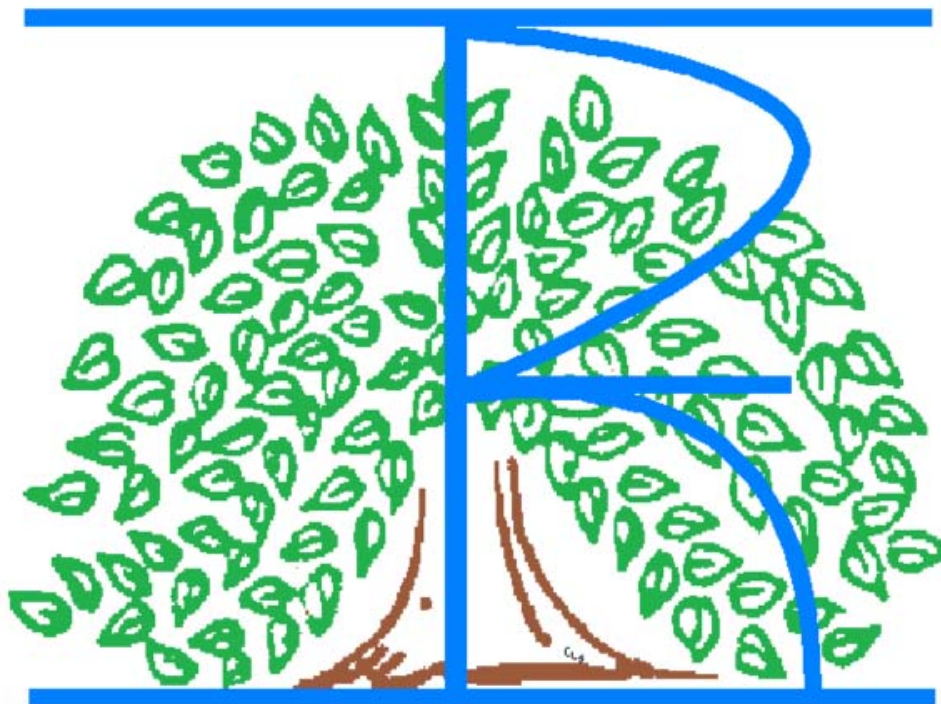


# An Orwellian Guide to Carbon Emissions Trading

Clive L. Spash

January 2010



Independent Research for the Environment (IRE)

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## **Preface**

The material forming this paper was discovered near the furnaces at The Ministry of Truth. The paper is compiled from a series of sentences and paragraphs cut from a larger document. The text forms a series of statements, using examples from Australia, which summarise why carbon emissions trading schemes are fundamentally problematic in ways which cannot be addressed by mere redesign. The arguments put forward form a set of critical viewpoints which counter the standard positions of economists at the Ministry of Plenty.

## **Warning**

This document constitutes material liable to lead to thoughtcrime in those unable to apply doublethink. Please be aware that in reading this document you are putting yourself at risk of investigation by the Thought Police. As all good citizens know, any person having original thoughts or holding unapproved opinions will be subject to punishment (ultimately leading to Room 101 at the Ministry of Love). The author of this material is now an unperson whose recent disappearance indicates they have been duly vaporised by the Thought Police.

***[As you know we have recently been concerned by a document on carbon emissions trading. The control centre applies the highest standards of objective truth for quality control. In that honourable tradition we have made the following corrections.]***

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***[We at the control centre have cut the following text from the Introduction, we hope this meets with Ministry of Truth guidelines.]***

Corporate power is shown to be a major force affecting emissions market operation and design. The potential for manipulation to achieve financial gain, while showing little regard for environmental or social consequences, is evident as markets have extended internationally and via trading offsets.

I conclude that the focus on such markets is creating a distraction from the need for changing human behaviour, institutions and infrastructure.

Interestingly then much attention has been focussed upon the efficient means of control for minimal reductions, rather than effective means for meeting a set of targets necessary to minimise enhancement of the Greenhouse Effect.

The divorce between the assumptions of economic theory and complex reality has been neglected.

A contention of this paper is that the serious problems posed by human induced climatic change soon become lost amongst concerns for designing complex exchange mechanisms to handle the large scale transfer and management of financial assets. Indicative of the complex design the Australian ETS White Paper extends to 820 pages in two volumes including justifications and explanations for specific policy positions.

Complexity means lack of public transparency and considerable room for manipulation of the process by powerful vested interests, while unintended incentives and consequences are likely and little GHG reduction may be achieved. Certainly the EU experience is far from encouraging.

This supports alternative, simpler and more easily controlled and less easily captured regulatory devices (i.e. legislation and taxation) and direct action (e.g. changing infrastructure and institutions).

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***[We at the control centre have cut the following text from the sections on Economic Theory and Practice, we hope this meets with Ministry of Truth guidelines.]***

A lack of realism in terms of market structure, and a total absence of anything in the economic model relating to power in society, mean implicitly adopting the existing political economy without awareness as to the consequences for public policy. These problems have implications for the choice of regulatory approach and what should realistically be expected from an ETS, which is being primarily advocated on grounds of economic efficiency.

Clearly many sectors fail to match the typical textbook characterisation of a polluter as a stationary smoke stack industrial manufacturer with easily identifiable emissions.

The scheme, covering 1000 firms, also has Galbraithian characteristics in proposing large polluters be 'compensated' with free permits while the smaller more numerous competitive fringe face buying theirs at auction. The 'compensation' to polluters on the basis of emissions intensity means that the worst (brown coal-fired power stations) gain the most.

European experience is typical, excessive free permit allocation in some countries and to specific sectors is likely to create competitive distortion between different countries. Governments seem to fear the political consequences of ‘underallocation’ to specific sectors more than those of collective ‘overallocation’ (Grubb, Azar and Persson, 2005: 130).

The transaction costs inherent in an ETS appear to be viewed by some as a source of economic growth, rather than a deadweight loss.

The grounds upon which the ETS is then advocated, as a gain for public welfare, diverges from the reality of who now advocates the scheme due to the potential for private gain. This becomes even clearer once actual ETS design is considered.

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***[We at the control centre have cut the following text from the section on Design of Emissions Trading Schemes, we hope this meets with Ministry of Truth guidelines.]***

The design of carbon trading schemes has involved several controversial aspects which undermine the effectiveness of hoped for pollution control.

Each issue will be shown to involve complexity leading to unrecognised strong uncertainty. The role of vested interests recurs and their power is seen as aimed at achieving ends which have little to do with GHG control.

Identifying and regulating key contributors would be the aim to achieve effective control. The difference under an ETS is the attempt to make GHGs themselves a valuable item of exchange which then implies having a comprehensive accounting system to achieve the claimed efficient outcome. This assumes a level of certainty about sources and sinks which is unattainable.

Rather than accepting such strong uncertainty, and developing social and institutional mechanism whereby it might be addressed, the pretence remains that perfect knowledge can be obtained by more research and idealised carbon accounting can be achieved.



Thus, during the attempts to get Kyoto ratified in 2001 Russia and Japan refused to sign until they received additional carbon credits for their domestic forests (Lohmann, 2006: 53). They succeeded and so effectively increased their carbon sinks on paper.

However, the political preference has been for giving away permits to existing polluters. That countries are prepared to freely allocate pollution rights, while taxing labour and savings, suggests that economic efficiency is not actually a prime consideration.

Yet, some analysts seem unaware of the potential for industry to have a considerable information advantage over government and to use this for their own ends.

Exactly how verification of source emissions and their control is then meant to be effective (let alone efficient) is unclear.

While net global emissions reductions should occur for source offset, where sink offsets are involved the total scale of systemic GHG cycling will be expanded (e.g., via more sources justified by more sinks). Such a process seriously risks enhancing the Greenhouse Effect.

This runs the risk of violating the Kyoto complementarity principle, although the Government is confident there will be domestic reductions (Australian Government, 2008a: 11-8) and these will be significant (Australian Government, 2008b: C-23). Unlimited import means most abatement will occur outside of Australia and the price of CDM and JI credits will set the price of domestic permits (assuming they are not over allocated in the first place).

The potential for exporting emissions control also raises serious concerns over the credibility of offsets.

What becomes clear from across the case studies is a disregard for local communities and their concerns. Those implementing such offset schemes seem to lack the skills to understand and address the problems of people in some of the poorest areas of the world.

This is more damning because of the aforementioned claim of offsets to support sustainable development.

That CDM projects may be positively harmful both socially and environmentally is apparently compensated by obtaining a plentiful supply of cheap permits.

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***[We at the control centre have cut the following text from the Conclusions, we hope this meets with Ministry of Truth guidelines.]***

If the incentives and overall reduction targets of the ETS are weak (as most are likely to be, at least initially), it may cause some individuals to increase their net emissions.

While carbon trading and offset schemes seem set to spread, they so far appear ineffective in terms of actually reducing GHGs. Despite this apparent failure, ETS remain politically popular amongst the industrialised polluters. The public appearance is that action is being undertaken. The reality is that GHGs are increasing and society is avoiding the need for substantive proposals to address the problem of behavioural and structural change.

Perhaps the most worrying aspect of the ETS debate is the way in which an economic model bearing little relationship to political reality is being used to justify the creation of complicated new financial instruments and a major new commodity market. In 2008 the financial sector was in a global crisis having manipulated bad debts and mismanaged its own finances to the point of requiring international banks to seek government bailouts. Yet ETS proposals place a new multi-billion dollar market in the hands of the same people and

organisations. Recent experience illustrates how market players continually seek new ways to profit from adapting institutional rules, and regulators struggle to keep-up.

A key weakness of an ETS compared to alternative policies—taxes or direct regulation—is that an excessive baseline or regulatory loophole in any one nation or sector eliminates the need for genuine reductions elsewhere. The more complex the scheme and the greater its scope, the greater the potential for a weak link. National carbon markets allow poorly regulated sectors to gain, just as international carbon markets are susceptible to rewarding countries with lax regulations and poor enforcement.

Once created, how politicians will cut the market by 80 percent—even within the 40 years they are allowing themselves—is hard to imagine. After all, the reason for emissions trading is that corporations and the technostucture proved too powerful for the political process to establish a tax or direct regulation in the first place.

The framing of the whole issue of human induced climate change is highly important to how it is addressed. There seem two opposing characterisations. On the one hand, financiers, bankers and major polluters argue we must bravely face the new opportunity for markets to innovatively show how the most

intangible of objects can be bought and sold, reaping vast financial gains and stimulating economic growth. On the other hand, society can realise that ever increasing material throughput based upon fossil fuels has led to serious environmental problems, and failed to address social inequity, so that a change in economic structure, institutions and behaviour is now necessary. Clearly the former is dominant and perhaps we must await a financial emissions trading crisis and increasing environmental disasters to reverse that situation.

In Aldous Huxley's *Brave New World*, the drug 'soma' offered inhabitants of a future Earth the means to distract themselves from addressing life's problems while supporting the established social and economic order in the promotion of happiness through hedonic pleasures. Today emissions trading promises a painless way to avoid human induced climate change which will leave the growth economy unaffected in its pursuit of happiness through materialism. The reader is left to judge illusion from reality and the desirability of the society created.

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**[We at the control centre conclude the following are References not to be cited.]**

Australian Government (2008a) Carbon Reduction Scheme: Australia's Low Pollution Future, Volume 1. Canberra, Commonwealth of Australia. 435.

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Lohmann, L. (2006) 'Made in the USA': A short history of carbon trading. *Development Dialogue* **48**(September): 31-70.

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**Long Live BB**

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