

The U.S. Carbon Market

Finding the “Right” Carbon Price
*And keeping it fair for consumers and
emitters*

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Why Carbon Market Structure Matters

U.S. Market Size

- At \$30/ton, 1 year of allowances \approx \$165 billion. If 100% auctioned:
 - \approx 6% of 2007 Total Government Expenditures
 - \approx 17% of 2007 Federal Expenditures

Recent Experience

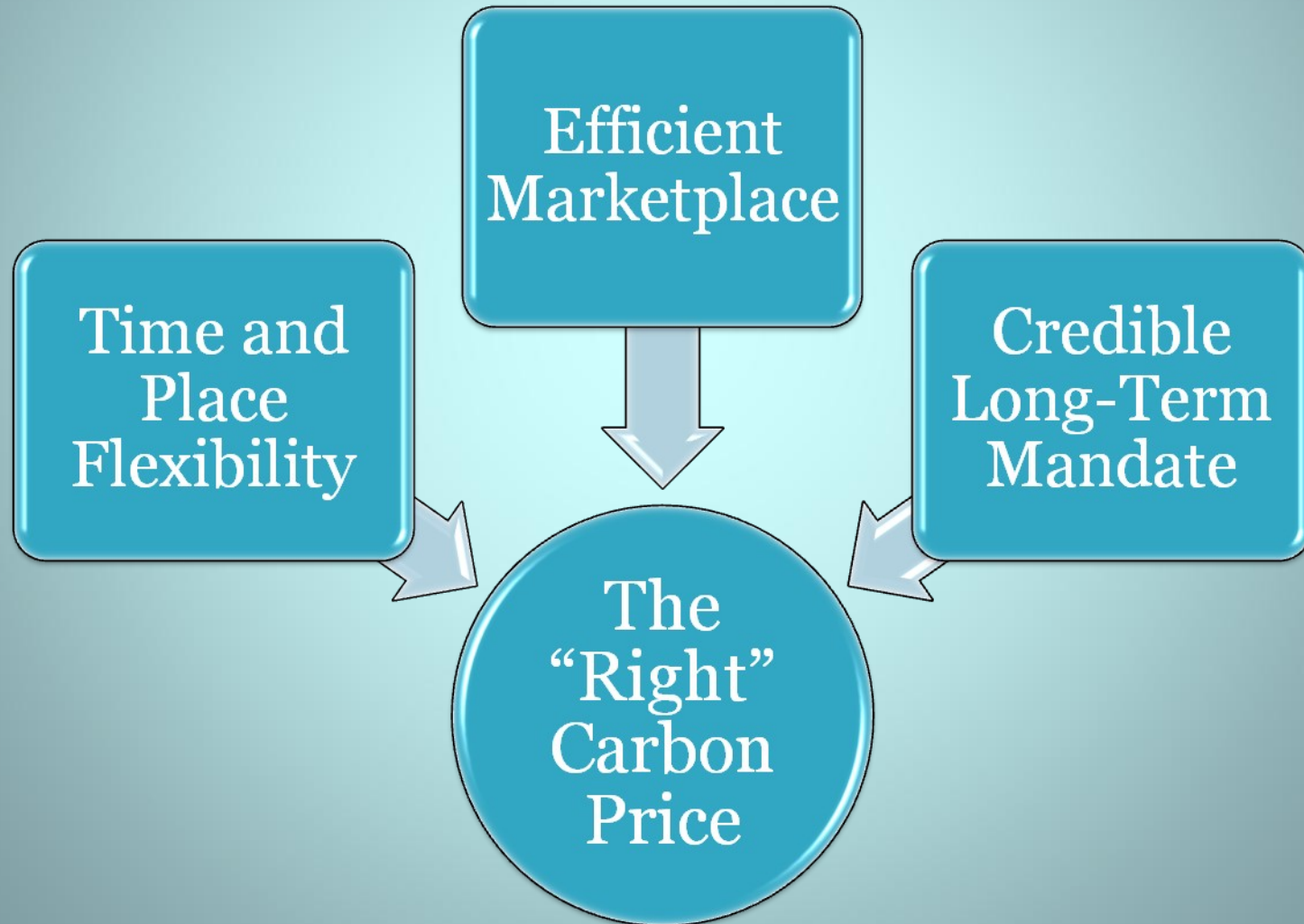
- Sub-prime mortgage crisis highlights risks
- Commodity markets are less transparent
- Government accountability for the market it creates

Affected Parties

- Consumers & emitters will be most affected. 2007:
 - Domestic Corporate Profits \approx 11% of GDP
 - Financial Industry \approx 33% of Corporate Profits
 - Utility Industry \approx only 3% of Corporate Profits

Finding the “Right” Carbon Price

Right = \uparrow Clean Technology + \downarrow Energy Demand
(+ \downarrow Volatility)



Time and Place Flexibility

Multi-year Banking and Borrowing of Allowances

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Efficient Hedging Tools for Emitters (and their Customers)

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Broad Trading Opportunities (including high-quality international allowances and *not* excluding domestic sectors)

Credible Long-Term Mandate

Incentivize Long-term Strategic versus Short-term Tactical Investment in Clean Technology




Optimize years-of-allowances-outstanding (“YAO”) taking account of emitters’ ability to finance auctions and the ability of Government to efficiently recycle auction revenue



Recognize that OTC instruments will dominate trading if YAO is kept short

Ideas for an Efficient Marketplace

Print every allowance trade (in real-time) on an exchange – and consider an NMS-like system to link exchanges

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Central Clearing of derivatives contracts to keep a deep pool of liquid hedging tools for emitters (on behalf of consumers)

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Accounting: fulsome disclosure - yet avoiding mark-to-market of allowances intended for compliance