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Cap And Trade: A System Made For Fraudsters

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Ever since Enron decided that carbon trading would "do more to promote Enron's business than almost any other regulatory initiative," informed observers have been wary of the idea.

Yet the idea of creating a new commodity by capping emissions of greenhouse gases and issuing tradable permits to produce the emissions has gained ground as hysteria over effects of global warming has grown.

Now, two separate investigations have demonstrated why carbon caps and trading are bad ideas, and why they were so attractive to Enron.

In the first, the Congressional Budget Office analyzed the effects of cap and trade on American households. In the European version of the scheme that has been in operation since 2005, the permits are given away to firms. Some businesses are very much in favor of this, because it gives them an opportunity to reap windfall profits, as has happened in Europe.

As the CBO found, "Because most of the cost of the cap would ultimately be borne by consumers, giving away nearly all of the allowances to affected energy producers would mean that the value of the allowances they received would far exceed the cost that they bear." So while energy companies benefit, the consumer suffers higher costs.

If the allowances are sold, individual companies benefit less, as they have to pay for the allowances in the first place. But even if there is some compensation in the form of a reduction in payroll or corporate taxes, most of the population still suffers reduction in household income.

Fraud Revealed

The poorest fifth of the population suffers worst, losing about 3% of its take-home household income. The richest fifth, on the other hand, increase its take-home pay. Only if there is some carbon welfare bureaucracy to administer rebate payments do lower-income families benefit, but that almost triples the cost to the economy as a whole.

All of this, moreover, is the effect of a very modest cut in emissions in the year 2010, certainly not enough to have any impact on warming temperatures. Some sectors of the economy would likely be hit extremely hard — like the 80,000 people who depend on coal mining for their living.

If that weren't enough to suggest that cap and trade would be a bad idea even if it worked as advertised, the Financial Times has now revealed that where it is being tried it is inefficient, fraudulent or both.

The newspaper's investigations have revealed "widespread failings in the new markets for greenhouse gases, suggesting some organizations are paying for emissions reductions that do not take place. Others are making big profits from carbon trading for very small expenditure and in some cases for clean-ups they would have made anyway."

A particularly galling example relates to chemical giant DuPont, which invites people to pay \$4 per ton to reduce emissions from a Kentucky plant, yet the equipment that reduces the gases is actually relatively cheap.

More Emissions?

My organization's investigations earlier in the year revealed DuPont's preferred strategy would realize a return in investment of around 900% for its emissions reductions so far. Yet this isn't new money — it's the consumer and taxpayer that are filling DuPont's pockets for very little in return.

This is one of the reasons why economists such as Ross McKittrick of the University of Guelph in Canada refer to cap and trade schemes as creating a "carbon cartel." Friends of the Earth agrees, calling DuPont's actions "greenwash."

Even worse, though, is the potential for fraud. The Financial Times found there is a risk that people might buy carbon credits for carbon reduction that does not exist.

Another significant risk relates to companies selling the same credits several times over. Large companies such as BP have found it difficult to find enough projects that passed its quality control standards. Individuals and smaller companies are much more vulnerable to the fraudsters and charlatans.

There's even a chance that trading will increase emissions. The Sunday Times of London recently revealed that an Indian factory had made more than \$600 million from selling emissions credits after investing just \$3 million in new equipment that eliminates emissions. With that profit windfall, it will be

building a new factory that will emit a refrigerator gas called HFC-143a, which is over 1,300 times more potent than carbon dioxide as a warming agent. As perverse incentives go, that one's a doozy.

Carbon trading is excellent for the fraudster, good for the robber baron, ineffective for the environment, bad for the economy as a whole and disastrous for the poor. No wonder Enron liked it.

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