May 17, 2009

From a Theory to a Consensus on Emissions

By JOHN M. BRODER

WASHINGTON — As Congress weighs imposing a mandatory limit on climate-altering gases — an outcome still far from certain — it is likely to turn to a system that sets a government ceiling on total emissions and allows polluting industries to buy and sell permits to meet it.

That approach, known as cap and trade, has been embraced by President Obama, Democratic leaders in Congress, mainstream environmental groups and a growing number of business interests, including energy-consuming industries like autos, steel and aluminum.

But not long ago, many of today's supporters dismissed the idea of tradable emissions permits as an industry-inspired Republican scheme to avoid the real costs of cutting air pollution. The right answer, they said, was strict government regulation, state-of-the-art technology and a federal tax on every ton of harmful emissions.

How did cap and trade, hatched as an academic theory in obscure economic journals half a century ago, become the policy of choice in the debate over how to slow the heating of the planet? And how did it come to eclipse the idea of simply slapping a tax on energy consumption that befouls the public square or leaves the nation hostage to foreign oil producers?

The answer is not to be found in the study of economics or environmental science, but in the realm where most policy debates are ultimately settled: politics.

Many members of Congress remember the painful political lesson of 1993, when President Bill Clinton proposed a tax on all forms of energy, a plan that went down to defeat and helped take the Democratic majority in Congress down with it a year later.

Cap and trade, by contrast, is almost perfectly designed for the buying and selling of political support through the granting of valuable emissions permits to favor specific industries and even specific Congressional districts. That is precisely what is taking place now in the House Energy and Commerce Committee, which has used such concessions to patch together a Democratic majority to pass a far-reaching bill to regulate carbon emissions through a cap-and-trade plan.

The bill is poised to win committee approval this week, although with virtually no support from Republicans. If there was a single moment when cap and trade crossed the threshold from relatively untested economic concept to prevailing government policy, it came in May 1989 in the West Wing office of C. Boyden Gray, counsel to President George H. W. Bush.

Mr. Gray had gathered a number of Mr. Bush's economic and environmental advisers to try to come up with a politically palatable plan to break a decade-long deadlock on the problem of acid rain, caused by sulfur dioxide emissions from coal-burning power plants in the Midwest.

Mr. Gray and the other Bush advisers knew that the power companies — and their allies in Congress — would vigorously oppose a tax on sulfur emissions or stringent new regulations to control them. But the environmental costs of the problem were too big to ignore.

One of Mr. Bush's outside advisers, Daniel J. Dudek, an economist with the Environmental Defense Fund, recalled that after years of unsuccessfully trying to sell the idea of setting a national limit on such emissions and letting companies trade permits or allowances to pollute, he finally came up with an analogy that broke the ice.

"I told Boyden: 'Imagine you just fired up the government printing presses and dumped an endless stream of money into the system. You'd have no way of controlling the money supply,' " Mr. Dudek said. "He understood totally and intuitively the importance of maintaining the cap, the key ingredient in our acid rain policy."

A month later, the Bush White House sent Congress a cap-and-trade plan for sulfur dioxide emissions that 18 months later became the linchpin of the 1990 amendments to the Clean Air Act, considered by many to be the most successful domestic environmental legislation ever enacted.

But the proposal came under ferocious political assault during those months. The final bill reflected a series of compromises needed to keep the coalition supporting it together. But the sulfur dioxide cap, a roughly 50 percent reduction in emissions over the next decade, held. The Environmental Protection Agency estimates that compliance with the program is close to 100 percent.

"Our proposal was at first ridiculed by environmentalists as little more than a license to pollute," said Representative Jim Cooper, a moderate Democrat from Tennessee and an early supporter of tradable permits. "But today, few dispute it is one of the government's most successful regulatory programs ever."

Representative Henry A. Waxman, a California Democrat and chairman of the energy committee, and his allies are marshaling many of the same arguments for the cap-and-trade approach as they used two decades ago for acid rain. A cap-and-trade program brings support from industries that prefer it to a top-down federal regulatory scheme, they say.

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Many regard it as the lowest-cost solution to a global pollution problem and a means of producing clean-energy breakthroughs. And it is a much easier political sell than a tax on fossil fuels. A measure of the political appeal of the final compromise on the 1990 cap-and-trade plan can be seen in the final votes: 401 to 25 in the House and 89 to 10 in the Senate.

But despite its success in the relatively contained problem of acid rain in the United States, cap and trade has proved less useful in other environmental problems and has gotten off to a troubled start in Europe.

Even some early devotees of a system of tradable emissions permits believe that it will not work for carbon dioxide, by definition a planetary problem. A straightforward tax on each ton of carbon dioxide emitted by any source, they say, would provide more a more predictable price and a simpler system to police.

“If a philosopher king could design a system, he or should might pick a taxation system,” said Robert Hahn, a White House economist under Mr. Bush who backed the acid rain program but is skeptical that it will work for the much more pervasive problem of carbon dioxide.

Former Vice President Al Gore has long supported a carbon tax. “Tax what you burn, not what you earn,” he says, as a way of both attacking global warming and remedying some of the inequities in the income tax.

But Mr. Gore also says a domestic cap-and-trade system would be easier to coordinate with other countries’ carbon control programs.

Cap and trade evolved from an academic debate that began in the early 1960s when Ronald H. Coase, then a professor at the University of Chicago Law School, wrote an influential paper, "The Problem of Social Cost,” that examined when government should intervene in cases where a private entity causes public harm.

In 1971, W. David Montgomery, a Harvard graduate student in economics, fleshed out the idea of emissions trading in his doctoral thesis and has spent much of the last three decades trying to figure out how the marketplace can deal with environmental problems that are caused by relatively few actors but have consequences felt globally.

He supported the acid rain trading program, but said it was based on “unique historical and economic circumstances” that did not apply to the much more difficult problem of carbon dioxide emissions.

Mr. Montgomery, now a vice president at Charles River Associates International, a consulting firm, said Mr. Waxman’s proposal would ultimately act like a tax on carbon-producing industries, disguised by a complex cap-and-trade system.

"It is a steel fist of regulation covered by a velvet glove of emission trading," Mr. Montgomery said. "Why not just impose a carbon tax?"