Is it a fee or tax? Cap-and-trade faces tough questions

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MANNY CRISOSTOMO Sacramento Bee file
The Valero Benicia oil refinery is one of the state companies covered in California’s greenhouse-gas emissions law. The state’s auctions face a legal challenge.

California’s marquee climate-change program faced tough scrutiny on Tuesday from a state appeals court judge who seemed skeptical that the $4.4 billion raised from the state’s cap-and-trade program complied with laws regulating taxes and fees.

“Where does this end?” Associate Justice Harry Hull asked state lawyers at a hearing in a long-running lawsuit that challenges the state’s ability to collect revenue from the cap-and-trade auctions it has sponsored since 2012.

Despite Hull’s questioning, two of three justices at the 3rd District Court of Appeal appeared to be leaning toward upholding the California Air Resources Board’s greenhouse gas cap-and-trade program. It aims to gradually reduce greenhouse-gas emissions over time by compelling industries to change the way they do business under the authority of the landmark 2006 law, Assembly Bill 32.

A decision from the court is expected within 90 days, but the losing side likely will appeal the case to the state Supreme Court.

The hourlong hearing unfolded in a packed courtroom across the street from the Capitol, where Gov. Jerry Brown delivered a defense of California values and his environmental policies at his State of the State address. He’s asking lawmakers to renew the cap-and-trade program, extending its authority past 2020.

The court case combines separate lawsuits filed by the California Chamber of Commerce and Woodland-based tomato processor Morning Star.

The chamber and the company contend that the Air Resources Board created a tax on businesses in violation of the state’s landmark Proposition 13 when it devised cap-and-trade auctions that steer revenue to state services.
A permit allows a business to emit 1 ton of greenhouse gas. Each permit cost $12.73 at a November auction.

If judges view the auction revenue as a fee, the Air Resources Board should only be able to raise enough revenue to cover the costs of managing the program. If it’s a tax, Proposition 13 requires that the auctions win the blessing of two-thirds of the Legislature.

“It’s either a regulatory fee or it’s a tax. That is the universe we operate from in California,” argued Chamber of Commerce attorney James Perrinello. The auction revenue is “essentially an enormous slush fund and they’re not necessary to meet AB 32’s greenhouse gas reduction goals,” he said.

David Zonana, a deputy attorney general representing the Air Resources Board, countered that revenue from the cap-and-trade auctions represented a different kind of charge. He wouldn’t put a name on it. “It’s something else,” he said.

He characterized the money raised from the auctions as a “regulatory tool.” He insisted that businesses do not have to buy permits at the auctions. For instance, they can hit pollution targets by investing in their own businesses to reduce their carbon footprint. They can buy pollution permits from other companies, or purchase offsets from groups that do work to reduce greenhouse-gas emissions. “What ARB did was create a program where their emitters could design their own compliance,” Zonana said.

Associate Justices Elena Duarte and Kathleen Butz appeared willing to work with Zonana’s reasoning. When Morning Star’s attorney characterized the greenhouse gas allowances as permits for “the operation of pre-existing equipment,” Duarte interrupted by saying “they permit pollution.” Butz similarly likened the cap-and-trade auctions to other government regulations affecting business, such as the minimum wage and changes in workers’ compensation.

Hull’s questions suggested he was most concerned with how the state uses revenue from the auctions. In the past, the state has used auction revenue for affordable housing, environmental restoration and its high-speed rail project.

“If it’s true that almost any human activity, indeed animal activity, generates greenhouse gas emissions, then the money can be used for practically anything,” Hull said.

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Money raised for California greenhouse reduction fund from cap-and-trade auctions, $4.4 BILLION