By Robert N. Stavins

State Eyes on the Climate Policy Prize

In May, Senators John Kerry and Joe Lieberman released their American Power Act of 2010, legislative companion to Representatives Henry Waxman and Edward Markey's American Clean Energy and Security Act of 2009. Both proposals feature cap-and-trade systems at their heart, and constitute the best remaining shot at addressing climate change in the near future. But there's an issue brewing that could undermine their effectiveness and drive up their costs.

Government officials from California, New York, and other states are lobbying in Washington to retain their existing state and regional systems for reducing greenhouse gas emissions, even after a federal system comes into force. That would be a mistake — and a potentially expensive one for residents of those states, who could wind up subsidizing the rest of the country. National climate legislation should preempt state and regional cap-and-trade systems. There's no risk, because if federal legislation is not enacted, such preemption will not take effect.

The regional systems — including the Regional Greenhouse Gas Initiative in the Northeast and Assembly Bill 32 in California — seek to limit carbon dioxide by making emissions more costly for firms and individuals. These systems were developed because the federal government was not moving fast enough.

Though the Congress has typically allowed states to act more aggressively on environmental protection, this makes no sense when it comes to climate change policy. For other, localized environmental problems, California or Massachusetts may wish to incur the costs of achieving cleaner air or water within their borders than required by a national threshold. But with climate change, it is impossible for regions, states, or localities to achieve greater protection for their jurisdictions through more ambitious actions.

This is because greenhouse gases uniformly mix in the atmosphere — a unit of carbon dioxide emitted in California contributes just as much to the problem as carbon dioxide emitted in Tennessee. The overall magnitude of damages — and their location — are completely unaffected by the location of emissions. This means that for any individual jurisdiction, the benefits of action will inevitably be less than the costs. (This is the same reason why U.S. federal action on climate change should occur at the same time as other countries take actions to reduce their emissions).

Federal legislation should preempt state and regional cap-and-trade systems

If federal climate policy comes into force, the more stringent California policy will accomplish no additional reductions in greenhouse gases, but simply increase the state's costs and subsidize other parts of the country. This is because under a nationwide cap-and-trade system, any additional emission reductions achieved in California will be offset by fewer reductions in other states.

A national cap-and-trade system — which is needed to address emissions meaningfully and cost-effectively — will undo the effects of a more stringent cap within any state or group of states. RGGI, which covers only electricity generation and which will be less stringent than the federal policy, will be irrelevant once the federal system comes into force.

In principle, a new federal policy could allow states to opt out if they implement a program at least as stringent. But why should states want to opt out? High-cost states will be better off joining the national system to lower their costs. And states that can reduce emissions more cheaply will be net sellers of federal allowances.

This is certainly not to say that there is no possible role for state and local policies. Price signals provided by a national cap-and-trade system are necessary to address climate change at sensible cost, but other market failures call for supplementary policies. Take, for example, the principal-agent problem through which despite higher energy prices, both landlords and tenants lack incentives to make economically efficient energy-conservation investments, such as installing insulation. This problem can be handled by state and local authorities through regionally differentiated building codes and zoning.

But for the core of climate policy — which is carbon pricing — the simplest, cleanest, and best way to avoid unnecessary costs and unnecessary actions is for existing state systems to become part of the federal system. Political leaders across the country would do well to follow the progressive lead of Massachusetts Governor Deval Patrick, who has publicly supported RGGI preemption by a meaningful national program.

California's leaders and those in the Northeast may take great pride in their state and regional climate policies, but if they accomplish their frequently-stated goal — helping to bring about the enactment of a meaningful national climate policy — they will better serve their states and the country by declaring victory and getting out of the way.

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