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Chairman Harkin, Ranking Member Chambliss and members of the Senate Agriculture Committee, thank you for the opportunity to testify today. I am pleased to be here on behalf of Bipartisan Policy Center (BPC), which was founded by four former majority leaders, Senators Tom Daschle, Bob Dole, Howard Baker and George Mitchell. BPC was created to help provide the motivation and infrastructure to forge bipartisan consensus we believe is necessary for durable change. BPC hosts two active projects that bear directly on the Committee's inquiry here today.

The first initiative, the National Commission on Energy Policy (NCEP) was formed in 2001 to bring together a diverse group of stakeholder to address critical energy policy issues. NCEP has worked diligently to design climate policy solutions that address the legitimate concerns that business, organized labor and energy intensive industries like agriculture have about mandatory limits on greenhouse gas emissions. We believe that it is possible to design an effective economy-wide cap and trade program that encourages innovation and investment while limiting program costs harmful price volatility. In my testimony, I will be drawing upon the work of NCEP to identify opportunities to mitigate the concerns that agricultural producers have expressed about the increased costs of energy under a cap and trade regime.

The second initiative, the 21st Century Agricultural Policy Project, was led by former U.S. Senate Majority Leaders and long-time members of this committee, Senators Bob Dole and Tom Daschle. The 21st Century Agriculture Policy Project recognized that this rapidly changing economic landscape for agriculture calls for a more expansive and creative approach to national farm policy. In 2006 and 2007, the senators worked closely with farmers, ranchers, and other stakeholders to forge bipartisan consensus around a new agenda for U.S. farm policy in the 21st century. In 2007, Daschle and Dole released a report on the challenges and opportunities for agriculture in the transition toward a low carbon economy entitled "Competing and Succeeding in the 21st Century: New Markets for American Agriculture." The Senators concluded that a national cap and trade program could provide significant new market opportunities and additional income benefits to American agriculture.

The BPC believes strongly that action must be taken to address climate change and that urgency must take precedence over competing views of perfection. We recognize that farmers are highly-sophisticated when it comes to managing risk and do not suggest that the near-term risks of a changing climate justify actions that would imperil the basic economic proposition for domestic agriculture. At the same time, there is no question that left unchecked, climate change will compound the risks to U.S. and global agriculture. The BPC recently sponsored a study by a group of former military leaders about the national security challenges posed by climate change. These military leaders concluded that in the context of our national security, climate change is a "threat multiplier." I believe that the same is true for our agricultural and forest production. As

Bruce Babcock of Iowa State University recently wrote in his paper “Costs and Benefits to Agriculture from Climate Change Policy,” (Iowa Ag Review, Summer 2009, Vol. 15, No. 3):

“Given the likelihood of modest costs and benefits from a cap and trade system, perhaps agriculture should look at whether a cap and trade policy will change growing conditions for the better or worse as a deciding factor in whether to support a change in policy. Given how much irrigated agriculture in the West relies on consistent snowfall and Corn Belt agriculture relies on warm summers and abundant rainfall, any disruptive change in the climate will have a far greater impact on livelihoods than will the price of carbon.”

Most observers recognize that farmers, ranchers, and foresters can play a significant role in solving our climate problem. EPA and others estimate that improved agriculture and forestry practices can mitigate significant portions of our national greenhouse gas output. At the same time, greenhouse gas offsets can generate a significant new income stream for American agriculture. Similarly, agriculture and rural landowners can play a critical role in the clean energy economy that would result from a cap and trade policy. Farmers can provide the nation with biofuels, wind power and biomass energy that could heat houses and provide electricity to millions of consumers across the country. The task before us is to design an approach that enables a reasoned transition to a low carbon economy. For agriculture, this means ensuring that the costs of energy inputs remain reasonable and predictable while we create economic incentives that take full advantage of opportunities to sequester greenhouse gas emissions.

Controlling Costs in a Cap and Trade Program

NCEP’s overall view of offsets is that they are invaluable and should be an integral part of a cap-and-trade approach. This view is informed by economic modeling of recent climate bills, which has shown that an offset program could significantly reduce the costs of a cap and trade program. But NCEP does not believe it is appropriate or realistic to rely on offsets as the primary mechanism for managing economic risk in the context of a mandatory climate policy. While the inclusion of offsets as an alternative compliance option gives emissions sources greater flexibility and can reduce short- and long-term costs, it also introduces an additional source of uncertainty since numerous difficult-to-predict administrative and environmental factors will affect the supply of offset credits and ultimately allowance prices. Thus, as discussed below, we believe that it is important to include additional economic risk management mechanisms that can provide greater assurances about the potential costs of a climate program.

Clearly, one of the most important and contentious issues being debated right now is how to keep the economic cost of mitigating greenhouse gases (for the agriculture sector) to a minimum. On the one hand, farmers, businesses, consumers, and workers need assurance that a cap-and-trade program won’t result in excessively high costs or excessively volatile energy prices. At the same time, any successful program must have economic and environmental integrity—not only in the sense that it achieves its long-term emissions objectives, but also in the sense that it generates the meaningful and reasonably consistent financial incentives needed to initiate and sustain investment in new, low-carbon technologies over time.

With these goals in mind, the NCEP released a paper last week that recommended several improvements to the generally constructive cost containment approach taken in the House. The House bill contains provisions for a “strategic reserve” allowance auction that would make additional allowances available through an auction that begins at a specified price. Allowances for the reserve are borrowed from future years, thereby maintaining the integrity of the cumulative multi-year emissions cap while providing some price certainty in the near-term. The House bill also contains a price floor that will assure that there will always be a minimum level of investment in low and no carbon technologies.

An allowance reserve coupled with a price floor offers many of the benefits of a simple price cap and provides greater certainty about cumulative emissions reductions over the time horizon of the program. To be effective as a mechanism for managing economic risk, however, the allowance reserve must be structured to reduce uncertainty, not add to it. In our paper, we make several recommendations that would make this cost containment mechanism more predictable and effective. For example, we recommend changes to the way that the trigger price for the allowance reserve is set so that the price would rise over time in a transparent, pre-determined fashion (just as we would recommend for a straightforward price cap).

Overall, a price floor coupled with a price cap, or a robust, well-designed reserve auction mechanism could be extremely useful for increasing public confidence in the nascent greenhouse gas market. These mechanisms will limit volatility and will make allowance prices more predictable and transparent. In addition, a well designed cost containment mechanism can limit the risk that credit-trading will lead to the enrichment of Wall Street at the expense of Main Street. Importantly, a price collar can achieve this without imposing constraints on market activity that would undermine the pursuit of lowest-cost compliance and/or undermine necessary investment in low carbon technologies. Designing a reliable, reasonably simple, and effective approach to managing economic uncertainty *from the outset* will be critical to ensuring that a new U.S. climate policy achieves meaningful environmental results and commands broad support from policy makers, key stakeholders, and the American public.

In short, we believe that with modest but important revisions, the cost containment provisions of the House-passed climate and energy legislation can effectively reduce uncertainty over the economic impacts of climate legislation. It is also our view that simplifying and strengthening the cost-containment provisions in the House legislation is critical to building a bipartisan consensus for meaningful action this year.

Offset Program Design

How a climate change policy will affect agriculture will depend on the details in the final bill. Therefore, it is imperative that state and national agriculture organizations and their champions in Congress engage vigorously in the legislative process. During the negotiations over the recently-passed cap and trade legislation in the House, Agriculture Committee Chairman

Peterson worked out the details of the domestic offset program with Energy and Commerce Committee Chairman Waxman. Under the House-passed bill, the agriculture and forestry sectors are exempt from the bill's greenhouse gas emission reduction requirements. The USEPA will implement a carbon offset program and USDA will implement a separate agriculture and forestry offset program.

The question of which federal agency should administer a national carbon credit offset program has been hotly debated. The BPC applauds Chairman Peterson's efforts to develop an approach that enjoys the support of the agricultural community. The BPC believes that it is critical that advocates for agriculture and the environmental community advocates to build a strong foundation of partnership and trust. USDA has a large national network of field offices, research facilities and expertise in agriculture and forest management. Moreover, USDA understands the farming culture. At the same time, an agricultural offset program must benefit from technical expertise available at EPA and by the ultimate certification of credits by EPA. In recent years some observers have expressed skepticism about the quality of offsets sold on the voluntary market. The reputation of these offsets must be unquestioned if they are to have long-term value in the marketplace. We encourage the Committee to consider approaches that will encourage and strengthen the partnership between USDA and EPA.

While not explicitly addressing the USDA vs. EPA issue, Senators Daschle and Dole released a report in 2008 that suggested a structure that might be a useful way to address the roles of USDA and EPA in a carbon offset program. Senators Daschle and Dole concluded that unlimited offset credits should be available for agriculture-based mitigation projects—including soil carbon sequestration projects—that can meet rigorous standards for assuring measurement, additionality, and permanence. At the same time, they recognized that it may take some time to design an efficient system to measure and credit the full range of offset activities. Sequestration activities – just like other technology advancements - - require innovation and experimentation. Even a small number of imperfectly documented offset credits could significantly undermine confidence in the emerging offset market. As a result, early market participants are likely to be highly risk adverse. There is every reason to expect continued controversy, critical media attention and a high degree of scrutiny by the Inspector General and other oversight bodies. This dynamic has the potential to stifle innovation and slow the learning that will be necessary to build the technical foundation and experience needed to realize the full potential of terrestrial sequestration.

To ensure that we move boldly to develop a robust offset market, Senators Daschle and Dole proposed the creation of an allowance “set aside” to reward agricultural sequestration *in addition to* an offset provision for these activities. By using emission permits to in essence “insure” new and innovative sequestration activities, it will be possible to create a more streamlined approach than under a traditional offset regime - - regardless of which Agency is running the program. Set-aside allowances taken from under the cap provide a particularly effective mechanism for rewarding projects that provide important carbon benefits, but that may have more difficulty meeting these tests, such as no-till practices undertaken long before the cap-and-trade program goes into effect (so-called ‘early action’ projects). This approach may be especially well suited to rewarding early actors in the agriculture sector for emissions reductions activities adopted prior

to implementation of the mandatory policy. The rationale is that it may be difficult to demonstrate “additionality” for some of these early reductions.

Rulemaking Under the Clean Air Act

The question before Congress is whether to create new programs that are specifically designed to cost-effectively reduce greenhouse gas emissions. In the absence of Congressional action, EPA will be compelled to move forward with imperfect tools under existing authority. The Supreme Court on April 2, 2007, in *Massachusetts v. EPA*, 549 U.S. 497 (2007), the Supreme Court found that greenhouse gases are air pollutants as defined in the Clean Air Act. The Court held that the EPA Administrator must determine whether or not greenhouse gas emissions from new motor vehicles cause or contribute to air pollution which may reasonably be anticipated to endanger public health or welfare. In April of 2009, the agency proposed a finding that carbon dioxide and five other greenhouse gases endanger public health and welfare. It is widely anticipated that EPA will move forward over the next two years to complete its endangerment finding and then draft regulations to reduce greenhouse gas emissions from a variety of sources. Between those two choices, it is far preferable for agricultural producers, and all Americans, to have a cap and trade program that provides opportunities for the generation and sale of offset credits.

Conclusion

While we can all agree that U.S. action alone cannot solve a global problem, it is equally true that we have no hope of securing effective and equitable global action absent U.S. leadership. The key is to design a program that protects our economy, strengthens our security and encourages innovation in both the production of low carbon energy and sequestration of carbon emissions. The BPC is greatly encouraged by this Committee’s clear commitment to ensure that U.S. agriculture plays a critical role in the transition to a low-carbon economy and we look forward to doing whatever we can to support your deliberations in the coming weeks.