

Update on U.S. Climate Legislation

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NATIONAL
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POLICY

Overview

- Political context for legislation in the U.S.
 - What has changed?
 - What hasn't changed?
- Key design elements of legislative proposals
- Conclusions

Political context: What has changed in the U.S.?

- Increased public awareness and concern
- Congress controlled by Democrats
- New players at the table: evangelicals, farmers, hunters/fishermen, security hawks
- State efforts build political pressure
- Political tipping point for many industry groups/companies

Political context: What hasn't changed in the U.S.?

- Bush Administration policy
- Regional differences (coal vs. non-coal)
- Competitiveness concerns
- Need 60 votes in Senate
- Learning curve for legislative complexities

Key design elements

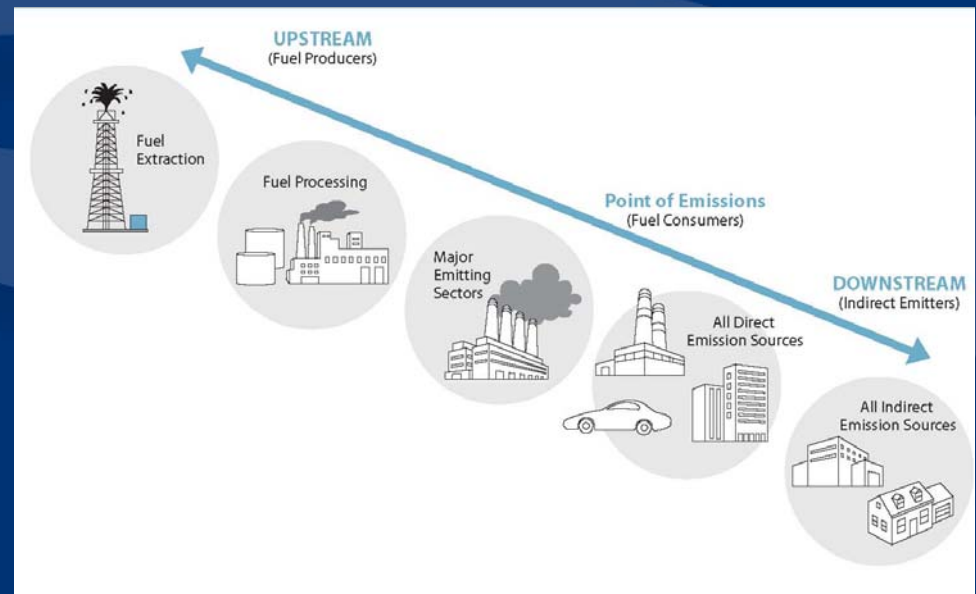
- Targets and timing
- Scope and point of regulation
- Allowance distribution
- Mechanisms to limit price uncertainty (safety valve)
- Additional incentives for R&D, technology deployment
- International and competitiveness issues

Targets and Timing

- Proposals vary widely
 - Bingaman-Specter: Target calculated based on projected reductions in emissions intensity (2.6% annually during Phase I and 3.0% annually during phase II)
 - Lieberman-McCain: Emissions gradually decrease to approximately 1/3 of 2004 levels in 2050.
 - Sanders-Boxer: Emissions reduced to 80% below 1990 levels by 2050

Scope & Point of Regulation

- Some proposals are economy-wide, others are just the power sector
- Economy-wide
 - some have regulation only upstream
 - others are a hybrid of upstream and downstream



Allowance distribution

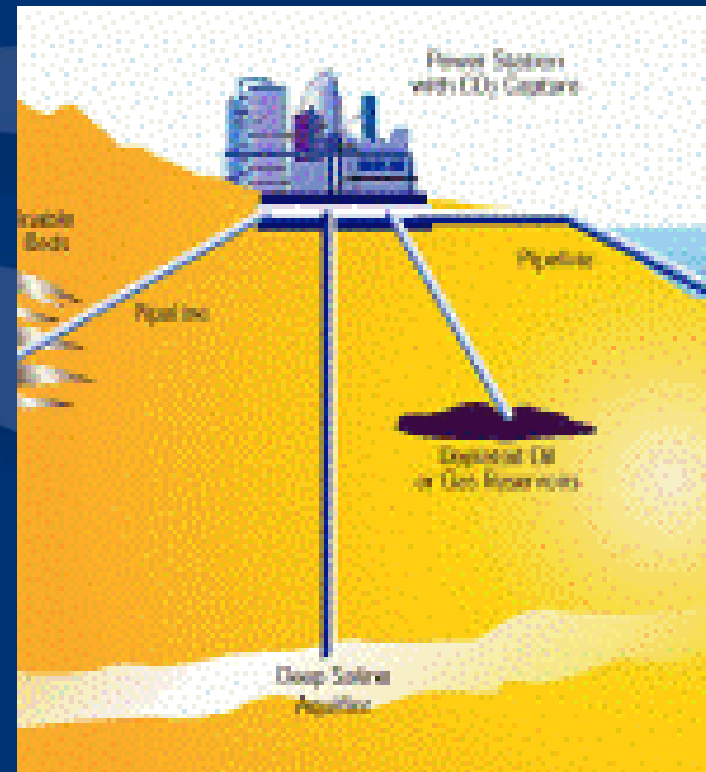
- Some proposals include auctions
 - Bingaman: 10% auction increases to 55% over 30 years
 - McCain-Lieberman: Climate Change Trust fund will auction a portion
- Some proposals use auction proceeds or allowances to compensate groups that aren't at point of regulation
- Some proposals defer to US EPA for allocation

Cost containment

- Proposals use a variety of measures that address different aspects of costs: e.g., overall costs, price certainty, price volatility
- Proposals:
 - Safety valve
 - Borrowing
 - Circuit breaker
 - Offsets, with varying degrees of restrictions
- Some of these mechanisms have implications for linking

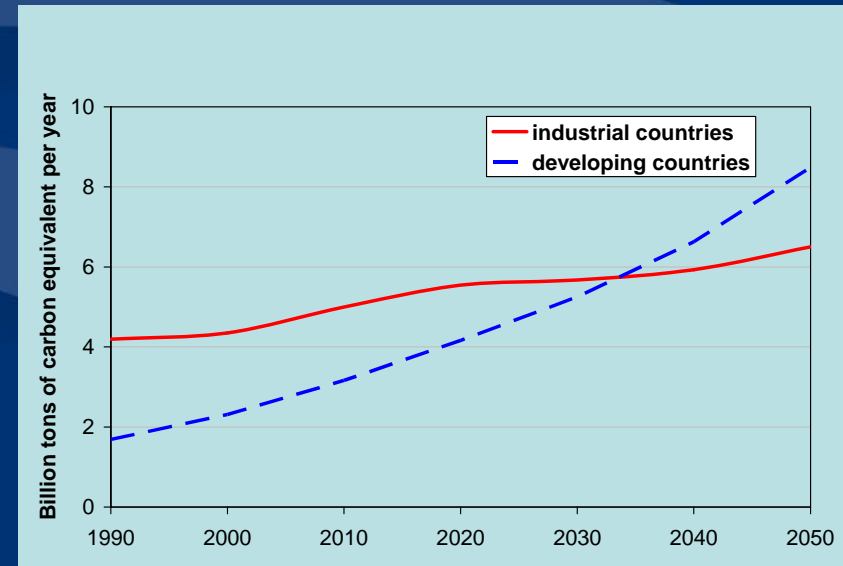
Incentives for R&D, technology deployment

- Most legislative proposals provide additional incentives for R&D, technology deployment
 - Funded through auction revenues or other means



International issues

- Carrots
 - Incentives for developing country projects
- Sticks
 - After first step, further U.S. action would be dependent on actions of large trade partners and emitters
- Even bigger sticks?



Conclusions: Five Things to Watch

- Organized labor
- Key Republican senators
- Influence of state programs
- 2008 Presidential campaign
- Impending economic analysis of bills