World Leadership for an International Problem

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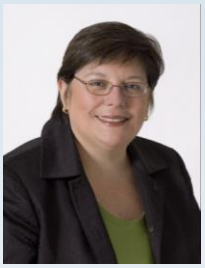

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Ted Gayer presents a compelling analysis of the derailment of a comprehensive climate policy after 2008. While acknowledging that revisiting the issue in the next administration is a long shot, he provides an appealing pathway that couples a price on carbon with fiscal and environmental reform. While I agree with much of his analysis, I would add a note of caution: there will be significant transition costs; some industries and communities will be losers, at least in the short term.

Many of the elements of previous attempts at a comprehensive climate policy that Gayer decries as inefficient were included precisely because of the political imperative to address these costs, and this imperative will not go away. For instance, a carbon price is regressive, and reducing marginal tax rates will not address the impact of these costs on low-income earners. Gayer also points to U.S. industry concerns about the competitiveness impacts of the proposed cap-and-trade bill on the so-called trade-exposed industry. These same concerns will arise from a carbon tax. Instead of demanding free allowances, however, these industries will seek tax exemptions.

I also agree that setting a price on carbon—in Gayer's formula, through a carbon tax—is the best way to spur action on climate change. However, non-price barriers and market failures will still arise and could stall the introduction of new technologies that may founder in the well-recognized "valley of death" between research and development and full commercialization. Government policy and public-private partnerships to address these market failures may still be needed, as will public investment in research and development.

Setting a price on carbon will not only make U.S. action on climate change stronger and more effective, but it will also allow the country to regain some of its leadership role in the international arena of climate change. The United States will be in a stronger position to get concrete results from the new formulas for international cooperation that have evolved over the past few international conferences on climate change. These new formulas aim to spur deeper action by all major greenhouse gas emitters, including those from rapidly industrializing countries like China, which is now the largest source of new emissions.

While negotiations from the United Nations Framework Convention on Climate Change (UNFCCC) have advanced at a glacial pace, there has been movement in recasting the global response so as to recognize that the world is no longer strictly divided between historical emitters and developing countries. The climate change meetings in Copenhagen in 2009 and in Cancun in 2010 resulted in voluntary commitments to reduce emissions from the advanced and rapidly industrializing countries now responsible for the majority of emissions growth. However, these pledges do not go far enough to ensure the internationally agreed-upon goal of maintaining the global temperature rise at no more than 2 degrees Celsius, or 3.6 degrees Fahrenheit, above preindustrial levels.

This was reconfirmed at the 2011 climate change talks in Durban. But in an unexpected move, international climate negotiators agreed to a process to move beyond the voluntary approach agreed to in Cancun to some type of agreement with legal force. The agreed language is intentionally vague, stating that countries should "launch a process to develop a protocol, another legal instrument or an agreed outcome with legal force under the [UNFCCC] applicable to all parties." For the United States, the key phrase is that the outcome should be "applicable to all parties." While this is sure to be disputed in future discussions, the language is another "thin edge of the wedge" toward including China and other new emitters in future agreements. China must be included both to reach

the climate goal and to get political support for more aggressive levels of emission reductions in the United States. Strong action from the next administration would allow it to call for deeper emission reduction pledges by all major emitters, while also joining Europe and countries like Australia that have been carrying the leadership banner in the absence of the United States.

The next administration will also need to lead on policies that help developing countries meet their own emission reduction pledges. It should, in addition, support the costs of adapting to a new climate reality. As part of the agreements at Copenhagen and Cancun, the developed countries pledged $100 billion a year in funding by 2020 to support efforts to mitigate and adapt to climate change in developing countries. Some of the funding would likely be channeled through the Green Climate Fund, which was also agreed upon in Durban.

The sources of this financing are still unclear. While most of the proceeds from a carbon tax would, under Gayer's strategy, be recycled to fund deficit reduction or a reduction in marginal tax rates in the United States, some should go toward U.S. obligations to fund part of the $100 billion global pledge. Given the deep fiscal challenges in the United States, this will of course be resisted, and public funding will likely be tight. This means that finding ways of using public funds to leverage private sector finance, particularly for mitigation, will be critical for the next administration. The Green Climate Fund may be one vehicle to move this agenda forward, but it will not be in place for some time. In addition, developing countries have only a weak appetite for using some money from the Green Climate Fund to catalyze private investment. So the next administration should try to leverage private finance through the Overseas Private Investment Corporation and multilateral vehicles such as the multilateral development banks, which will be more adept at testing new modalities for this purpose.

Finally, the next administration can project leadership even beyond the formal setting of the UNFCCC negotiations through technology partnerships. Partnerships on technology development and deployment—such as those developed under the Clean Energy Ministerial, which brings together ministers from over twenty industrial and rapidly industrializing nations—should continue and broaden out to a wider set of countries, focusing not just on mitigation but also on adaptation.