of all of the circumstances, CARB's establishment of an auction system generating billions of dollars in revenues for the state as part of the Cap and Trade Regulation is an ultra vires act. *Dep't of Alcoholic Beverage Control v. Alcoholic Beverage Control Appeals Bd.*, 100 Cal. App. 4th 1066, 1072 (2002) ("[T]he discretion exercised by [an administrative agency] is not absolute but must be exercised in accordance with the law."). As such, the

auction provisions of the Cap and Trade Regulation are void. *Water Replenishment Dist. of Southern Cal. v. City of Cerritos*, 202 Cal. App. 4th 1063, 1072 (2012) ("conduct by an agency lacking authority to engage in that conduct is void"); *Turlock Irrigation Dist. v. Hetrick*, 71 Cal. App. 4th 948, 951 (1991) (irrigation district's attempt to provide natural gas service was held ultra vires and void because the statutes governing the district did not authorize the district to provide such service). Such a statutory construction is consistent with the principals of constitutional avoidance. *Harrot*, 25 Cal 4th at 1138, 1153.

Significantly, in the event the language of A.B. 32 is construed to provide CARB with authority to conduct the auctions as promulgated in the Cap and Trade Regulation, both the auction provisions of the regulation *and* A.B. 32 itself are unconstitutional under California Constitution, Article XIII A, Section 3 (Proposition 13), for the reasons set forth in Section I, *supra*.

III

STATUTES ENACTED AFTER A.B. 32 CANNOT BE INTERPRETED TO AUTHORIZE CARB TO RAISE REVENUE AT AUCTION, WITHOUT VIOLATING PROPOSITION 26

On November 2, 2010, California voters approved Proposition 26, the Supermajority Vote to Pass New Taxes and Fees Act, which in relevant part amended the provisions of Proposition 13 that were designated as Article XIII

A, Section 3, of the California Constitution. Proposition 26 applies to legislation enacted after November 3, 2010. Cal Const. art. XIII A, § 3.

In passing Proposition 26, the people of the State of California declared that (1) taxes continue to rise notwithstanding requirements of Proposition 13, because new statutory levies on taxpayers have been "disguised" as regulatory fees, and (2) this poses an unreasonable burden on the taxpayers of California, requiring that the supermajority vote mandate of Proposition 13 be made more effective. Voter Information Guide, Gen. Elec. (Nov. 2, 2010) text of Prop. 26, §§ 1(a), (c), (e), (f) at p. 114.

In relevant part, Proposition 26 amended Section 3 of Article XIII A of the California Constitution to define the term "tax" as "*any* levy, charge, or exaction of *any kind* imposed by the State." Cal. Const., art. XIII A § 3(b). (Emphasis added). Moreover, Proposition 26 established that

> [t]he *State bears the burden of proving by a preponderance of the evidence* that a levy, charge, or other exaction is not a tax, that the amount is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor's burdens on, or benefits received from, the governmental activity.

Cal. Const., art. XIII A, section 3(d). (Emphasis added.)

It is undisputed that none of the relevant statutes enacted in 2012 was passed by a supermajority vote. Those enactments purport to allocate certain revenues generated at the auctions. But if any of the 2012 enactments, either

individually or collectively, are needed to provide CARB with authority after-the-fact to generate revenues at auction from the sale of emissions allowances, they run afoul of Proposition 26 because they constitute "change[s] in state statute[s] which result[] in . . . a higher tax." Cal. Const. art. XIII A § 3(b). Accordingly, if the auctions were ultra vires before the 2012 enactments, those enactments fail to authorize the *generation* of auction revenue unless at least one of Proposition 26's seven specific exceptions applies. But none of the exceptions applies to any of the statutes.

S.B. 1018 provides that "loans" of moneys in the "Greenhouse Gas Reduction Fund" may be made to the "General Fund" "for cash flow" purposes. There is no "cash flow" exception in Proposition 26. To the extent that auctions were not authorized before S.B. 1018 was enacted, and to the extent S.B. 1018 purports to authorize the auctions after-the-fact, it constitutes the enactment of a "higher tax" without a supermajority vote. Accordingly, S.B. 1018 is void as unconstitutional under Proposition 26.

Next, A.B. 1532 directs California's Finance Department to develop a three-year Investment Plan to use the funds to reduce greenhouse gas emissions. Investments would target areas such as clean energy, low carbon transportation and infrastructure, natural resource protection, and research and development. On May 14, 2013, California issued a first installment of the Investment Plan. The Investment Plan identifies and prioritizes "[s]tate

investments to help achieve greenhouse gas reduction goals," but does not provide cost estimates of *actual* services or regulatory activity to be funded by auction revenues, which depend entirely on future actions that may or may not be taken by the Legislature. JA0736 ("Inclusion of a recommended investment in this plan does not guarantee funding."). In fact, A.B. 1532 does not come close to authorizing CARB to conduct its auctions. But if it is interpreted to do so, not one of the seven exceptions to Proposition 26 applies, as there is no exception for projects recommended to the Legislature by the Director of Finance. Accordingly, if A.B. 1532 is construed to authorize CARB's auction provisions after-the-fact, the enactment is void under Proposition 26.

In turn, S.B. 535 mandates 25% and 10% set-asides for "disadvantaged areas." It also does not meet any of the exceptions in Proposition 26, as there is no exception for "disadvantaged areas." Accordingly, to the extent S.B. 535 is required to authorize otherwise ultra vires auctions, it too constitutes the enactment of illegal taxes void under Proposition 26.

A.B. 1464 provides that the Director of Finance may allocate or otherwise use an amount of "at least" $500 million from moneys derived from the sale of greenhouse gas emission allowances. 2012 Stats., Ch. 21, § 15.11(a). If auctions were not authorized by A.B. 32, then A.B. 1464 could not be used to support CARB's authority to sell emissions allowances at auction without running afoul of Proposition 26 because there is no exception

set forth in Proposition 26 that could apply to the authorization to the Director of Finance to confiscate "at least" $500 million from the Greenhouse Gas Reduction Fund and make corresponding adjustments to the General Fund. Accordingly, to the extent A.B. 1464 is required to authorize CARB's auctions, it and the auctions are unconstitutional under Proposition 26.

The 2014 legislation fares no better, because neither S.B. 852 nor S.B. 862 passed by a two-thirds supermajority vote in both houses, and there is no exception in Proposition 26 for funding the designated projects, such as high-speed rail and affordable housing. *See* Ex. 1 hereof (vote tallies); *See also,* Statement of Facts, *supra.*

CONCLUSION

For the foregoing reasons, Petitioners respectfully request that (1) a writ of mandate issue from this Court, enjoining Respondents from conducting further auctions of greenhouse gas emissions allowances pursuant to 17 C.C.R. §§ 95830-95834, 95870, and 95910-95914, and that (2) the Court declare that 17 C.C.R. §§ 95830-95834, 95870, and 95910-95914, violate California Constitution, Article XIII A, Section 3, Proposition 13 or Proposition 26 or, in the alternative, are ultra vires under A.B. 32.

DATED: October 17, 2014.

Respectfully submitted,

JAMES S. BURLING
THEODORE HADZI-ANTICH
HAROLD E. JOHNSON

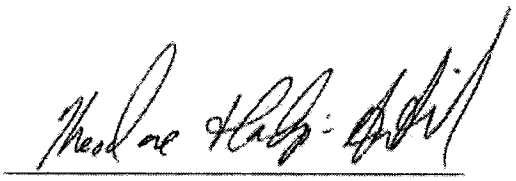
By _____
THEODORE HADZI-ANTICH

Attorneys for Petitioners-Appellants
Morning Star Packing Co., et al.

CERTIFICATE OF COMPLIANCE

Pursuant to California Rule of Court 8.204(c)(1), I hereby certify that the foregoing APPELLANTS' OPENING BRIEF is proportionately spaced, has a typeface of 13 points or more, and contains 12,762 words.

DATED: October 17, 2014.



THEODORE HADZI-ANTICH

EXHIBIT - 1

UNOFFICIAL BALLOT

MEASURE: SB 852
AUTHOR: Leno
TOPIC: Budget Act of 2014.
DATE: 06/15/2014
LOCATION: ASM. FLOOR
MOTION: SB 852 Leno Conference Report By SKINNER
(AYES 55. NOES 24.) (PASS)

AYES
****

Alejo	Ammiano	Bloom	Bocanegra	
Bonilla	Bonta	Bradford	Brown	
Buchanan	Ian Calderon		Campos	Chau
Chesbro	Cooley	Dababneh	Daly	
Dickinson	Eggman	Fong	Fox	
Frazier	Garcia	Gatto	Gomez	
Gonzalez	Gordon	Gray	Hall	
Roger Hernández	Holden	Jones-Sawyer		Levine
Lowenthal	Medina	Mullin	Muratsuchi	
Nazarian	Pan	Perea	John A. Pérez	
V. Manuel Pérez	Quirk	Quirk-Silva		Rendon
Ridley-Thomas	Rodriguez		Salas	Skinner
Stone	Ting	Weber	Wieckowski	
Williams	Yamada	Atkins		

NOES
****

Achadjian	Allen	Bigelow	Chávez	
Conway	Dahle	Donnelly	Beth Gaines	
Gorell	Grove	Hagman	Harkey	
Jones	Linder	Logue	Maienschein	
Mansoor	Melendez	Nestande		Olsen
Patterson	Wagner	Waldron	Wilk	

ABSENT, ABSTAINING, OR NOT VOTING
****

Vacancy

UNOFFICIAL BALLOT

MEASURE: SB 852
AUTHOR: Leno
TOPIC: Budget Act of 2014.
DATE: 06/15/2014
LOCATION: SEN. FLOOR
MOTION: Conference Reports SB852 Leno
(AYES 25. NOES 11.) (PASS)

AYES
****

Beall	Block	Cannella		Corbett
Correa	De León	Evans	Galgiani	
Hancock	Hernandez		Hill	Hueso
Jackson	Lara	Leno	Lieu	
Liu	Mitchell		Monning	Padilla
Pavley	Roth	Steinberg		Torres
Wolk				

NOES
****

Anderson		Berryhill	Fuller	Gaines
Huff	Knight	Morrell	Nielsen	
Vidak	Walters	Wyland		

NO VOTE RECORDED
****

Calderon	DeSaulnier	Wright	Yee

UNOFFICIAL BALLOT

MEASURE: SB 862
AUTHOR: Committee on Budget and Fiscal Review
TOPIC: Greenhouse gases: emissions reduction.
DATE: 06/15/2014
LOCATION: ASM. FLOOR
MOTION: SB 862 B.& F. R. Senate Third Reading By SKINNER
(AYES 53. NOES 26.) (PASS)

AYES
****

Alejo Ammiano Bloom Bocanegra
Bonilla Bonta Bradford Brown
Buchanan Ian Calderon Campos Chau
Chesbro Dababneh Daly Dickinson
Eggman Fong Fox Frazier
Garcia Gatto Gomez Gonzalez
Gordon Gray Hall Roger Hernández
Holden Jones-Sawyer Levine Lowenthal
Medina Mullin Muratsuchi Nazarian
Pan Perea John A. Pérez V. Manuel Pérez
Quirk Quirk-Silva Rendon Ridley-Thomas
Rodriguez Skinner Stone Ting
Weber Wieckowski Williams Yamada
Atkins

NOES
****

Achadjian Allen Bigelow Chávez
Conway Cooley Dahle Donnelly
Beth Gaines Gorell Grove Hagman
Harkey Jones Linder Logue
Maienschein Mansoor Melendez Nestande
Olsen Patterson Salas Wagner
Waldron Wilk

ABSENT, ABSTAINING, OR NOT VOTING
****

Vacancy

UNOFFICIAL BALLOT

MEASURE: SB 862
AUTHOR: Committee on Budget and Fiscal Review
TOPIC: Greenhouse gases: emissions reduction.
DATE: 06/15/2014
LOCATION: SEN. FLOOR
MOTION: Unfinished Supp 1 SB862 Committee on B. & F.R. (Leno) Concurrence
(AYES 22. NOES 12.) (PASS)

AYES
****

Beall	Block	Corbett	Correa	
De León	Evans	Galgiani		Hancock
Hernandez		Hill	Hueso	Jackson
Lara	Leno	Lieu	Liu	
Mitchell		Monning	Padilla	Steinberg
Torres	Wolk			

NOES
****

Anderson		Berryhill	DeSaulnier	Fuller
Gaines	Huff	Knight	Morrell	
Nielsen	Vidak	Walters	Wyland	

NO VOTE RECORDED
****

Calderon		Cannella	Pavley	Roth
Wright	Yee			

DECLARATION OF SERVICE

I, Pamela Spring, declare as follows:

I am a resident of the State of California, residing or employed in Sacramento, California. I am over the age of 18 years and am not a party to the above-entitled action. My business address is 930 G Street, Sacramento, California 95814.

On October 17, 2014, true copies of APPELLANTS' OPENING BRIEF were placed in envelopes addressed to:

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which envelopes, with postage thereon fully prepaid, were then sealed and deposited in a mailbox regularly maintained by the United States Postal Service in Sacramento, California.

I declare under penalty of perjury that the foregoing is true and correct and that this declaration was executed this 17th day of October, 2014, at Sacramento, California.

PAMELA SPRING

EXHIBIT C

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Attorneys for Plaintiffs

IN THE UNITED STATES DISTRICT COURT

FOR THE EASTERN DISTRICT OF CALIFORNIA

FRESNO BRANCH COURTHOUSE

BARRY BAUER, STEPHEN WARKENTIN, NICOLE FERRY, JEFFREY HACKER, NATIONAL RIFLE ASSOCIATION OF AMERICA, INC., CRPA FOUNDATION, HERB BAUER SPORTING GOODS, INC. Plaintiffs vs. KAMALA HARRIS, in Her Official Capacity as Attorney General For the State of California; STEPHEN LINDLEY, in His Official Capacity as Acting Chief for the California Department of Justice, and DOES 1-10. Defendants.	CASE NO. 1:11-cv-01440-LJO-MJS **SECOND AMENDED COMPLAINT FOR DECLARATORY AND INJUNCTIVE RELIEF** **42 U.S.C. sections 1983, 1988**

PLAINTIFFS, by and through their undersigned attorneys, bring this Complaint for Declaratory and Injunctive Relief against the above-named Defendants, their employees, agents, and successors in office (collectively "DEFENDANTS"), and in support thereof allege the following:

INTRODUCTION

1. This case involves an important constitutional principle, that while the government may impose fees on individuals seeking to engage in certain constitutionally protected activities, the monies generated by such fees cannot be used to finance state activities not reasonably related to regulating the fee payer's impact on the state.

2. Vindication of this principle requires that DEFENDANTS be enjoined from using monies generated by a fee, payment of which is required to obtain a firearm in California, for the purpose of funding general law enforcement activities associated with the California Department of Justices' ("DOJ") Armed Prohibited Persons System ("APPS")program. For, such activities share no reasonable nexus with regulating lawful firearm purchases and, thus, forcing fee payers like PLAINTIFFS to subsidize them is an unlawful infringement on the Second Amendment right to lawfully obtain a firearm.

3. When a person wishes to obtain a firearm in California, state law generally requires the person to obtain the firearm through a federally licensed California firearm vendor (commonly known as an "FFL").

4. In doing so, the would-be purchaser[1] must, among other things, fill out a Dealer's Record of Sale form ("DROS"), the information from which is used by DEFENDANTS[2] to conduct a background check and confirm the would-be purchaser may lawfully receive firearms before he or she can take possession of any firearm. In the case of a handgun, the information is also used to register the

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[1] These fees apply even if a firearm is not being purchased but gifted or traded as well. But for simplicity sake "purchase" will be used throughout this Complaint to include all such activities unless specifically stated otherwise.

[2] DEFENDANTS are being sued in their official capacity as heads of the California Department of Justice, which entity is authorized by the Legislature to expend the monies at issue in this action.

handgun to the purchaser in DEFENDANTS' Automated Firearm System ("AFS").

5. DEFENDANTS have statutory discretion to charge firearm purchasers a mandatory fee for processing each DROS for every firearm transaction (a "DROS Fee"), which is collected from the firearm recipient through the FFL at the time of initiating the firearm's transfer.

6. The monies that are collected by DEFENDANTS from the DROS Fee are placed in a special account separate from the general fund, from which the Legislature may appropriate monies to the DEFENDANTS for statutorily prescribed purposes.

7. Originally, monies from the DROS Fee were intended to cover only DOJ's costs of processing a DROS, conducting a background check, and, in the case of a handgun, registration. But the activities for which DROS Fee funds are used have been ever-expanding for years, going far beyond funding these basic regulatory functions of the DOJ.

8. PLAINTIFFS bring this suit to challenge the constitutionality of DEFENDANTS' use of the revenues generated from the DROS Fee for general law enforcement activities which have no relation to fee payers; specifically, activities associated with the DOJ's Armed Prohibited Persons System program provided for by California Penal Code section 28225(b)(11) [12076(e)(10)].[3]

9. That section was recently amended to add mere *possession* of firearms to the list of activities for which DEFENDANTS could use DROS Fee revenues,[4]

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[3] Pursuant to the Legislature's enactment of Assembly Concurrent Resolution 73 (McCarthy) 2006, which authorized a Non-Substantive Reorganization of California's Deadly Weapons Statutes, various California Penal Code sections were renumbered, effective January 1, 2012. For convenience and ease of reference, the corresponding previous code section for each referenced Penal Code section is provided in brackets.

[4] See S.B. 819, 2011 Reg. Sess. (Ca. 2011).

thereby allowing the State to force *lawful* firearm *purchasers* to finance any law enforcement operation concerning *unlawful* firearm *possession*. And that it has done.

10. Governor Brown recently signed into law Senate Bill 140 ("SB 140"), appropriating $25 million dollars of the DROS Special Account's surplus – a surplus that was not supposed to exist in the first place[5] – solely to fund activities associated with the APPS program, which seeks to investigate individuals suspected of possessing firearms unlawfully and to remove the firearms from their possession.

11. Law-abiding firearm purchasers like PLAINTIFFS are thus not just being required to internalize the full social costs of their choice to exercise their fundamental Second Amendment rights, but also those costs of choices *made by others* to *criminally* use firearms – much as if, for instance, those exercising their fundamental right to marry were forced to fund enforcement of domestic violence restraining orders with their marriage license fees because some spouses become subject to one, or, as if the license fees from those who exercise their fundamental right to assemble in a public forum were taken to fund counter-gang measures

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[5] California law requires that the DROS fee "shall be no more than is necessary to fund" certain activities provided by statute (Penal Code section 28225(b)(1)-(11) [12076(e)(1)-(10)]), and constitutional principles prohibit excessive fees on constitutionally protected conduct. *Murdock v. Pennsylvania*, 319 U.S. 105, 112-14 (1943). Arguably, the large surplus, here, is evidence suggesting the current DROS fee is excessive, in violation of state and federal law. Plaintiffs in this case, however, do not ask the Court to resolve that argument. The passage of SB140 has made the *expenditure* of the existing $25 million dollar surplus the more immediate concern. Moreover, whether the DROS fee is excessive depends, in part, on first determining what activities may be considered to fall within the scope of the DROS program and thus properly funded thereby. This case seeks a declaration that SB140 improperly authorizes expenditures on APPS activities that do *not* fall within that scope, along with injunctive relief preventing such expenditures.

simply because they relate to gatherings of people, or, as if those who exercise their fundamental right to vote were forced to fund voter fraud enforcement actions via a poll tax.

12. Because DEFENDANTS' use of DROS Fee revenues on purposes unrelated to the fee payer affects constitutionally protected activity, irreparable harm is presumed. Accordingly, PLAINTIFFS seek from this Court a declaration that DEFENDANTS' use of revenues generated from the DROS Fee to fund general law enforcement activities associated with the DOJ's APPS program is unconstitutional, because the criminal misuse of firearms is not sufficiently related to the fee payers' activities, i.e., lawful firearm transactions. And, as such, an injunction prohibiting DEFENDANTS from using those revenues on such activities should issue.

JURISDICTION and VENUE

13. Jurisdiction of this action is founded on 28 U.S.C. §§ 1331 and 1343, in that this action arises under the Constitution and laws of the United States, and under 28 U.S.C. § 1343(a)(3) and 42 U.S.C. § 1983, in that this action seeks to redress the deprivation, under color of the laws, statutes, ordinances, regulations, customs, and usages of the State of California and political subdivisions thereof, of rights, privileges, or immunities secured by the United States Constitution and by Acts of Congress.

14. PLAINTIFFS' claims for declaratory and injunctive relief are authorized by 28 U.S.C. §§ 2201 and 2202.

15. Venue in this judicial district is proper under 28 U.S.C. § 1391(b)(2) because a substantial part of the events or omissions giving rise to the claims occurred in this district.

PARTIES

I. Plaintiffs

16. Plaintiff BARRY BAUER is a resident, property owner, and taxpayer of

Fresno, California. Within the last five years, Plaintiff BAUER has lawfully purchased firearms from an FFL, for which he has had to pay the DROS Fee. Plaintiff BAUER intends to continue to purchase firearms through an FFL in the future.

17. Plaintiffs STEPHEN WARKENTIN and JEFFREY HACKER are residents, property owners, and taxpayers of Fresno, California. Within the last five years, each has purchased multiple firearms from both an FFL and a private party, through an FFL as required by California Penal Code § 26500 [12070]. Plaintiffs WARKENTIN and HACKER intend to continue their pattern of regularly purchasing firearms through an FFL in the future.

18. For each of their transactions, Plaintiffs WARKENTIN and HACKER have paid the DROS Fee. Plaintiffs WARKENTIN and HACKER have had to pay the DROS Fee multiple times in the same year, and, in some cases, the same month.

19. Plaintiff NICOLE FERRY is a resident of Fresno, California. Within the last five years, Plaintiff FERRY has purchased handguns from an FFL for self-defense and target practice. For each of her transactions, Plaintiff FERRY has paid the DROS Fee. Plaintiff FERRY intends to purchase firearms through an FFL in the future.

20. Plaintiff NATIONAL RIFLE ASSOCIATION OF AMERICA, INC. (hereafter "NRA") is a non-profit entity classified under section 501(c)(3) of the Internal Revenue Code and incorporated under the laws of New York, with its principal place of business in Fairfax, Virginia. NRA has a membership of approximately 4 million persons. The purposes of NRA include protection of the right of law-abiding citizens to keep and bear firearms for the lawful defense of their families, persons, and property, and from unlawful government regulations and preconditions placed on the exercise of that right. NRA spends its resources on each of those activities. NRA brings this action on behalf of itself and its hundreds

of thousands of members in California, including Plaintiffs BAUER, WARKENTIN, and HACKER, who have been, are being, and will in the future be subjected to DEFENDANTS' imposition of the DROS Fee.

21. Plaintiff CRPA FOUNDATION is a non-profit entity classified under section 501(c)(3) of the Internal Revenue Code and incorporated under California law, with headquarters in Fullerton, California. Contributions to the CRPA FOUNDATION are used for the direct benefit of Californians. Funds contributed to and granted by CRPA FOUNDATION benefit a wide variety of constituencies throughout California, including gun collectors, hunters, target shooters, law enforcement, and those who choose to own a firearm to defend themselves and their families. The CRPA FOUNDATION spends its resources seeking to raise awareness about unconstitutional laws, defend and expand the legal recognition of the rights protected by the Second Amendment, promote firearms and hunting safety, protect hunting rights, enhance marksmanship skills of those participating in shooting sports, and educate the general public about firearms. The CRPA FOUNDATION supports law enforcement and various charitable, educational, scientific, and other firearms-related public interest activities that support and defend the Second Amendment rights of all law-abiding Americans.

22. In this suit, the CRPA FOUNDATION represents the interests of the many citizen and taxpayer members of its related association, the California Rifle and Pistol Association, who reside in California and who wish to sell or purchase firearms, or who have sold or purchased firearms, and have been charged the DROS Fee. These members are too numerous to conveniently bring this action individually. The CRPA FOUNDATION brings this action on behalf of itself and its tens of thousands of supporters in California, including Plaintiff BAUER, who have been, are being, and will in the future be subjected to the DROS Fee being used to fund unrelated activities.

23. Plaintiff HERB BAUER SPORTING GOODS, INC., is a California

corporation with its principal place of business in the County of Fresno, California. It is a licensed firearms dealer under both federal and California law (i.e., an FFL) that sells a variety of firearms. California law requires Plaintiff HERB BAUER to collect the DROS Fee for DOJ, at DOJ's direction, from firearm transferees. Accordingly, Plaintiff HERB BAUER is injured by its being forced to facilitate DEFENDANTS' unlawful use of revenues collected from the DROS Fee.

24. The individual PLAINTIFFS identified above are residents and taxpayers of California from the City and County of Fresno who have been required to pay the DROS Fee, Defendants' use of which violates PLAINTIFFS' constitutional rights.

25. Each of the associational PLAINTIFFS identified above either has individual members or supporters, or represents individual members of a related organization, who are citizens and taxpayers of California, including in Fresno County, who have an acute interest in purchasing firearms and do not wish to pay unlawful fees, taxes, or other costs associated with that purchase and thus have standing to seek declaratory and injunctive relief to halt or reduce the unconstitutional use of the monies collected from the DROS Fee. The interests of these members are germane to their respective associations' purposes; and neither the claims asserted nor the relief requested herein requires their members participate in this lawsuit individually.

II. Defendants

26. Defendant KAMALA HARRIS is the Attorney General of California. She is the chief law enforcement officer of California, and is charged by Article V, Section 13 of the California Constitution with the duty to inform the general public and to supervise and instruct local prosecutors and law enforcement agencies regarding the meaning of the laws of the State, including the DROS Fee, and to ensure the fair, uniform and consistent enforcement of those laws throughout the state. She is sued in her official capacity.

27. Defendant STEPHEN LINDLEY is the Acting Chief of the DOJ Bureau of Firearms and, as such, is responsible for executing, interpreting, and enforcing the laws of the State of California – as well as its customs, practices, and policies – at issue in this lawsuit. He is sued in his official capacity.

28. Defendants HARRIS and LINDLEY (collectively "DEFENDANTS") are responsible for administering and enforcing the DROS Fee, are in fact presently enforcing the DROS Fee against PLAINTIFFS, and will continue to enforce the DROS Fee against PLAINTIFFS.

29. DEFENDANTS also are responsible for spending monies appropriated to the DOJ by the Legislature from the DROS Special Account, and have been spending, are spending, and will continue to spend monies from the DROS Fee on the APPS program.

30. The true names or capacities, whether individual, corporate, associate or otherwise of the DEFENDANTS named herein as DOES 1-10, are presently unknown to PLAINTIFFS, who therefore sue said DEFENDANTS by such fictitious names. PLAINTIFFS pray for leave to amend this Complaint and Petition to show the true names, capacities, and/or liabilities of DOE Defendants if and when they have been determined.

OVERVIEW OF REGULATORY SCHEME

I. Constitutional Provisions and Controlling Law

31. The Second Amendment to the United States Constitution provides: "A well regulated militia, being necessary to the security of a free State, the right of the people to keep and bear arms, shall not be infringed." U.S. Const. amend. II.

32. The Second Amendment protects a fundamental, individual right to possess firearms for self-defense that is incorporated through the Due Process clause of the Fourteenth Amendment to restrict state and local governments from infringing on the right.

33. The right to keep and bear arms for self-defense implies a corresponding

right to acquire firearms.

34. The U.S. Supreme Court has made clear that government's authority to levy fees on the exercise of constitutional rights is limited. Such fees may only be imposed to defray the government's expenses incurred in regulating activities reasonably related to the fee payer.

II. The Dealer's Record of Sale (DROS) Fee Imposed on Firearm Transfers

35. California confers discretion on DOJ to impose various fees on firearm purchasers, which they must pay as a prerequisite to qualify for receiving a firearm. The only fee at issue in this case is the DROS Fee, the one associated with processing the Dealer's Record of Sale.

36. California Penal Code sections 28225(a)-(c) [formerly 12076(e)], 28230 [12076(f)], 28235 [12076(g)], and 28240(a)-(b) [12076(i)], establish the fees associated with a DROS, and govern what the funds collected therefrom can be used for.

37. Subdivision (a) of Penal Code section 28225 [12076(e)] provides:

> The [DOJ] may require the [FFL] to charge each firearm purchaser a fee not to exceed fourteen dollars ($14), except that the fee may be increased at a rate not to exceed any increase in the California Consumer Price Index as compiled and reported by the Department of Industrial Relations.

38. The DOJ promulgated California Code of Regulations, Title 11, section 4001, increasing the cap on the DROS fee from $14 to $19 for the first handgun or any number of rifles/shotguns in a single transaction, and capping the DROS fee for each additional *handgun* being purchased along with the first handgun at $15.

39. Subdivision (b) of Penal Code section 28225 [12076(e)] further provides that "[t]he [DROS] fee shall be no more than is necessary to fund" the activities enumerated at Penal Code section 28225(b)(1)-(11) [12076(e)(1)-(10)].

40. Penal Code section 28225(b)(11) [12076(e)(10)] purports to authorize the DOJ to use revenues from the DROS fee to fund "the estimated reasonable costs of [DOJ] firearms-related regulatory and enforcement activities related to the sale,

purchase, possession, loan, or transfer of firearms."

41. Prior to January 1, 2012, section 28225(b)(11) [12076(e)(10)] did not provide for expenditure of DROS fee revenues on the mere "possession" of firearms. But the Legislature amended that section during the 2011 Legislative session to allow for such, based on its following purported findings:

> SECTION 1. The Legislature finds and declares all of the following:
>
> (a) California is the first and only state in the nation to establish an automated system for tracking handgun and assault weapon owners who might fall into a prohibited status.
>
> (b) The California Department of Justice (DOJ) is required to maintain an online database, which is currently known as the Armed Prohibited Persons System, otherwise known as APPS, which cross-references all handgun and assault weapon owners across the state against criminal history records to determine persons who have been, or will become, prohibited from possessing a firearm subsequent to the legal acquisition or registration of a firearm or assault weapon.
>
> (c) The DOJ is further required to provide authorized law enforcement agencies with inquiry capabilities and investigative assistance to determine the prohibition status of a person of interest.
>
> (d) Each day, the list of armed prohibited persons in California grows by about 15 to 20 people. There are currently more than 18,000 armed prohibited persons in California. Collectively, these individuals are believed to be in possession of over 34,000 handguns and 1,590 assault weapons. The illegal possession of these firearms presents a substantial danger to public safety.
>
> (e) Neither the DOJ nor local law enforcement has sufficient resources to confiscate the enormous backlog of weapons, nor can they keep up with the daily influx of newly prohibited persons.
>
> (f) A Dealer Record of Sale fee is imposed upon every sale or transfer of a firearm by a dealer in California. Existing law authorizes the DOJ to utilize these funds for firearms-related regulatory and enforcement activities related to the sale, purchase, loan, or transfer of firearms pursuant to any provision listed in Section 16580 of the Penal Code, but not expressly for the enforcement activities related to possession.
>
> (g) Rather than placing an additional burden on the taxpayers of California to fund enhanced enforcement of the existing armed prohibited persons program, it is the intent of the Legislature in enacting this measure to allow the DOJ to utilize the Dealer Record of Sale Account for the additional, limited purpose of funding enforcement of the Armed Prohibited Persons System.

42. Penal Code section 28230(a)(2) [12076(f)(1)(B)] provides for DOJ to also

use DROS fee revenues for "the actual processing costs associated with the submission of a [DROS] to the [DOJ]."

43. Pursuant to statute, revenue from the DROS fee is supposed to be deposited into the DROS Special Account of the General Fund ("DROS Special Account") and appropriated by the Legislature. Cal. Penal Code § 28235 [12076(g)].

GENERAL ALLEGATIONS

44. All of the above paragraphs are re-alleged and incorporated herein by reference.

45. Individual PLAINTIFFS BAUER, WARKENTIN, HACKER, and FERRY, and those persons represented by organizational PLAINTIFFS NRA and CRPA FOUNDATION, have each been required to pay, have in fact paid, and expect to pay in the future the DROS Fee as currently required by California law before taking possession of firearms purchased from an FFL or transferred through an FFL as a private party transfer.

46. The funds from the DROS Fee that PLAINTIFFS paid and expect to pay in the future are purportedly deposited into the DROS Special Account and ultimately surrendered to DEFENDANTS' control pursuant to appropriation from the DROS Special Account by the Legislature.

47. The Legislature has appropriated, and DEFENDANTS intend to spend from the DROS Special Account, $25 million to fund, at least in part, general law enforcement activities associated with the APPS Program.

48. Because the fundamental right to possess a firearm under the Second Amendment includes a corresponding right to acquire a firearm, monies collected from the DROS Fee must only be used to fund activities that are reasonably related to the fee payer's impact on the state.

49. Simply because the crimes targeted by the APPS program involve

firearms does not mean they have a sufficient nexus to DROS Fee payers such that its enforcement costs may constitutionally fall on the shoulders of PLAINTIFFS and other lawful firearm purchasers via the DROS Fee; they do not and cannot.

50. DEFENDANTS cause PLAINTIFFS irreparable harm by choosing to spend revenues obtained from the DROS Fee on general law enforcement operations associated with the APPS program because they are requiring PLAINTIFFS to uniquely subsidize government services that are not reasonably related to regulating lawful firearms transactions, but are admittedly for the general welfare.

51. The utilization of the DROS Fee by DEFENDANTS for these improper purposes necessitates judicial action to halt infringements and violations of PLAINTIFFS' constitutional rights.

DECLARATORY JUDGMENT ALLEGATIONS

52. All of the above paragraphs are re-alleged and incorporated herein by reference.

53. There is an actual and present controversy between the parties hereto in that PLAINTIFFS contend that the manner in which DOJ currently uses the revenues from the DROS Fee is unconstitutional and on information and belief, allege that DEFENDANTS' disagree.

54. PLAINTIFFS desire a judicial declaration of their rights and DEFENDANTS' duties; namely, that the DOJ's expenditure of monies collected from the DROS Fee on general law enforcement activities associated with the APPS program infringes on PLAINTIFFS' Second Amendment rights.

55. To be clear, PLAINTIFFS do not ask this Court to address the legality of imposing the DROS Fee in the first place nor that of the APPS System. PLAINTIFFS here merely seek a declaration as to whether the monies from a fee that they are required to pay before they may lawfully engage in Second

Amendment protected conduct, i.e., obtaining a firearm, can be appropriated to general law enforcement purposes unrelated to regulating PLAINTIFFS' impact on the state.

INJUNCTIVE RELIEF ALLEGATIONS

56. All of the above paragraphs are re-alleged and incorporated herein by reference.

57. PLAINTIFFS have been, are presently, and will continue to be irreparably harmed by the assessment of the DROS Fee as a precondition on the exercise of PLAINTIFFS' Second Amendment rights insofar as the revenues from such assessment are utilized for purposes not reasonably related to regulating fee payers' activities in lawfully obtaining a firearm, i.e., general law enforcement activities.

58. If an injunction does not issue from this Court enjoining DEFENDANTS from spending DROS Fee revenues on such general law enforcement activities, DEFENDANTS will continue to do so in derogation of PLAINTIFFS' Second Amendment rights, thereby irreparably harming PLAINTIFFS.

59. PLAINTIFFS have no adequate remedy at law. Damages are indeterminate or unascertainable and, in any event, would not fully redress any harm suffered by PLAINTIFFS as a result of DEFENDANTS subjecting PLAINTIFFS to the illegal precondition on the exercise of PLAINTIFFS' constitutional right to acquire firearms, i.e., funding general law enforcement activities.

60. Injunctive relief would eliminate PLAINTIFFS' irreparable harm and allow PLAINTIFFS to acquire firearms free from the unlawful precondition currently inherent in the mandatory DROS Fee, in accordance with their rights under the Second and Fourteenth Amendments.

61. Accordingly, injunctive relief is appropriate.

CLAIM FOR RELIEF:
VALIDITY OF DEFENDANTS' USE OF DROS FEE REVENUES
Violation of the Second Amendment Right to Keep and Bear Arms
(U.S. Const., Amends. II and XIV)
(By All Plaintiffs Against All Defendants)

62. All of the above paragraphs are re-alleged and incorporated herein by reference.

63. DEFENDANTS use revenues collected from a fee, payment of which is generally required as a precondition for the lawful receipt of a firearm in California, in order to fund general law enforcement activities not reasonably related to regulating the behavior or impact on the state of the fee payers – like PLAINTIFFS. In doing so, DEFENDANTS are propagating customs, policies, and practices that infringe on PLAINTIFFS' right to acquire firearms as guaranteed by the Second and Fourteenth Amendments.

64. DEFENDANTS cannot satisfy their burden of justifying these customs, policies, and practices that infringe PLAINTIFFS' rights.

65. PLAINTIFFS are entitled to declaratory and injunctive relief against DEFENDANTS and their officers, agents, servants, employees, and all persons in active concert or participation with them who receive actual notice of the injunction, enjoining them from engaging in such customs, policies, and practices.

PRAYER

WHEREFORE PLAINTIFFS pray for relief as follows:

1) For a declaration that DEFENDANTS' enforcement of the APPS program is not sufficiently related to PLAINTIFFS' lawful firearm purchases so as to justify DEFENDANTS' using the revenues from the DROS Fee – which PLAINTIFFS must pay to obtain a firearm – for the purpose of funding the APPS program, and that such use of DROS Fee funds impermissibly infringes on PLAINTIFFS' Second Amendment rights because it improperly requires PLAINTIFFS to bear the burden of financing general law enforcement activities as a precondition to exercising those rights;

2) For a preliminary and permanent prohibitory injunction forbidding DEFENDANTS and their agents, employees, officers, and representatives from using DROS Fee revenues to fund the APPS program;

3) For remedies available pursuant to 42 U.S.C. § 1983 and for an award of reasonable attorneys' fees, costs, and expenses pursuant to 42 U.S.C. § 1988, and/or other applicable state and federal law;

4) For such other and further relief as may be just and proper.

Dated: July 24, 2013

Michel & Associates, P.C.

/s/ C. D. Michel
C. D. Michel
Attorney for the Plaintiffs

IN THE UNITED STATES DISTRICT COURT

FOR THE EASTERN DISTRICT OF CALIFORNIA

FRESNO BRANCH COURTHOUSE

BARRY BAUER, STEPHEN WARKENTIN, NICOLE FERRY, LELAND ADLEY, JEFFREY HACKER, NATIONAL RIFLE ASSOCIATION OF AMERICA, INC., CALIFORNIA RIFLE PISTOL ASSOCIATION FOUNDATION, HERB BAUER SPORTING GOODS, INC. Plaintiffs vs. KAMALA HARRIS, in Her Official Capacity as Attorney General For the State of California; STEPHEN LINDLEY, in His Official Capacity as Acting Chief for the California Department of Justice, and DOES 1-10. Defendants.	**CASE NO. 1:11-cv-01440-LJO-MJS** **CERTIFICATE OF SERVICE**

IT IS HEREBY CERTIFIED THAT:

I, the undersigned, am a citizen of the United States and am at least eighteen years of age. My business address is 180 E. Ocean Blvd., Suite 200, Long Beach, California, 90802.

I am not a party to the above-entitled action. I have caused service of:

SECOND AMENDED COMPLAINT FOR DECLARATORY AND INJUNCTIVE RELIEF

on the following party by electronically filing the foregoing with the Clerk of the District Court using its ECF System, which electronically notifies them. Electronically filed documents have been served conventionally by the filer to:

Anthony R. Hakl, Deputy Attorney General
California Department of Justice
Office of the Attorney General
Civil Law Division
Government Law Section
1300 I Street, Suite 125
Sacramento, CA 94244

I declare under penalty of perjury that the foregoing is true and correct. Executed on July 24, 2013.

/s/ C. D. Michel
C. D. Michel
Attorney for Plaintiffs