

Is Cap-and-Trade Dead?

A. Denny Ellerman

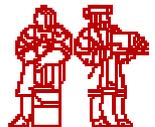
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‘Cap and Trade’ Loses Its Standing as Energy Policy of Choice

- NY Times article heading, 3/25/2010
- Some inaccuracies, but reflective of general malaise and disappointment
- Depends on how “cap-and-trade” is defined and what is meant by “dead”
- More re-branding than factual

Topics

- What is cap-and-trade and what do we know about it?
- A recap of where we are for GHGs
- A realistic look at the prospects

What is Cap-and-Trade?

- A known, tested, and tried concept
 - SO₂, NO_x, RECLAIM and other programs
 - Creates a price on emissions and reduces emissions with few other side effects
- A form of environmental regulation
 - Radically different from conventional “command-and-control”
 - Object is to reduce and limit emissions
 - Trading is a means to least-cost compliance, not a source of profit

What have we learned?

- More effective and lower cost than conventional regulation
 - Firms do respond to prices
- Many new, unexpected ways to reduce emissions
 - Many more ways than could be mandated
 - No favored approaches/technologies
- Cheapest reductions tend to where there are the most emissions: “Dirtier is cheaper”
 - A matter of amortizing fixed costs: Paid by the ton

Recapping Where We Are

- RGGI and state action: Not leading anywhere
- Serious discussion engaged at the federal level for the past 3-4 years; beyond posturing
- A new administration that claims climate action is a high priority
- A bill has passed the House: Waxman-Markey
- But stalled in the Senate: less disciplined, advocates less heavily represented, effective super-majority required
 - Not even a simple majority among democrats

Kerry-Graham-Lieberman (KGL)

- First, three Senate heavy-weights
- Two new features that have opened the way
 - A significant boost for conventional energy: nuclear and oil and gas drilling
 - A “linked fee” to include transportation proposed by the oil industry
- Mostly like Waxman-Markey for the rest
- Including CAA exemption for GHGs
 - An important motivation on both sides

A Note on Allocation

- The biggest disadvantage of cap-and-trade
 - Scarcity rents are no longer hidden
- Many claimants and uses; none are obviously right
 - Entities required to surrender allowances?
 - More public expenditure? R&D? New tech?
 - Reduce taxes, national debt?
- Not a matter of auctioning vs. free allocation
- A new and compelling entrant: “cap-and-dividend,” direct distribution to households

What are the Prospects?

- Very unlikely this year
 - Presidential/congressional priorities elsewhere
 - Need more time to work out understandings
- Some imponderables
 - Can the extremes be kept in check?
 - Can a bipartisan majority be constructed?
 - Can allocation issues be resolved?
- Mass vs. EPA looms in case of failure
 - Slow, costly, and not so effective
 - CAIR-type cap might be possible

Is Cap-and-Trade Dead?

- If dead means this year, yes. If forever, no.
- It may not be called cap-and-trade, but it will act like it: a comprehensive cap and a price on GHG emissions
- The strongest argument for adopting cap-and-trade is that the alternatives are worse
- Unless we decide that climate change is not a problem