

Chapter 10

Administrative Implications of WCI

The WCI initiative would establish a bureaucracy to set a cap for emissions and then monitor the CO₂ emissions of every company, and would allow companies who come in below the cap to sell their extra cap space to companies that come in over the cap. It is highly questionable whether "cap and trade" would have any effect other than to create an expensive and intrusive bureaucracy, and create opportunities for entities to manipulate the system by setting up non-producing companies which could then obtain unused cap space that they could trade with others. Cap and trade creates a gigantic bureaucracy paid for and funded by tax dollars (which will require higher taxes to pay for its administration) and new government agencies that will restrict economic activity and will create a high probability of corruption.

A basic criticism is that cap-and-trade has no real effect on pollution, since it allows non-polluters to simply sell other companies the right to pollute, increasing costs without creating any benefit. In addition, existing polluters are either grandfathered in (and allowed to keep polluting at whatever level) or they are coerced into buying the right to pollute from a third party, all under the premise that the activity in which they are engaged has been conclusively deemed to be bad.

The WCI would set a limit, or cap, on CO₂ emissions from fossil fuel use. The effect of such a cap would be to impose rationing of coal, oil, and natural gas on the West's economy. Each covered utility, company, and manufacturing facility would be given allowances based on past emissions or some other formula. Those companies that emit less CO₂ than permitted by their allowances could sell the excess to those that do not; this is the trade part of cap and trade. Over time, the cap would be ratcheted down, requiring greater cuts in emissions.

However, the WCI program may be counterproductive. For example, over the long-term, energy companies will find ways to capture and store CO₂ emissions underground, rather than emit them into the air, or switch to lower-emitting

alternative energy sources as they are developed. But most experts see these advances as taking decades -- much longer than the initial WCI targets allow. In fact, the WCI targets may actually complicate the development of longer-term innovations, as they will divert resources to near-term fixes.

The chief political virtue of cap-and-trade is its complexity, which allows its advocates to shape public perceptions in essentially deceptive ways. Cap-and-trade would act as a tax, but it is not described as a tax. It would regulate economic activity, but it is promoted as a "free market" mechanism. Finally, it would trigger a huge amount of influence-peddling, as lobbyists scrambled to exploit the system for different industries and localities. This would undermine whatever abstract advantages the system has. This "environmental pork" would just be a start, and the program's potential to confer subsidies and preferential treatment would stimulate a lobbying frenzy. Think of today's farm programs -- and multiply exponentially.

The laws, regulations, mandates, and bureaucracy the WCI is proposing can best be described as potentially "Orwellian" in nature. For example, as noted in Chapter I, the WCI climate bureaucrats would even have authority over private company organization and reorganization. The WCI initiative represents the first step in what could be described as the "Californication" of the entire West's energy, environmental, and economic policies, with all of the attended increases in government bureaucracy, bureaucratic red tap, higher taxes, and higher consumer costs that characterize California's economic situation.

10.A. Illustration: Scope of the Problem

An indication of the potential administrative and bureaucratic complexities implied by the WCI cap-and-trade proposal can be gained by examining EPA's proposed CO₂ regulations. On July 11, 2008, EPA released an Advance Notice of Proposed Rulemaking (ANPR) that would declare carbon dioxide a dangerous pollutant to be regulated. The draft and 800 appendices supporting it in the Federal Register run to 18,094 pages, and stacked up would rise 6 - 1/2 feet. According to the U.S. Chamber of Commerce, EPA currently issues permits to 15,000 businesses under the Clean Air Act. If carbon dioxide were declared a dangerous pollutant and regulated under the Clean Air Act, more than 1.2 million new permits would have to be issued. Among those needing permits to stay in business are:

- 1 million mid- to large-sized buildings, including 10 percent of all churches, 20 percent of all food service businesses, half of

the buildings in the lodging industry, and 92,000 health care facilities.

- 200,000 manufacturing operations.
- 20,000 large farms.

The magnitude of construction delays, economic uncertainty, paperwork burdens, and engineering expenses that would surface under this regulatory plan is truly frightening. The flood of permit applications would overwhelm the resources of state EPAs that administer regulations under the Clean Air Act.

For example, farms would be considered a stationary source of greenhouse gas emissions just like power plants, and the U.S. Department of Agriculture reports the following agriculture operations would be required to secure permits:

- Dairy facilities with more than 25 cows.
- Beef operations with more than 50 cattle.
- Swine operations with more than 200 hogs.
- Farms with more than 500 acres of corn.

The U.S. Department of Agriculture concluded in its initial review of ANPR, "These operations simply could not bear the regulatory compliance costs that would be involved."

Further, the mere act of designating CO₂ as a dangerous pollutant may well trigger regulatory action under other provisions of the Clean Air Act -- actions that would dwarf the Kyoto Protocol in their scale, scope, and cost. Onerous restrictions on energy use would likely result from EPA action on CO₂ – and from the WCI initiative. In effect, the WCI initiative could foster a sustained regional economic recession in the West and encourage a rapid de-industrialization across the region, with the attendant job losses, reduced economic opportunity and depressed family incomes that such a process would bring.

10.B. Caution from Europe

Fortunately for U.S. policymakers struggling to devise CO₂ management plans such as cap-and-trade, Europe's ongoing efforts to impose a cap-and-trade program under the Kyoto Protocol

provide real-world insights into this challenge. Unfortunately for U.S. consumers, the European experience shows that these approaches incur significant costs while failing to reduce emissions.¹²⁵ Nearly every European country participating currently has higher emissions than when the treaty was first signed in 1997. Further, despite ongoing criticism of the U.S. from Kyoto parties for failing to ratify the treaty, emissions in many of these nations are actually rising faster than in the U.S.

The European experience also demonstrates the economically devastating problem of cap-and-trade fraud.¹²⁶ Ironically, it was Enron's former CEO Ken Lay who was a strong supporter of CO₂ cap-and-trade when the idea was first advanced in the 1990s, saying that it could "do more to promote Enron's business than almost any other regulatory initiative." These carbon allowances that will be bought and sold have a value estimated at \$50 billion to \$300 billion annually, and the trade in them would be a huge new business.¹²⁷ Enron may be gone, but others ready to take advantage of cap and trade -- often at public expense -- are not. In fact, as has been publicly noted, some of the strongest policy advocates for cap-and-trade regimes are already involved in multi-billion-dollar private-sector efforts designed to profit from trade in carbon allowances.¹²⁸

Europe's program covers 45 percent of the continent's emissions, 10,000 companies, and 27 European Union countries, and has constructed registries that list carbon dioxide emissions for every major plant. However, the approach has become a bureaucratic morass with a host of unexpected and costly side effects and a much smaller effect on carbon emissions than planned, and many companies contend that it is fundamentally unfair.¹²⁹ For example:

¹²⁵ European Environment Agency, *Greenhouse Gas Emission Trends and Projections in Europe 2006*, EEA Report No. 9, 2006, pp. 17-22, and Open Europe, "Europe's Dirty Secret: Why the EU Emissions Trading Scheme Isn't Working," August 2007; James Kanter, "Obama Beware: Brinkmanship Over Carbon Trading in Europe," *New York Times*, December 8, 2008.

¹²⁶ *Ibid.*, pp. 19-26, 46-49.

¹²⁷ Congressional Budget Office, "Trade-Offs in Allocating Allowances for CO₂ Emissions," Economic and Budget Issue Brief, April 25, 2007, p. 2.

¹²⁸ See James Kanter and Jad Mouawad, "The Energy Challenge - Money and Lobbyists Hurt European Efforts to Curb Gases," *New York Times*, December 10, 2008; U.S. General Accountancy Office, *International Climate Change Programs: Lessons Learned from the European Union's Emissions Trading Scheme and the Kyoto Protocol's Clean Development Mechanism*, GAO-09-151, November 2008; Iain Murray, "Cap and Trade: A System Made for Fraudsters," Competitive Enterprise Institute, May 1, 2007.

¹²⁹ Steven Mufson, "Europe's Problems Color U.S. Plans to Curb Carbon Gases," *Washington Post*, April 9, 2007, p. A01.

- Kollo Holding's factory in the Netherlands produces silicon carbide, a material used as an industrial abrasive and lining for high-temperature furnaces and kilns. The plant is an ecological exemplar: It uses waste gases to generate energy and has installed the latest pollution-control equipment. However, Europe's cap-and-trade program has driven electricity prices so high that the facility routinely shuts down for part of the day to save money on power, and although demand for its products is strong, the plant has laid off 40 of its 130 employees and reduced production. Two customers have turned to cheaper imports from China, which is not covered by Europe's costly regulations.
- Of all the effects of the cap-and-trade program, the rise in the price of power has aroused the most outrage. Much of the anger of consumers and industries has been aimed at the continent's utility companies which, like other firms, were given slightly fewer allowances than they needed. But instead of charging customers for the cost of buying allowances to cover the shortfall, utilities in much of Europe charged customers for 100 percent of the tradable allowances they were given, even though the government handed them out free, and electricity rates increased dramatically.
- Due to lobbying by well-connected companies, the EU's limits on emissions ended up being higher than the actual emissions. As a result, fewer companies than expected had to buy emissions in 2007, and the price of carbon allowances, which had been above \$30/ton of carbon, declined to about \$1/ton.
- Contentious disputes have erupted as countries seek to guard their interests. Eastern European nations have lobbied for more generous allocations because of their communist legacies and lower living standards. Germany, the continent's largest wind-energy producer, wants an E.U. mandate that each country get 20 percent of its energy from renewable resources by 2020;

Poland, which uses no renewable resources, is (not surprisingly) resisting.

- Germany contends that it has reduced emissions to 18.4 percent below 1990 levels, the benchmark used in the Kyoto Protocol and in Europe. However, nearly half the reduction was the result of decreased industrial output in the former East Germany after reunification. For the 2008-2012 period, EU officials have reduced Germany's emissions allocation by five percent.