

Political climate change

Developments in Washington, in states throughout the country and in the business community show the US may be approaching a tipping point on the climate-change issue, writes Truman Semans, director for markets and business strategy at the Pew Center on Global Climate Change

ENACTMENT of greenhouse-gas (GHG) regulation in the US may be a few years away, given prevailing views in the White House and parts of Congress. But the process of determining the shape of future climate-related regulations in the US is under way – at least in a handful of influential states.

These early steps could affect the timing and distribution of enormous economic costs and benefits for decades to come. The debate within companies and other organisations with much at stake should shift from “should we act?” to “how best to act?”. Those that engage constructively now are likely to hold some of the most influential seats at the table.

Turnaround in the US Senate

The final Energy Bill contains several provisions related to climate. It retained aspects of amendments offered by Senator Chuck Hagel (Republican, Nebraska) that promote voluntary deployment of GHG intensity-reducing technologies in the US and developing countries. More meaningful elements include: streamlined approval paths for liquefied natural gas terminals; improved government standards to reduce GHG impacts of products and buildings; several billion dollars of federal aid to support deployment of clean-coal technology; new nuclear power generation; hybrids and other efficient vehicles; energy efficiency; and renewable energy, ranging from ethanol and other bio-fuels to wind and solar.

These technology-push items will have little effect in the absence of regulated GHG limits. Yet that significant climate provisions survived the process of reconciling versions of the bill shows attitudes are changing in Congress. This is certainly true in the Republican-controlled Senate and perhaps even in the House, which has strongly resisted action on climate for several years.

The Senate took a significant step forward on climate in preparing its version of the bill. A solid majority supported a resolution stating “that Congress should enact a national mandatory, market-based programme to slow, stop and reverse growth of these emissions”. Although resolutions of this type are not legally binding, they can significantly influence future decisions by Congress and the White House. For example, the Byrd-Hagel resolution established parameters for what the Senate would accept regarding international action on the issue. The latest resolution shows the Senate is ready for the US to move towards regulating GHG emissions.

Perhaps more importantly, the powerful chairman of the Senate Energy Committee, Pete Domenici (Republican, New Mexico), began hearings in July on proposed legislation to establish a GHG cap-and-trade programme. The bill, authored by Senator Jeff Bingaman (Democrat, New Mexico) and based on recommendations of the National Commission on Energy Policy (NCEP), would establish an annual cap on emissions, although its “safety valve” would allow emitters to exceed caps if emission allowance prices top \$7 a tonne.

Some are concerned that the Bingaman bill would not reduce emissions, but only slow their growth and that this will not solve the problem – a view the Pew Center shares. Nevertheless, the NCEP report has opened the valve for serious discussion in Congress and many of its recommendations will form a basis for debate in coming months, including during hearings around the Bingaman bill.

The Climate Stewardship Act developed by Senators John McCain (Republican, Arizona) and Joseph Lieberman (Democrat, Connecticut) would cap emissions, rather than only slow down their growth. Although it did not receive majority support in Energy Bill debate and lost some votes because of revisions supporting nuclear power, the bill will probably remain on the table and influence whatever climate regulation emerges.

Pressure from the states

Despite the modest outcomes on climate of this summer’s G8 summit, one driver of change in Washington has been the sense of falling behind the European Union and other Kyoto countries taking a lead on the issue. There is rising awareness that the US needs at least to re-engage effectively in the global negotiating process, to chart the course for post-2012. Greater pressure for Washington to get serious about climate comes from state-level and industry leadership.

Nearly every major federal environmental law had a state or local precedent. Action in California and other states not only accelerated the timing of federal laws but also furnished elements of both sets of regulation. History is likely to repeat itself as GHG regulation develops. Growing activity on climate outside Washington, leaving Washington increasingly out of step, perhaps helped motivate the Senate’s move forwards.

A total of 21 states and the District of Columbia have adopted renewable energy mandates. Nine northeastern governors are designing a carbon-dioxide (CO₂) cap-and-trade programme for power plants.

California’s Republican governor, Arnold Schwarzenegger, has announced statewide goals to reduce GHG emissions, complementing the state’s groundbreaking GHG standards for vehicles. New Mexico governor Bill Richardson has also set targets and joined Schwarzenegger in leading the Western Governor’s Association to agree on a goal of adding 30 gigawatts of renewable generating capacity by 2015. Climate-related legislation is pending in many other states.

State and regional activity will drive action on climate in several ways. Aside from generally encouraging proponents, it will test new approaches, force difficult decisions about allocating gains and burdens among industries and parts of society, and help clarify the costs and benefits of regulation. In addition, the patchwork of regulation that state and regional action creates presents increasingly serious obstacles for businesses. These problems are already motivating some major corporations to call for greater certainty and consistency through national regulation and history indicates this chorus will grow.

The longer we postpone acting on the issue, the more extreme the measures might have to be to deal with the issue in the future

In a recent article in the *Financial Times*, GE’s chief executive officer (CEO), Jeffrey Immelt, wrote: “All that we ask for – and this will allow us to grow as a healthy, responsible company – is consistency. Policies that commit to market-based approaches will drive innovation and lead to environmental improvements.” This is just one of several recent instances in which influential new business leadership has emerged in US.

HP’s Mark Hurd and Ford’s William Clay Ford joined over 20 global corporate leaders in calling publicly for George Bush and the G8 to set climate-stabilisation targets and adopt cap-and-trade or other market-based mechanisms. Jim Rogers, CEO of Cinergy, who will head one of the world’s largest utilities when Cinergy and Duke Energy merge, has taken on a powerful advocacy role, despite his firm’s reliance on coal for fuel.

Asked by a radio commentator in April if he could live with more government regulation, Rogers said: “The longer we postpone acting on the issue, the more extreme the measures might have to be to deal with the issue in the future.” In June, four other

Fortune 500 companies – Baxter, DuPont, UTC and Whirlpool – joined Rogers in providing testimony on climate to the House Science Committee of Congress with the basic message that they are living with carbon limits outside the US, already reducing emissions in the US and that their businesses are thriving nonetheless.

Major US financial players are also moving ahead. Bank of America has pledged to reduce GHG emissions by 9% between 2004 and 2009 and trains its bankers to assess climate risk in its financings. JP Morgan Chase has called for “policy dialogue to advocate that the US government adopt a market-based national policy on GHG emissions, which includes all sources of emissions and is fair”. A UN conference in June drew institutional investors representing over \$3 trillion in assets who take into account climate-related risk and clean-energy business opportunities when investing.

The unifying theme, as more and more companies realise, is that GHG regulation is inevitable and that it makes sense in the interest of sound business planning and corporate governance for the US to adopt efficient, mandatory national policies accounting fairly for all sectors.

The business case is, therefore, increasingly compelling for industries that have much at stake to integrate climate policies into their business. For example, it makes

sense for energy firms to implement programmes to cut their own emissions. John Browne, BP’s CEO, says “emissions can be reduced at a very low cost simply by reducing waste and inefficiencies. We did that in BP and we made money in the process.”

Both BP and Shell have developed mechanisms for mitigation that help the best opportunities compete successfully against standard capital projects, such as internal cap-and-trade systems, investment pools especially designated for GHG reducing projects and shadow pricing, in which project evaluations are adjusted to reflect the projected environmental cost of emissions. Shell has reduced emissions by 9% below 1990 levels, while BP has reduced them by over 15% in the past six years.

The second direction is for companies to begin adapting to the physical, regulatory, and market changes that lie ahead, such as increased storm activity, higher energy prices or greater demand for energy-efficient equipment. Physical adaptation may require major redesign of infrastructure for extraction and transport of oil and gas, as well as new approaches to risk management. In terms of regulatory and market changes, climate may benefit oil and gas production by making CO₂-injection for enhanced recovery cost effective for many fields, because annual carbon sequestration requirements from coal combustion could reach 10bn

tonnes of CO₂ a year. Other opportunities range from cleaner fossil fuels and lubricants to renewable energy, hydrogen production and emissions trading. At the highest level, companies need to consider whether in the future they will be dedicated to petroleum or involved in a wider range of energy activities.

Working together

With regard to policy, the developments in Washington signal that the time has come for the energy industry to open up public dialogue on designing market-based approaches including cap-and-trade schemes. One critical issue needing input from petroleum companies, working together with the auto industry and its suppliers, is how to deal effectively and efficiently with cutting emissions from transportation.

Independent groups such as the Pew Center on Global Climate Change, with its Business Environmental Leadership Council, which includes BP, Shell, Sunoco, and Toyota, as well as important suppliers such as Alcoa and Alcan, can help companies set up dialogues between industries and work with members of Congress on legislation. It also makes sense to steer petroleum industry associations, which to date have mainly worked to block progress on climate, towards a more positive role. Becoming a part of the solution will let the industry mind its interests better than trying to delay the inevitable. □