

**Cap and No Trade:**  
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The adage that everyone wants to go to heaven but no one wants to die is on display again as the House of Representatives considers a massive 932-page climate change bill, introduced by Reps. Henry Waxman (D-Calif.) and Ed Markey (D-Mass.), that would establish a “cap-and-trade” system for carbon dioxide and other greenhouse gas emissions. Its sponsors tout it as a measure that will keep low and middle-income consumers whole while the U.S. cuts emissions 83% below 2005 levels by 2050 and transitions to a clean energy economy.

Nothing could be further from the truth.

On paper, the Waxman-Markey bill puts a cost on carbon dioxide by imposing a ceiling, or cap, on greenhouse gas emissions and then setting up a market for regulated industries – such as the electric power sector – to buy and sell allowances to pollute under that cap. As the cap is reduced each year, market participants will exchange allowances in a complex auction market. And if you liked what credit default swaps did to our economy, you’re going to love cap-and-trade. Just read Title VIII of the bill (“Additional Market Assurance”), which lets investment banks, hedge funds, and other speculators participate in the cap-and-trade market. And they don’t have emissions to cut; they have commissions to make.

The real hidden catch of the cap-and-trade system, though, is that it will require consumers to pay twice, first for emission allowances and then for the construction of new low- and zero-carbon power plants.

Congressional estimates of government revenues from the sale of cap-and-trade allowances range from the hundreds of billions to trillions of dollars. In fact, contrary to assurances from the bill’s sponsors that utility customers won’t have to pay these costs for the first decade, some coal-dependent utilities will be forced to purchase more than half their allowances when the program is scheduled to begin in 2012. Will these allowances reduce our greenhouse gas emissions? No; that comes when consumers will foot a second bill – for the cost of their utilities either to retrofit coal and gas plants to capture carbon – something that cannot be done today on a commercial scale – or to shut them down and build non-carbon producing nuclear plants and wind farms instead. In fact, to the extent cap-and-trade auctions increase ratepayers’ bills, they will actually impede utilities’ ability to develop a less carbon-intensive infrastructure.

Markets thrive on volatility. Electric utilities, on the other hand, are highly regulated to ensure price stability – not price volatility – for their customers. The Waxman-Markey bill imposes a market-based (read unregulated) trading program on a highly regulated industry that must make enormous long-term and least-cost capital decisions to reduce carbon dioxide emissions. In an unprecedented and unwise fashion, it turns American industry over to the US Environmental

Protection Agency by giving it the authority to change the rules on allowances every five years. Is this sound public and economic policy? I think not.

If Congress wants to achieve 83% reductions in greenhouse gas emissions by 2050, the electricity sector can get there, but there is no need for that first cost. Get rid of auctions, speculation, trading, new Wall Street “products” (yes, the bill allows for credit default swaps and carbon derivatives), and the trillions of dollars in government revenues that may end up being spent on other programs. Get rid of the 12 new advisory boards, committees, and other institutions established under the Waxman-Markey bill. Focus instead on the most efficient and inexpensive way to cut carbon dioxide emissions.

The solution? Keep the cap and remove trading from the equation: Mandate that the industry, over the same 40-year time period, simply limit its emissions to the same levels in the Waxman-Markey bill. This can be accomplished with a clear plan that gives states an option: Either they participate in a cap-and-trade program or they elect an alternative compliance mechanism to reach the same greenhouse gas emission goals by working with their utilities to develop a 40-year program of shutting down aging coal plants, retrofitting them to capture carbon dioxide if the technology becomes available, and/or building zero-carbon energy plants. More importantly, the carbon dioxide reductions in this proposal can be achieved while providing adequate time to plan in order to minimize price shock and economic dislocation. And it is the states, through their public utility commissions – not the federal government – that have both the interest and obligation to manage their citizens’ costs while transitioning to a carbon-free future.

This transformation of our entire electricity sector won’t be cheap, but it will be less expensive than the double cost of a complex cap-and-trade program followed by that same transformation.