



## Marketable Permits

### Committee on Regulation

#### Proposed Recommendation for Committee | March 28, 2017

1 [Preamble]

#### RECOMMENDATION

##### 2 **Establishment of Marketable Permitting Programs**

- 3 1. When an agency designs a marketable permitting system, the agency should be cognizant  
4 of the present and future resources that are required to develop and operate the system. In  
5 the case of marketable permits, the agency should consider that designing and  
6 implementing a marketable permitting system may require significant upfront costs, but  
7 require fewer resources to administer once the system has been established.
- 8 2. Agencies should consider the following additional factors when deciding whether to  
9 adopt a marketable permitting system. Agencies should consider adopting a marketable  
10 permitting system when:
- 11 a. Agencies can clearly define the privileges or obligations to be assigned by the  
12 program, and have the necessary information to set caps or baselines at the  
13 appropriate level.
  - 14 b. Regulated entities have more information about compliance costs, and the value  
15 of the resources to be allocated, than regulators. This often occurs when the  
16 activity to be regulated is conducted by heterogeneous or small sources.
  - 17 c. The overall level of an activity matters more to regulators than the identity of the  
18 actors, and the risk of unintended consequences from trading, such as the potential  
19 for highly localized problems, can be efficiently managed.



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- 20           d. Regulators are reasonably confident that a robust market is feasible. This requires  
21           interest and participation by regulated entities, and requires them to have  
22           sufficient knowledge to make efficient decisions in the market. In addition,  
23           variation across different permittees' compliance costs or utilities in the resources  
24           traded is needed to encourage trading of permits.
- 25        3. Agencies must be cognizant of legal authority when designing a marketable permitting  
26        program. At a minimum, regulators need implicit regulatory authority from broad  
27        statutory language to design such a program. Explicit language authorizing a marketable  
28        permitting system may help minimize legal uncertainty, but it is not necessary in every  
29        instance. In addition, before establishing such a program, regulators should make sure  
30        they have sufficient legal authority to monitor permit markets for fraud, manipulation,  
31        and other abuses.

### 32    **Desired Features of Marketable Permitting Programs**

- 33        4. When designing a marketable permitting program, agencies should cap the total level of  
34        activity of the marketable permitting system, rather than capping the rate of activity.  
35        During the design phase, agencies should create a mechanism for fine-tuning the cap. In  
36        addition, agencies should allow open access to the market so citizens can retire credits.
- 37        5. When distributing the initial allocation of permits, agencies should opt for auctions over  
38        grandfathering to prevent windfalls and barriers to entry for regulated parties. If auctions  
39        are not feasible, agencies should consider alternate allocation techniques, like set-asides  
40        for new entrants, and output or community-based allocations.
- 41        6. If an auction is used, agencies should emphasize the market management and  
42        distributional reasons for choosing auctions besides raising revenue. This could help  
43        avoid potential categorization of the permit auction as an impermissible tax.
- 44        7. In designing a marketable permitting program, regulators should include clear sanctions.  
45        Ideally, sanctions would include both penalties for non-compliance and the creation of  
46        plans for coming into compliance.



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47 8. When possible, agencies should pursue economies of scale in managing marketable  
48 permitting programs. Federal agencies should provide clear guidance on trading policy to  
49 regional and state offices, where applicable. This may include providing training sessions  
50 to regional and state officials.

### 51 **Legal Authority and Guidance**

52 9. Where marketable permit programs exist without explicit statutory authority, Congress  
53 should consider endorsing these programs to help reduce uncertainty for market  
54 participants and regulators. In the absence of explicit statutory authority, agencies should  
55 communicate to Congress any legal barriers to marketable permits.

56 10. To avoid misperceptions about permits' permanence or compensation for takings,  
57 agencies and Congress should avoid calling marketable permits "rights," and should  
58 instead use the language of marketable licenses or obligations.

59 11. Agency guidance on marketable permit programs should, at a minimum, go through  
60 public notice and comment. Agencies should consider codifying marketable permitting  
61 regulations to reduce uncertainty and inconsistent implementation.

### 62 **Oversight of Marketable Permitting Programs**

63 12. When designing a marketable permitting program, an agency should include a  
64 mechanism for oversight. Depending on feasibility and efficiency, agencies should  
65 consider overseeing the program directly, making use of self-verification, or engaging  
66 third-party credit verifiers. If an agency chooses to use third-party verifiers, it should set  
67 standards to ensure that third-party credit verifiers are qualified, insured, and free from  
68 conflicts of interest.

69 13. CFTC should consult with other agencies on the oversight of secondary permit markets,  
70 and should identify to Congress any need for additional statutory authorities to regulate  
71 permit markets. In addition, Agencies should work with CFTC to develop procedures for  
72 monitoring derivative markets relating to regulatory permits. CFTC should monitor



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73 active derivative markets relating to regulatory permits, and exercise its authority to  
74 prevent fraud, manipulation, and excessive speculation.

### 75 **Information Sharing**

76 14. Agencies should collect data on the operation of marketable permitting programs, and  
77 should periodically assess both the policy effectiveness and economic efficiency of  
78 existing marketable permitting programs.

79 15. To the extent feasible, agencies should release non-confidential data to the public that  
80 would help the public gauge a market's policy effectiveness.

81 16. Agencies that manage marketable permitting systems should coordinate with each other  
82 to improve existing marketable permitting systems and design more efficient systems in  
83 the future.