Challenging Cap and Trade:
Legal and Strategic Avenues for The Trump Administration

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Introduction

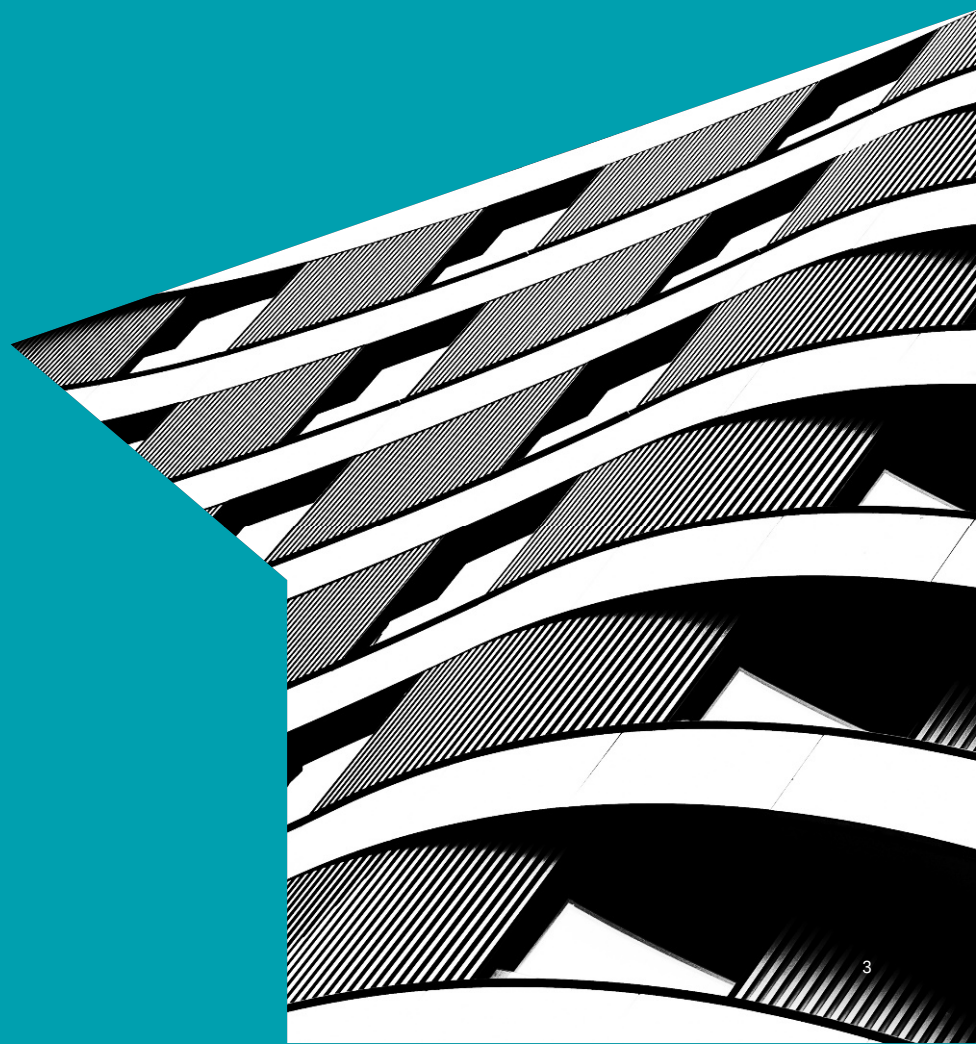
Recent actions by Trump Administration signal intent to challenge California's Cap-and-Trade program and similar state policy initiatives as part of effort to promote use of coal and other fossil fuels

Represents continuation of efforts during the first Trump Administration to challenge California's Cap-and-Trade program as unlawful

Today's presentation will focus on potential legal avenues that Trump Administration may pursue to challenge or undermine Cap-and-Trade programs

Trump Efforts to Challenge State Policy

Protecting American Energy from “State Overreach”



Overview of Trump Efforts To Date

- Trump Administration has issued close to 30 executive orders addressing the energy sector since taking office in January 2025
- Majority of EOs direct heads of relevant executive agencies to take steps to remove barriers to the production and use of fossil fuels, including coal, natural gas, and oil—both at federal and state level
- EOs reflect willingness of Trump Administration to use federal authority to impede state and local efforts to support transition away from fossil fuels to greater reliance on renewable and zero-carbon resources
- Frames state policies promoting use of renewable and zero carbon resources as unlawful, increasing costs for consumers, and endangering reliability

Notable Trump Energy EOs and Proclamation

- Initial Recissions of Harmful Executive Orders and Actions (Jan. 20)
- Delivering Emergency Price Relief for Americans (Jan. 20)
- Unleashing Alaska's Extraordinary Resource Potential (Jan. 20)
- Temporary Withdrawal of All Areas of OCS from Offshore Wind Leasing (Jan. 21)
- Declaring a National Energy Emergency (Jan. 24)
- Establishing the National Energy Dominance Council (Feb. 14)
- Unleashing American Energy (Feb. 19)
- Immediate Measures to Increase American Mineral Production (Mar. 20)
- Strengthening the Reliability and Security of The U.S. Electric Grid (Apr. 8)
- Reinvigorating America's Beautiful Clean Coal Industry (Apr. 8)
- Regulatory Relief for Certain Stationary Sources to Promote American Energy (Apr. 8)
- Protecting American Energy from State Overreach (Apr. 8)
- Zero-Based Regulatory Budgeting to Unleash American Energy (Apr. 9)

EO 14260: Protecting American Energy from State Overreach

- Directs AG, in consultation with appropriate executive agencies, to identify all State and local laws, regulations, causes of actions, policies, and practices burdening the identification, development, siting, production, or use of domestic energy resources that are or may be unconstitutional, preempted by Federal law, or otherwise unenforceable.
- Identifies California—along with New York and Vermont—as guilty of attempting to "dictate national energy policy" by "punishing" carbon use
- Directs AG to expeditiously take all appropriate actions to stop the enforcement of unconstitutional or unlawful state laws
- Within 60 days (by June 7, 2025), AG must submit report identifying action to stop enforcement of state laws and recommending any additional Presidential or legislative action necessary to stop the enforcement of State laws

Efforts To Implement EOs Remain In Early Stages

- Implementation of EO 14260 and other EOs remain in early stages
- With deadline for AG report rapidly approaching, we are likely to see an escalation in the Trump Administration's campaign against Cap-and-Trade programs and other similar state initiatives and policies
- Indeed, in early May, DOJ filed suits against Michigan, Hawaii, New York, and Vermont challenging programs seeking to hold polluters financially responsible for role in climate change
- Challenge to Cap-and-Trade and other programs likely to play out concurrently with broader efforts by Trump Administration to use authority to require the retention and operation of coal, oil, and natural gas resources to meet system needs

EO Represents Continuation of Prior Effort To Challenge Cap-and-Trade

United States v. California, No. 2:19-cv-02142 (E.D. Cal.)

Primary allegations

- Preempted by Federal government's exclusive authority over foreign affairs
- Agreement between California and Quebec violates Treaty and Compact Clauses of U.S. Constitution

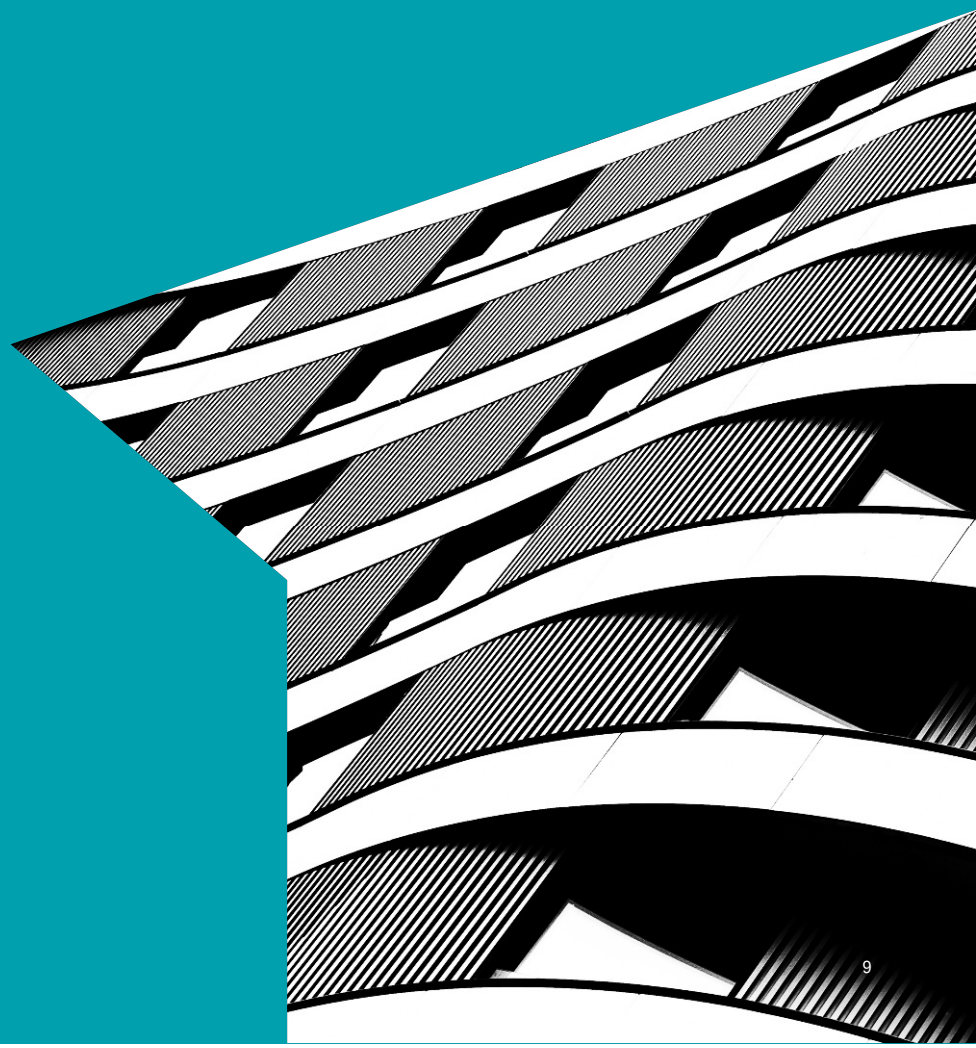
Foreign Affairs Power Claim

- Found that no "express federal foreign policy" exists that conflicts with California program
- Determined that Cap-and-Trade program extended beyond areas of traditional state authority, but that U.S. had failed to demonstrate that actions would have more than "incidental or indirect effect on foreign affairs"

Treaty Clause and Compact Clause

- California-Quebec agreement not a "treaty," as it did not create an alliance for peace/war, mutual governance, or confer sovereignty
- Found that agreement lacked the "classic indicia" of a compact and did not enhance state power in a way that threated federal supremacy

The Path Forward



State Authority To Regulate Emissions And Resource Mix Well-Established

States retain broad "police powers" under the 10th Amendment to regulate matters related to health, safety, and the environment

- Courts have recognized that state police power includes authority to regulate the quality of air within a state
  - "Legislation designed to free [the air] from pollution . . . clearly falls within the exercise of even the most traditional concept of . . . the police power." *Huron Portland Cement Co. v. City of Detroit*, 362 U.S. 440 (1960).

Federal law also includes carve outs that preserve state jurisdiction in key areas

- Federal Power Act exempts from FERC's jurisdiction facilities used in the generation of electric energy
- Clean Air Act preserves state authority to adopt or enforce emissions standards or limits that are more stringent than federal standards

Potential Challenges to California's Cap-and-Trade Program

- Lawsuits that have been filed following issuance of EO 14260 highlight willingness on the part of the administration to challenge existing legal precedent in effort to limit authority of States to regulate GHG emissions
- These actions highlight claims that are likely to be raised in challenge to Cap-and-Trade programs:
  - —Dormant commerce clause
  - —Preemption by federal law
  - —Foreign Affairs Doctrine

Dormant Commerce Clause - Overview

- Congress's authority over interstate commerce prohibits states from adopting laws that discriminate against, or impose undue burdens on, interstate commerce
- Courts examine:
  - —Facial discrimination — whether a law explicitly discriminates based on origin
  - —Purpose or effect — whether the law discriminates in practical effect or legislative intent
  - —Extraterritoriality — whether a law regulates conduct wholly outside the state's borders
  - —Pike balancing test — applied when a law is neutral but burdens interstate commerce: the burden must not be clearly excessive in relation to local benefits
- Facially discriminatory laws must satisfy strict scrutiny: the state must prove the law serves a legitimate local purpose that cannot be achieved through nondiscriminatory means

Dormant Commerce Clause – Application to Cap-And-Trade

Potential legal challenges

- Trump Administration likely to argue that Cap-and-Trade violates dormant commerce clause because it targets commercial activity that occurs primarily, if not exclusively, outside of the state (e.g., coal generation located outside of California)

Counterarguments

- State likely to argue that program is neutral, applies equally to all market participants, and serves compelling public interest in reducing GHG emissions
- Courts generally have upheld state environmental policies absent evidence that program was intended to protect in-state businesses

Dormant Commerce Clause (cont'd)

***Rocky Mt. Farmers v. Corey,* 730 F.3d 1070 (9th Cir. 2013) and 913 F.3d 940 (9th Cir. 2019**)

- Challenged California's Low Carbon Fuel Standard's ("LCFS") use of life cycle analysis to determine carbon intensity on basis that discriminated against out-of-state fuel
- Court found that regulation was not facially discriminatory "simply because it affects in-state and out-of-state interests unequally" and that treatment under LCFS was based not on a "fuel's origin but on its carbon intensity."
  - "The Constitution does not require California to shut its eyes to the fact that some ethanol is produced with coal and other ethanol is produced with natural gas because these kinds of energy production are not evenly dispersed across the country or because other states have not chosen to regulate the production of greenhouse gases. If the states are to remain a source of innovative and far-reaching statutes that supplement national standards, they must be permitted to submit the goods and services sold within their borders to certain environmental standards without having thereby discriminated against interstate commerce from states with lower local standards."

Federal Preemption - Overview

Under the Supremacy Clause of U.S. Constitution, if a federal law and a state law conflict, the federal law wins.

Types of Preemption:

- Explicit Preemption – Congress clearly says that federal law overrides state law.
- Field Preemption – The federal government regulates an area so thoroughly that there's no room for states to add their own rules.
- Conflict Preemption – Even if Congress doesn't say so directly, a state law can't stand if:
  - It's impossible to follow both federal and state rules at the same time, or
  - The state law gets in the way of what Congress is trying to achieve.

Federal Preemption – Clean Air Act

- Clean Air Act explicitly recognizes continued role for states in regulating air pollution and emissions
  - Preamble to CAA states that "air pollution control at its source is primary responsibility of States and local governments."
  - Savings clause and other provisions of the CAA recognize authority of states to regulate emissions
- Nevertheless, recent suits by Trump Administration take expansive view of federal government's role in regulating emissions and displacement of state law

U.S. v. Hawaii, No. 1:25-cv-00179 (D. Haw.)

- Argues that Congress gave EPA authority to determine "whether and how to regulate greenhouse gas emissions, thereby displacing federal common law claims and occupying the field of interstate air pollution regulation."
- Hawaii state law is preempted because it impermissibly regulates "out-of-state greenhouse gas emissions and obstructs the Clean Air Act's comprehensive federal-state framework[.]"
- Savings clause limited to adopting and enforcing "air pollution control requirements and limitations on in-state sources"
- State actions to regulate GHG emissions create a "chaotic 'patchwork' of regulations that undermine the national interest in readily available and affordable energy and the government's ability to effectively administer coherent national environmental policy and regulation of global pollution."

Federal Preemption – Federal Power Act

Potential legal challenges

- Trump Administration could argue that Cap-and-Trade program represents attempt to exercise control over wholesale prices or otherwise interferes with wholesale markets subject to exclusive jurisdiction of FERC

Counterarguments

- Courts have generally upheld the authority of the states to shape resource mix—even when such programs affect wholesale markets—so long as state is not attempting to set wholesale rates
- FERC policy statement on carbon pricing describes Cap-and-Trade programs as falling within state authority to regulate generation facilities

Federal Preemption – FPA (cont'd)

- *Allco Finance Ltd. v. Klee, 861 F.3d 82 (2d Cir. 2017)*
  - Upheld Connecticut's renewable procurement program
  - Court emphasized the state's ability to pursue public policy goals through resource selection that does not usurp FERC's role in rate-setting.
- *Coalition for Competitive Electricity v. Zibelman*, 906 F.3d 41 (2d Cir. 2018) and *Electric Power Supply Ass'n v. Star*, 904 F.3d 518 (7th Cir. 2018):
  - Upheld Illinois and New York ZEC programs that supported nuclear resources.
  - Courts found these programs did not intrude on FERC's domain because payments were not tethered to the wholesale market participation of resources.

Foreign Affairs Doctrine

- Recent actions by Trump Administration have claimed that effort to impose liability for GHG emissions harms government's ability to "speak with one voice" on a "uniquely international problem" that is "not well-suited to the application of state law"
- Although court in *U.S. v. California* rejected similar arguments, prior decision may not fully insulate Cap-and-Trade program against such challenge
  - Court's holding was based on failure to identify conflict between Cap-and-Trade and concrete "federal action such as a treaty, federal statute, or express executive branch policy."
  - Recognized that Cap-and-Trade extended beyond areas of traditional state responsibility, but found that there was not sufficient evidence that power to conduct foreign affairs had been substantially circumscribed or compromised by California's Cap-and-Trade program

Strategic Benefits Of Litigation

- Lack of case law clearly supporting Trump Administration's position unlikely to deter administration from pursuing action against Cap-and-Trade programs
- Even if unsuccessful, the institution of litigation is likely to serve other strategic ends:
  - Generate uncertainty
  - Obtain leverage
  - Win political points with supporters

QUESTIONS?

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