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Cap'n Trade's Unintended Carbon Consequences

As loyal readers know, Cap'n Trade is not who I think should steer California's global warming reduction ship. Nevertheless, the CPUC and the CEC appear determined to put the Cap'n in charge. If they are not careful, the Cap'n may have a mutiny on his hands.

Cap-and-trade schemes are all the rage these days with 'free' marketeers planning to reduce greenhouse gas emissions. Under these schemes, electric utilities—among others—receive permits to emit carbon dioxide. The number of permits declines over time, and utilities can trade them among themselves as needed to cover their emissions. Utilities needing excess permits would have to buy them, perhaps from utilities needing fewer. A fine concept, at least, in theory.

The reality is much more complicated, as the agencies found out at their workshop November 5. The fundamental problem is how to get the program launched in a way that's equitable to all the players.

Some proposals would require the customers of the Los Angeles Department of Water and Power and other southern munis to pay more money into the system than customers of PG&E. Under other proposals, PG&E customers would even be *collecting* money from the poor suckers in LA LA land.

Neither of these is a good outcome, no matter how much you may look down your nose at LA and its DWP. The state bureaucrats would do well to avoid launching a program that is so patently unfair to customers of some utilities.

The problem arises from the way the permits are proposed to be allocated. One way is to require utilities to purchase the permits they need, perhaps through an auction. Since DWP is currently heavily dependent on coal-fired power, they would have to buy a lot of permits and pass the cost through to customers. PG&E is much less dependent on coal, so they would buy fewer. DWP-haters may think that this is fitting retribution, but DWP customers undoubtedly have a different opinion.

True, selling the emission permits would raise considerable amounts of money that could be used for worthy causes—research and development for clean generation technology, for example. Some environmental groups love this idea. But it's hard to argue that the people of LA should be required to support state R&D programs at higher levels than PG&E customers.

The second proposal for issuing permits is even worse. Under this proposal, every utility would be given permits sufficient to cover the average statewide carbon emission level. DWP, whose emissions are above average, would then have to buy permits from PG&E, whose emissions are less than average. Assuming that PG&E didn't simply pocket the dough but gave it to its customers, people in LA would be subsidizing people in Northern California. Even though I would be one of those subsidized, I think it's a foolish idea.

Having finally gotten religion on global warming, it would be wrong for California to make the biggest heathens pay for past sins while others—through no particular virtue of their own—get a free or even a subsidized ride to heaven. The DWP sinners should be given a reasonable amount of time to repent.

Mayor Villaraigosa and the new head of DWP have indeed vowed repentance, promising to have 35 percent of their power generated by renewable resources by 2020, nearly twice the 20 percent mandated in state law. By all indications, they are sincere. But replacing coalfired generation with renewable energy isn't going to be quick, easy or cheap. If Cap'n Trade siphons off more money from LA customers to finance R&D programs or subsidize PG&E, DWP's repentance will be that much harder.

The solution is to make Cap'n Trade wait a bit before giving him control of the ship. In the meantime, the state should establish interim goals that get all utilities to the same emissions levels (so many pounds of carbon emitted per megawatt-hour) in say 10 years. During this interval, payment would be required only if emissions exceeded the interim goals. DWP and the southern munis would still have the biggest job ahead, but their customers wouldn't be further penalized so long as their utilities' keep their promises to clean up their acts.

Alas, I fear that the fanatics touting Cap'n Trade will remain heedless of the consequences of their market fervor. In my opinion, the inequity apparent in the current proposals makes them inherently unstable. Lawyers are already itching to sue, and litigation could last indefinitely.

An outraged contingent of LA legislators could torpedo the entire program.

A political compromise is needed quickly, or Cap'n Trade may be forced to walk the plank.

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