**Testimony of**

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# International Aspects of the American Clean Energy and Security Act

Chairman Waxman, Chairman Markey, Ranking Members Barton and Upton, members of the committee, thank you for the opportunity to testify on the international aspects of Waxman-Markey discussion draft of the American Clean Energy and Security Act. My name is Elliot Diringer, and I am the Vice President for International Strategies at the Pew Center on Global Climate Change.

The Pew Center on Global Climate Change is an independent non-profit, non-partisan organization dedicated to advancing practical and effective solutions and policies to address global climate change. Our work is informed by our Business Environmental Leadership Council (BELC), a group of 44 major companies, most in the Fortune 500, that work with the Center to educate opinion leaders on climate change risks, challenges, and solutions. The Pew Center is also a founding member of the U. S. Climate Action Partnership (USCAP) , a coalition of 25 leading businesses and five environmental organizations that have come together to call on the federal government to quickly enact strong national legislation to require significant reductions of greenhouse gas emissions.

For the United States to effectively address climate change, the enactment by Congress of mandatory market-based legislation to significantly reduce U.S. greenhouse gas emissions is of the utmost priority. The Pew Center commends Chairman Waxman and Chairman Markey for significantly advancing this effort with their discussion draft. An essential complement to strong domestic climate legislation is an effective international agreement ensuring that other major economies also contribute their fair share to what must be a global effort. It is in the strong interest of the United States to ensure that domestic climate legislation is fashioned in ways that maximize prospects for such an agreement. In the international negotiations now underway under the Bali Action Plan, the United States will be best able to lead efforts toward an effective global agreement if our domestic legislation:

- Sets a solid foundation for a verifiable international commitment by the United States, and provides means for the U.S. to take additional actions that can encourage strong commitments by others;
- Creates positive incentives for stronger emission reduction actions and commitments by the major emerging economies;
- Dedicates resources to addressing the critical adaptation needs of poor and vulnerable countries;
- Facilitates the linkage of the United States' emissions trading system in a global greenhouse gas market; and
- Includes transitional measures to address the potential competitiveness risks to energy-intensive, trade-exposed industries.

The Pew Center believes that, on the whole, the Waxman-Markey discussion draft would establish a strong foundation for effective U.S. engagement in the global climate effort. In my testimony today, I would like to offer a number of suggestions for strengthening the proposed legislation to better ensure that the very considerable domestic effort it would initiate is maximally leveraged to achieve a fair and effective global climate agreement.

**Foundation for a Verifiable International Commitment**

An effective global response to climate change requires clear and verifiable international commitments by all major greenhouse gas-emitting nations. Countries can be expected to deliver their strongest possible efforts only if they have confidence that their counterparts and competitors are delivering theirs as well. The best means of instilling and maintaining this confidence is a treaty, or a set of international agreements, establishing mutual legal commitments with international accountability. These commitments must be measurable, reportable, and verifiable.

Given the tremendous diversity among the major economies, it is reasonable that their commitments vary not only in stringency but in form as well. In *A Blueprint for Legislative Action*, USCAP recommends a framework that would establish "binding absolute economy-wide reduction targets for developed countries while allowing developing countries a range of binding policy commitments, taking into account national capacities, circumstances, and policy approaches."

The Pew Center believes the Waxman-Markey discussion draft would create a very strong foundation for U.S. participation in such a framework. The emission reduction targets it proposes are ambitious and achievable, and would represent a very credible contribution by the United States toward the ultimate goal of safely stabilizing greenhouse gas concentrations in the atmosphere. In establishing mandatory targets through 2050, the legislation would provide the basis in domestic law for a corresponding commitment, or series of commitments, at the international level. To be meaningful, these international commitments must be legally distinct from, and in addition to, the domestic law in which they are rooted. If countries are merely to pledge national actions – even if these actions are "binding" under domestic law – they are accountable only to themselves. International commitments create international accountability, and the willingness of the United States to assume such a commitment is the only basis on which it can expect the same of other sovereign governments.

The emission targets set under cap-and-trade legislation will fundamentally guide any U.S. targets agreed internationally. The United States will have greater leverage in international negotiations, however, if it has the flexibility to take additional actions that can encourage stronger commitments by others. One way to do this is by committing support for mitigation and adaptation efforts in developing countries, as is discussed below. Another way is through mechanisms facilitating emission reductions outside the United States above and beyond those required under domestic cap-and-trade legislation (i.e., not as international emission offsets used for domestic compliance). The discussion draft would establish one such mechanism by setting aside a portion of emission allowances to support supplemental emission reductions from reduced deforestation in developing countries. We encourage the Committee to consider broadening these provisions to allow the use of allowance value to facilitate other types of mitigation actions in developing countries, or to acquire emission credits meeting U.S. offsetting criteria, and then retire them.

## Incentives for Developing Country Mitigation

To achieve an effective international agreement, the United States and other developed countries must be prepared to provide effective incentives and support for stronger action by the major emerging economies. Under the 1992 U.N. Framework Convention on Climate Change, developed countries committed to provide financial and technological assistance to developing countries. This commitment is underscored in the Bali Action Plan adopted in 2007 by the United States and other Convention parties. In framing negotiations toward a new climate agreement, the Bali plan states that future mitigation actions by developing countries are to be "supported and enabled by technology, financing and capacity-building." Early and sustained action by the United States to deliver this support will greatly enhance prospects for an effective post-2012 agreement. Broadly speaking, this support can be delivered as direct assistance, either bilateral or multilateral, and through market-based mechanisms.

### Public Finance

There is broad recognition that the majority of investment for mitigation will come from private financial flows, in part through greenhouse gas markets, as discussed below. But additional public finance is needed to supplement these market flows. We believe the United States must be prepared to commit such support, and that these incentives will be most effective if: a) the support provided is adequate and predictable; and b) it is structured as a phased-in program providing some immediate assistance for capacity-building and technology deployment, and greater support for technology deployment once countries commit to effective climate policies. This assistance should be provided through bilateral programs and multilateral mechanisms, including the Clean Technology Fund recently established at the World Bank.

We believe the International Clean Technology Fund proposed in the discussion draft could be an important element of an effective funding strategy. It would allow support to be delivered through both bilateral programs and multilateral mechanisms, and would establish eligibility criteria providing a clear incentive for developing countries to adopt and commit to effective climate mitigation policies. However, we would recommend strengthening the provision in several respects.

First, it is critical that a clear, reliable, and predictable source of revenue be designated for these purposes. We believe the legislation should authorize immediate appropriations for two purposes: a) to support capacity-building activities, as discussed further below; and b) to fulfill the United States' pledge to help fund the World Bank's new Clean Technology Fund. These efforts would immediately demonstrate the United States' commitment to support developing countries and would help position those countries to undertake stronger efforts. For the longer term, the legislation should designate a portion of allowance value to provide sustained support for technology deployment. As proposed in the discussion draft, this further support should be conditioned on a recipient countries' ratification of an effective international climate agreement, or on the President's determination that it is undertaking nationally appropriate mitigation activities. The funds generated through this portion of allowance value could be held in reserve until such time as these eligibility criteria are met.

Second, we believe as a general matter that support for technology deployment should be technology-neutral, so that each dollar invested can achieve maximum return in emissions reduction. We are concerned that, as written, the discussion draft may exclude funding for more efficient coal-fired electrical generating facilities. Given the very strong likelihood that many countries will continue to rely on coal as a major energy source, and will continue building substantial new coal-fired generating capacity, we favor using technology support to ensure that these new facilities are as efficient, and least GHG-intensive, as possible. Eligibility criteria should require that supported facilities deploy the best available combustion technologies and achieve substantial efficiency improvements and emission reductions beyond business as usual.

Third, we believe the legislation should provide explicit and immediate support for a range of capacity-building activities in developing countries. These should include:

- Emissions measurement – Strengthening capacity to accurately monitor and measure GHG emissions in key sectors and, ultimately, economy-wide as a basis for policy development, crediting and other market-based responses, and assessing progress.
- Economic modeling – Strengthening capacity to project emissions and economic conditions under different scenarios, and to evaluate the costs and emission reduction potentials of alternative mitigation approaches.
- Policy development – Strengthening capacity to design, implement, and enforce nationally appropriate policies that would contribute to emission reduction and could form the basis of international commitments.
- Technology assessment – Strengthening capacity to assess available mitigation technologies and to identify those best suited to national circumstance.

Market-based Incentives

Access to the U.S. greenhouse gas market can provide another important incentive for stronger action by developing countries. The Pew Center strongly supports the use of international emissions offsets, both as an incentive for developing country action and as a mechanism to contain costs in a U.S. cap-and-trade system. EPA's recent modeling analysis of the Waxman-Markey discussion draft found that the exclusion of international offsets could increase allowance prices by 96 percent.

USCAP recommends allowing up to 1.5 billion tons of international offsets per year within the cap-and-trade system. Criteria must be established for all offsets, domestic and international, to ensure they are environmentally additional, verifiable, permanent, measurable, and enforceable. In the case of international offsets, USCAP recommends that EPA be directed to establish a process to evaluate and approve proposed offsets, and that over time developing countries be required accept climate mitigation commitments to remain eligible for GHG crediting. In addition, USCAP favors the use of emission offsets from reduced deforestation to supply a strategic emissions reserve available to covered entities to help reduce compliance costs. The overall aim of these recommendations is to encourage developing countries to move rapidly to curb their emissions, while providing verifiable emission offsets to help contain costs for U.S. emitters.

Although the discussion draft allows fewer offsets (domestic and international) than favored by USCAP, the Pew Center believes that it is in many ways consistent with these recommendations. Its offsetting provisions would provide a strong positive incentive for developing countries to undertake stronger efforts and to assume reasonable climate commitments. By allowing crediting on a sectoral basis, the proposed legislation would help mobilize larger-scale reduction efforts in key sectors, while the provisions on reduced deforestation would establish the safeguards needed to ensure the integrity of forest-based offsets.

Importantly, the draft would allow for the recognition of credits issued by an international body under the UN Framework Convention, or a new climate agreement, provided they meet U.S. offsetting criteria. A well-functioning international crediting mechanism is important to the efficiency of the global greenhouse gas market. By potentially allowing offsets from an international mechanism, Congress would help position the United States to strongly influence the restructuring of the existing Clean Development Mechanism or the design of a successor mechanism.

## Supporting Adaptation Efforts

As noted in the discussion draft, the United States committed under the UN Framework Convention and the Bali Action Plan to provide "new and additional" resources to help poor and vulnerable countries adapt to climate change, and such assistance must be predictable and sustainable. Consensus among governments on the appropriate means and levels of adaptation support will be critical to achieving a comprehensive climate agreement.

Conceptually, the discussion draft would provide a sound basis for significantly enhanced U.S. support for adaptation efforts in the least developed countries, small island states, and other especially vulnerable countries. It would establish a stronger framework for delivering direct bilateral assistance, and importantly, it would reserve 40 percent to 60 percent of the support available for U.S. contributions to any international adaptation funds established or designated under a new climate agreement.

To be effective, and to help secure a strong climate agreement, the legislation must establish a clear, predictable, and sustained source of funding for these international adaptation efforts. The Pew Center strongly supports designating an appropriate portion of allowance value for these purposes.

**Linking Trading Systems**

Emission reduction efforts in the United States and elsewhere will be more cost-effective if linked through a global greenhouse gas market. It is critical, therefore, that domestic U.S. legislation anticipates and facilitates the linkage of a U.S. cap-and-trade system to existing and emerging market-based systems in other countries and regions, provided they are of comparable environmental integrity.

The discussion draft appears to lay the necessary foundation for linkage to other market-based systems. It would establish sound criteria for determining qualifying programs, including the requirement of absolute emission limits, and of comparable stringency with respect to compliance, enforcement, and offset quality. By also allowing the recognition of allowances from programs establishing sectoral targets, the draft would provide another strong incentive for stronger efforts by countries not yet prepared to take on economy-wide targets.

**Addressing Competitiveness Concerns**

In recent testimony before the Energy and Environment Subcommittee, Pew Center President Eileen Claussen outlined our views and recommendations concerning potential competitiveness impacts on trade-exposed, energy intensive industries.[1] In brief, our analysis indicates that these potential competitiveness impacts are modest and manageable through a range of policy options.

We believe that in the long term, concerns over competitiveness and associated emissions leakage are best addressed through effective international climate commitments, and that the overriding objective should therefore be to facilitate their establishment. In the interim, we favor the use of transitional measures such as output-based emission allocations or rebates to vulnerable industries, and transition assistance to affected workers and communities. We strongly discourage the use of unilateral trade measures. Such measures

[1] "Competitiveness and Climate Policy: Avoiding Leakage of Jobs and Emissions," Testimony of Hon. Eileen Claussen, President, Pew Center on Global Climate Change, submitted to the Energy and Environment Subcommittee, Energy and Commerce Committee, U. S. House of Representatives, March 18, 2009,

would not fully counter competitiveness risks; as they would apply only to imports to the United States, they would not help “level the playing field” in the larger global market where U.S. producers may face greater competition from foreign producers. Further, they risk retaliatory trade measures, and put climate relations on the path to confrontation rather than cooperation.

On the whole, we believe the discussion draft takes a very sound approach to addressing competitiveness concerns. As we favor, it relies primarily on an output-based approach to compensate firms in qualifying sectors for the direct and indirect costs of greenhouse gas regulation. Also consistent with our recommendations, the draft would: structure the compensation so as to provide an incentive for investments in energy efficiency; phase down the level of compensation over time; provide for Presidential review to slow this phase-down if necessary; and end compensation if 70 percent of global output is subject to commensurate greenhouse gas regulation. We believe this approach addresses the transitional competitiveness concerns likely to arise under a mandatory cap-and-trade program, while maintaining the environmental integrity of the program and providing an ongoing incentive for producers to improve their GHG performance.

Critically, the draft contemplates the use of trade measures against other countries only as a last resort if the President finds that, despite the rebate program, regulatory costs have harmed production or employment by energy-intensive U.S. manufacturers, or that emissions from competitors in countries without commensurate climate obligations have increased. This approach preserves trade measures as an option, but defers their use to allow a reasonable period to assess the efficacy of the rebate program and to achieve effective international agreements.

In conclusion, the Pew Center believes that the Waxman-Markey discussion draft would provide the foundation for a strong U.S. contribution to the global climate effort, and that with further refinements, the proposed legislation would well position the United States to lead efforts toward an equitable and effective international agreement. We appreciate the opportunity to provide our input on the discussion draft, and look forward to working with the Subcommittee and the Committee as this critical legislation moves forward.