Center for Clean Air Policy

Dialogue. Insight. Solutions.

THE "SAFE MARKETS DEVELOPMENT APPROACH" TO CAP-AND-TRADE

CONTAINS COSTS, ELIMINATES SPECULATION, MEETS EMISSION GOALS

An Overview

Developed by the Center for Clean Air Policy, the Safe Markets Development Approach responds to concerns about the possibility of volatile emission allowance prices, market manipulation and speculators interfering with new carbon markets. During Phase I (2012 through 2019) of a cap-and-trade program, the Approach acts as "training wheels" for the development of an allowance market. It creates predictable allowance prices and meets critical 2020 emissions goals. The Approach also enforces a cumulative emissions budget for the period while allowing some fluctuation in annual emissions as needed to stabilize allowance prices. Beginning in 2020, Phase II moves to a more traditional cap-and-trade program with annual emissions caps.

HOW THE SAFE MARKET DEVELOPMENT APPROACH WORKS

- **Setting the Price Path**. Each year of Phase I, an independent Board establishes a forecast path for allowance prices for the entire Phase I period with the goal of meeting annual and cumulative emissions targets. Four quarterly auctions are held each year and are designed to maintain this price on average.
- **Reviewing Performance and Adjusting the Price Path Annually.** Each year the Board reviews emissions performance for the previous year and adjusts its price projections if needed to ensure that the gradual trend path of emissions reductions is in line to achieve the 2020 emission target.

BENEFITS OF THE SAFE MARKET DEVELOPMENT APPROACH

- **Creates Price Predictability.** By publishing a gradually rising path for allowance prices, the Board provides regulated entities with greater confidence in the returns they would earn on greenhouse gas (GHG) mitigation investments. The predictability and stability of the price will help sustain technology investments needed to meet environmental goals.
- **Assures Environmental Integrity**. The independent Board is composed of experts whose mandate is to establish the allowance price necessary to achieve the annual and cumulative emissions targets. The cumulative emissions goal for Phase I is enforceable. In the unlikely event that cumulative emissions exceed expectations at the end of Phase I, the difference is made up by reducing the annual emissions targets over the next decade to maintain the necessary overall emissions reductions.
- **Prevents Allowance Price Booms and Busts and Market Manipulation.** The Approach prevents allowance prices from rising too high or dropping too low, virtually eliminating, opportunities for speculators, traders or investors to manipulate the market.
- **Ensures Transparency.** Transparency of the Board's activities is ensured through required annual testimony before Congress regarding price projections and the progress toward achieving the 2020 emission goal.
- **Gives New Market Participants and Regulators Time to Adjust.** The Approach provides confidence in the early years of the program when there are many new market participants and untested regulatory mechanisms. It also provides time for government agencies to test their monitoring, surveillance and enforcement mechanisms.

The Approach is discussed in detail in a background paper titled "Preventing Market Disruptions in Cap-and-Trade Programs". To read this paper and to find the latest news and information on the Safe Markets Development Approach, please visit http://ccap.org/safe-markets.html or contact Director of Policy Research, William Whitesell, at wwhitesell@ccap.org or Director of Legislative Affairs, Marty Spitzer, at mspitzer@ccap.org.

Since 1985, CCAP has been a recognized world leader in climate and air quality policy and is the only independent, non profit think-tank working exclusively on those issues at the local, national and international levels. Headquartered in Washington, D.C., CCAP helps policy-makers around the world to develop, promote and implement innovative, market-based solutions to major climate, air quality and energy problems that balance both environmental and economic interests. More information about CCAP can be found at www.ccap.org.