

## California Cap-and-Trade Program on Hold Pending Additional Environmental Review

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A California state court has halted implementation of the California Cap-and-Trade Program. The court issued a ruling based on compliance with requirements of the California Environmental Quality Act (CEQA) that could have significant impacts on the California Air Resources Board's (CARB) planned implementation of California's landmark greenhouse gas (GHG) law, Assembly Bill 32 (AB 32).

The March 17, 2011, Statement of Decision from San Francisco Superior Court in *Association of Irrigated Residents v. California Air Resources Board* [Case No. CPF-09-509562] has the potential to delay implementation of a wide range of measures set forth in the AB 32 Scoping Plan, which includes the Cap-and-Trade Program that was scheduled to begin on Jan. 1, 2012.

### Background on the California Global Warming Solutions Act of 2006 (AB 32)

AB 32 was enacted on Sept. 27, 2006. The statute directs CARB to develop a Scoping Plan to reduce statewide GHG emissions to 1990 levels by the year 2020. In December 2008, CARB adopted its Scoping Plan.

CARB's AB 32 Scoping Plan sets forth CARB's overall program design for meeting its AB 32 statutory mandate. It includes a variety of strategies for reducing GHG emissions, including measures such as energy efficiency, a renewable portfolio standard, and a low carbon fuel standard. The Scoping Plan also endorsed the establishment of a Cap-and-Trade Program to meet AB 32's mandatory GHG reduction targets. Entities covered by AB 32 must rely on the GHG allowance and offset products available in the cap-and-trade market to satisfy their compliance obligations. The Cap-and-Trade Program is scheduled to begin for California's electricity sector and large industrial sources on Jan. 1, 2012. The transportation and natural gas sectors will be covered by mandatory AB 32 compliance obligations starting in January 2015.

### Environmental justice groups challenge the AB 32 Scoping Plan and the Cap-and-Trade Program

On June 10, 2009, the Association of Irrigated Residents (AIR) filed suit in San Francisco Superior Court against CARB along with a consortium of other environmental justice groups (Petitioners). Petitioners alleged that CARB failed to satisfy CEQA when it implemented the AB 32 Scoping Plan and the Cap-and-Trade Program. Petitioners also claimed that CARB's implementation of the AB 32 Scoping Plan failed to satisfy the statutory requirements of AB 32.

Petitioners challenged the environmental review document that CARB prepared to evaluate the Scoping Plan on the grounds that CARB failed to take the steps necessary to complete a valid environmental review under CEQA. More specifically, Petitioners claimed that CARB (1) did not adequately evaluate the impacts of Scoping Plan measures; (2) did not adequately evaluate alternatives; and (3) improperly approved and implemented the AB 32 Scoping Plan before CARB received and responded to public comments. Only the latter two challenges to the AB 32 Scoping Plan were successful.

### Respect for CEQA requirements drives delay in AB 32 implementation

*Alternatives to the AB 32 Scoping Plan and Cap-and-Trade Program were neglected in CARB's environmental review*

The Superior Court deemed CARB's analysis of potential alternatives to the measures set forth in the AB 32 Scoping Plan more generally, and the Cap-and-Trade Program in particular, insufficient. Under CEQA, CARB is required to consider "feasible alternatives to the proposed action" that reduce adverse environmental impacts and comply with CEQA's broad policy goals and substantive standards.

Petitioners alleged that CARB's environmental analysis does not demonstrate why CARB chose the Scoping Plan rather than other alternatives. The court agreed. In particular, the Statement of Decision found that while CARB had extensively analyzed the Cap-and-Trade Program, it had completely failed to provide any meaningful discussion of potential alternatives. With respect to alternatives, the decision found that "informative analysis is absent," and noted that only two paragraphs of the Scoping Plan were dedicated to consideration of a carbon fee or tax. The ruling also rejected CARB's argument that detailed analysis of alternatives would be satisfied in future rulemaking. Instead, the decision held that a factual analysis of each alternative to the Cap-and-Trade Program must be made available for public comment in order to satisfy CEQA.

*CARB approved the Scoping Plan before completing its environmental review*

Petitioners also alleged that CARB approved the Scoping Plan before satisfying its obligation to review and respond to public comment. In order to comply with CEQA, CARB must respond to comments that raise any significant environmental

issues. In addition, a decision maker such as the executive officer must approve written responses to each issue before final action is taken on the proposal.

CARB initiated steps towards final approval of the Scoping Plan with Resolution 08-47 on Dec. 11, 2008. The resolution noted that final approval of the Scoping Plan was subject to the executive officer's approval of written responses to environmental issues. Before CARB had responded to public comments on its environmental review document, CARB held a public workshop to discuss its process for implementing the Scoping Plan. The executive officer did not approve written responses to comments on the environmental review document until May 7, 2009. CARB did not make any changes to the Scoping Plan between December 2008 and May 2009 in response to any comments submitted.

The court upheld Petitioners' challenge on the grounds that CARB's approval of the Scoping Plan "undermine[d] CEQA's goal of informed decision making" because written responses were prepared after the decision to adopt the Scoping Plan was essentially made. As such, the court determined that CARB did not make an informed decision under CEQA when it adopted the Scoping Plan in December 2008 because it hadn't considered the public comments it had received on its environmental review document.

### **CARB must comply with CEQA's requirements to move forward with AB 32 implementation**

The scope of the court's remedy is broadly drafted. Not only does the ruling direct CARB to set aside certification of its environmental review document, it also enjoins any further implementation of Scoping Plan measures until CARB has successfully demonstrated compliance with CEQA. The court explicitly declined to authorize CARB to continue implementing the Scoping Plan in parallel with revising its environmental review document because moving forward with the current AB 32 Scoping Plan would further develop a mature Cap-and-Trade Program and essentially "render consideration of alternatives a nullity." The court found that it was necessary to halt implementation to ensure that alternatives were adequately considered.

The Cap-and-Trade Program was scheduled to begin on Jan. 1, 2012. It is unclear whether CARB will be able to complete an alternatives analysis and resume its rulemaking and implementation activities quickly enough to meet this deadline.

In addition, the court's decision to enjoin implementation of the AB 32 Scoping Plan more broadly also threatens to delay CARB progress on other AB 32-related measures beyond the Cap-and-Trade Program. As noted above, the AB 32 Scoping Plan includes a wide variety of strategies for reducing GHG emissions, including energy efficiency programs, the renewables portfolio standard, and the low carbon fuel standard. As drafted, the ruling appears to preclude CARB from working to implement these measures as well.

CARB has indicated that it plans to appeal the decision. In connection with that appeal, CARB may request, and be granted, a stay of the injunction that prevents it from working to implement the AB 32 Scoping Plan. In addition, CARB hopes to narrow the breadth of the stay and suggest that the ruling should only enjoin its work to implement Cap-and-Trade, not the other measures set forth in the AB 32 Scoping Plan, while it conducts the additional analysis necessary to make its environmental review document consistent with CEQA.

### **CEQA setback overshadows finding that Scoping Plan is consistent with AB 32 statutory requirements**

Although noncompliance with CEQA rules may delay implementation of key aspects of the AB 32 Scoping Plan, the court's decision handed CARB a decisive victory on the question of whether the Scoping Plan violated the statutory requirements of AB 32. Petitioners alleged that CARB violated AB 32 in numerous ways. They specifically cited CARB's analysis of maximum technologically feasible and cost effective measures, CARB's decision to pursue Cap-and-Trade as a market-based compliance mechanism, the public health and environmental analysis, and the quantity of information CARB considered as potential violations of the AB 32 statute. The court adopted a deferential, arbitrary, and capricious standard of review of Petitioners' claims and wholly rejected the challenge. The decision therefore preserves the overall substance of the AB 32 Scoping Plan, and leaves only the CEQA compliance issues described above for CARB to resolve.

For more information regarding this decision and its potential impact on California's plans to implement the GHG reduction measures set forth in the AB 32 Scoping Plan, including the Cap-and-Trade Program, please contact a Davis Wright Tremaine climate change professional.

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