The Carbon Cap versus Carbon-Saving Standards

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Over the years, environmentalists have devised many standards and subsidies to encourage energy savings and reduce carbon emissions. But they don't all work well together, and a cap on carbon, President Obama's central climate policy, endangers many other policies. This realization has dawned in Germany, where the effect has been dramatic. We should learn from them rather than repeat their mistake, as is now being proposed.

Senator Majority Leader Harry Reid (D-NV) plans to pass a renewable-electricity standard (RES) in the same bill with a carbon cap. The RES aims to increase wind power and reduce carbon emissions beyond the effect of a carbon cap alone.

Unfortunately, the bill's authors do not seem to realize that a cap will short circuit the RES. Senator Jeff Bingaman (D-NM), one of the principle sponsors of the RES, states as the first reason for passing such a provision that "A renewable standard can reduce our dependence on fossil fuel sources." That's not what happened under Europe's cap.

At the urging of the Green Party, the Germans are subsidizing a renewable-electricity industry only to find, as Spiegel Online tells us, that carbon emissions "haven't been reduced by even a single gram." A Green-Party economist put it this way in an internal email: "Dear Daniel, sorry, but Germany's renewable energy law won't do anything for the climate anyway." Here's how Europe's carbon cap causes such a paradoxical effect.

Germany's prodigious wind farms reduce Germany's carbon emissions by a hundred million tons a year. So German businessmen need fewer carbon permits. They sell their extra permits to the highest bidders—for example, to Poland and Slovakia where coal-fired power plants use them to burn more coal. So, as Spiegal Online explains, "German wind turbines aren't helping to reduce CO2 emissions. They simply allow Eastern European countries to pollute more."

The key to this paradox is the fact that, under a working cap, all the permits will be used. So emissions will stay equal to the cap, because the cap is just the total number of permits. This means, our Senate's RES, like Germany's renewable energy law, cannot push emissions below the cap, and will save no carbon at all.

It's worth checking the crucial step, the assumption that all permits will be used. So notice that if the cap is having an effect, permits will be scarce and businesses will spend good money buying them—$80 billion a year according to the budget. At such prices, any permit that's not needed will be sold to someone who will use it.

This principle that emissions will equal the cap, applies to every policy and private action—not just to wind turbines or renewable electricity. If California requires more fuel-efficient cars, carbon permits that would have covered some of California's car emissions will go elsewhere. And carbon emissions will follow the permits to other industries and other parts of the country. Under a cap, California's law will save no carbon. National carbon emissions will still equal the national carbon cap.

Under a cap, when Californians spend good money to buy fuel-efficient cars, that simply gives the rest of the country more permits, so they can emit more carbon. This saves the rest of the country money at California's expense.

The message of these conflicts is neither that a cap won't work, nor that other carbon-saving policies don't make sense. The point is simply that mixing policies in the carbon market, without checking how they interact, can lead to unexpected and wasteful outcomes. Fortunately, we still have time to learn from Germany's embarrassment.

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* Visit http://stoft.com/p/122.html for more information