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*CONGRESSIONAL TESTIMONY*

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**The European Experience with Cap  
and Trade**

**Testimony before  
Committee on Foreign Relations  
United States Senate**

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My name is Ben Lieberman, and I am the Senior Policy Analyst for Energy and Environment in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation. The views I express in this testimony are my own, and should not be construed as representing any official position of The Heritage Foundation.

I would like to thank the Subcommittee for European Affairs for inviting me to testify. What the Subcommittee is doing today is very important but was largely missing from the House global warming debate, and that is taking a look at the real world experience in Europe with the Kyoto Protocol and the cap and trade approach to reducing emissions of carbon dioxide and other greenhouse gases. Notwithstanding questions about the seriousness of man-made global warming, the Heritage Foundation is very concerned about the costs of this approach, which was embodied in the Waxman-Markey bill. Our analysis of that bill estimates higher energy and other costs for a household of four averaging nearly \$3,000 annually and overall lost gross domestic product of \$393 billion annually and \$9.4 trillion cumulatively by 2035.<sup>1</sup> We also estimate over a million lost jobs. And even assuming it works to reduce emissions, Waxman-Markey has been estimated by climate scientist Chip Knappenberger to reduce the earth's future temperature by no more than 0.2 degrees C by 2100.<sup>2</sup>

But will it even work? Will it even reduce emissions enough to accomplish that 0.2 degrees? The European experience with cap and trade strongly urges caution. The Washington Post recently described it as "Exhibit A" of what not to do on climate, and

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<sup>1</sup> William W. Beach, et al., "Son of Waxman-Markey: More Politics Makes for a More Costly Bill," Heritage Foundation Web Memorandum No. 2450, June 16, 2009, at <http://www.heritage.org/Research/EnergyandEnvironment/wm2450.cfm>.

<sup>2</sup> Chip Knappenberger, "Why Waxman-Markey Is Not A Climate Bill," June 29, 2009, at <http://masterresource.org/?p=3507#more-3507>.

for good reason.<sup>3</sup> The Senate would be wise to take a close look at Europe's track record with the 1997 Kyoto Protocol and the Emissions Trading Scheme adopted in 2005.

Most western European nations are currently learning, the hard way, that ratcheting down carbon dioxide emissions in this manner is very difficult and expensive. In fact, most of these nations (not to mention other Kyoto Protocol signatories like Canada and Japan) have not been reducing their emissions over the past several years, though it should be noted that they are doing so now but only as a result of the recent recession.<sup>4</sup> Indeed, several were seeing faster increases since 2000 than those in the U.S., which has not been subject to such a scheme.<sup>5</sup>

And despite lofty rhetoric from many European nations about setting even more stringent future standards, we also see signs of fracturing in their cap and trade coalition. From German automakers to Italian steelmakers to nations that still rely upon coal for a substantial percentage of electric generation, discussions about exclusions and delays and handouts are now very much a part of the debate in every European Union meeting on climate. The Russian cutoff of natural gas to Europe was also a reminder of the geopolitical risks of discouraging domestic coal under cap and trade.

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<sup>3</sup> "Climate Change Solutions Sen. Boxer is open to everything -- except what might work best," *The Washington Post*, February 16, 2009 at <http://www.washingtonpost.com/wp-dyn/content/article/2009/02/15/AR2009021501425.html>

<sup>4</sup> Press Release, "UNFCCC: Rising industrialized countries emissions underscores urgent need for political action on climate change," United Nations, November 16, 2008, at [http://unfccc.int/files/press/news\\_room/press\\_releases\\_and\\_advisories/application/pdf/081117\\_ghg\\_press\\_release.pdf](http://unfccc.int/files/press/news_room/press_releases_and_advisories/application/pdf/081117_ghg_press_release.pdf).

<sup>5</sup> Energy Information Administration, "International Energy Annual 2006," Table H.1co2: World Carbon Dioxide Emissions from the Consumption and Flaring of Fossil Fuels, 1980-2006, at <http://www.eia.doe.gov/pub/international/iealf/tableh1co2.xls> (December 11, 2008).

We have also seen examples of fraud and unfairness in the process.<sup>6</sup> Given the similar politics here, where big businesses have lobbied for free allocations much more effectively than the little guys –consumers, homeowners, small business owners, farmers – it is quite likely that the inequities would appear here as well.

The reason for the failure of carbon cap and trade is simple – reducing carbon dioxide from the existing installed base of energy producing and using equipment and vehicles is prohibitively expensive, and that isn't likely to change any time soon. Many nations committed to emissions reductions under the Kyoto Protocol are going to miss the targets (unless the recession lingers) and any talk of tougher targets is empty rhetoric.

The record in Europe suggests that the Heritage Foundation and others predicting high costs for Waxman-Markey are right, while those predicting postage stamp per day costs are wrong. If it really were postage stamp cheap, Europe's emissions reduction record would be much better, and there would be no need to make excuses for it.

Further, a study by the Taxpayers Alliance estimates the cost of various green taxes in the UK is up to \$1200 per household per year, and that to achieve only a fraction of what Waxman-Markey requires.<sup>7</sup> Again, this points to very high household costs for Waxman-Markey.

To the limited extent European nations have reduced emissions below business-as-usual-levels, it has hurt their economies. Almost every western European nation has had higher unemployment and energy costs than America, and a weaker overall economy, even as emissions were still rising. Far from seeing evidence of the bright

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<sup>6</sup> Open Europe, "Europe's Dirty Secret: Why the EU Emissions Trading Scheme isn't Working," August 2007, at <http://www.openeurope.org.uk/research/etsp2.pdf>.

<sup>7</sup> Mathew Sinclair, "The Burden of Green Taxes," Taxpayers Alliance, August 2008, at [http://tpa.typepad.com/home/files/the\\_burden\\_of\\_green\\_taxes.pdf](http://tpa.typepad.com/home/files/the_burden_of_green_taxes.pdf).

new green economy some are now promising, we are seeing that cap and trade has contributed to the harm. For example, Spain has been cited repeatedly as the example of a successful clean energy economy and source of green jobs, but it is rarely mentioned that Spain currently has 18 percent unemployment.

There are reasons that may explain this seemingly counterintuitive result that cap and trade is not only the wrong approach for the economy but is also the wrong approach for reducing greenhouse gas emissions. Any sensible approach to global warming has to center on technological innovation as it applies to energy production and use. Breakthroughs such as ways to produce energy economically with low or no carbon dioxide emissions or improvements in energy efficiency – these make good sense irrespective of global warming.<sup>8</sup>

Innovation is really what we really want. And we know from long experience that free economies innovate better than centrally planned ones. But cap and trade introduces a significant element of central planning and thus stifles innovation. We also know that strong economies innovate better than weak ones, but cap and trade weakens economies. Perhaps most importantly, stable economies innovate better than unstable ones, especially for something like energy where the investments often run into the billions of dollars and the payoffs play out over decades. But cap and trade adds a significant element of instability, which we have seen in Europe with wild swings in the price of carbon allowances, and energy companies less interested in long-term investment and more interested in short-term gaming of the system.

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<sup>8</sup> Iain Murray, and H. Sterling Burnett, “10 Cool Global Warming Policies,” National Center for Policy Analysis, June 2009, pp. 20-22, at <http://www.ncpa.org/pdfs/st321.pdf>.

In conclusion, the economic realities of cap and trade are becoming clear in Europe. If we adopt a similar approach here, expect considerable economic pain for minimal environmental gain.

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