

SMALL BUSINESS RESEARCH SUMMARY

Emission Trading for Small Businesses

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Purpose

Emission trading is an economic-incentive-based alternative to command-and-control regulation. In an emission trading program, a government or trading agency issues a limited number of certificates consistent with the desired level of emissions. The sources of a particular pollutant (most often an air pollutant) are allotted certificates to release a specified number of tons of the pollutant. The certificate owners may choose either to release the pollutants and use the certificates or to reduce their emissions and sell the certificates. The fact that the certificates have value as an item to be sold or traded gives the owner an incentive to reduce the company's emissions. When applied properly, emission trading is intended to be an economic incentive that can lower the aggregate cost of meeting local or regional air quality standards while reducing bureaucratic intrusion into the operation of individual businesses. It is also intended to provide greater flexibility in meeting production goals and emission reduction requirements.

Emission trading is potentially relevant to all businesses subject to air, water, and hazardous waste pollution requirements. Such businesses are primarily manufacturing firms, but some pollution requirements also apply to farms and to service and retail businesses.

Emission trading promises benefits to those who participate. This study focuses on two questions: (1) Will these benefits motivate firms to participate? (2) Will emission trading provide benefits to small businesses? This study defines small businesses as facilities emitting less than 50 tons per year of an air pollutant.

Scope and Methodology

Approximately 30 emission trading programs existed or were being developed in the late 1990s. The researchers studied nine programs that were deemed representative of the various programs throughout the United States. After describing each program, they address three specific questions:

- What impact does the program's eligibility requirement have on small businesses?
- How do small businesses learn about the program?
- To what extent is the program utilized, currently or prospectively, by the small business sector?

Overall Findings

When properly devised, emission trading programs can benefit both small and large firms. However, in many programs small businesses cannot realize these benefits because of either restrictions contained within the regulations or high implementation costs. To serve the interests of small businesses, a low transaction cost is a necessary attribute in any emission trading system. Other attributes that help expand small business participation in trading include the following:

- The ability to make trades for specific, relatively short time periods;
- Allowance for shutdown credits;
- Allowance for curtailment credits; and
- The ability to use emission reduction certificates for a variety of purposes.

Unfortunately, many existing systems do not have such attributes. For example, the open market trading rule proposed by EPA disallows source shutdowns

or curtailments as the basis for an emission trading reduction.

The potential exists for emission trading programs to benefit small businesses in their roles as buyers and sellers. However, one question still needs to be addressed: To what extent are these programs utilized, either currently or prospectively? Emission trading is still in the nascent stage. Potential benefits to small businesses exist, but rules and protocol development will determine whether emission trading is a boon or bust for small businesses.

Highlights

- Most of the emission control equipment and procedures developed to date have been designed for large emission sources.
- If transaction costs are low enough, small sources may find it cheaper to purchase emission reduction certificates from larger sources rather than install costly controls. In that situation, emission trading would be providing small businesses with a lower cost alternative.
- In reality, however, opportunities for small businesses are few. In regions with poor air quality, small businesses are required to purchase emission reduction certificates to offset new emissions. The market for certificates would need to be somewhat efficient for such transactions to occur. In fact, most new source revision rules impose high transaction costs on any emission reduction certificate provider. Small businesses seeking to use these systems are forced into creating protocols, which may be a costly undertaking.

Ordering Information

The full text of this report and summaries of other studies performed under contract to the U.S. Small Business Administration's Office of Advocacy are available on the Internet at www.sba.gov/advo/research.

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