

Economic ideas for a complex climate policy regime

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Abstract

The parsimony of economic theory provides general insights into an otherwise complex world. However, the most straightforward organizing principles from theory have not often taken hold in environmental policy or in the decentralized climate policy regime that is unfolding. One reason is inadequate recognition of a variety of institutions. This paper addresses three ways that the standard model may inadequately anticipate the role of institutions in the actual implementation of climate policy, with a U.S. focus: multilayered authority across jurisdictions, the impressionistic rather than deterministic influence of prices through subsidiary jurisdictions, and the complementary role of prices and regulation in this context. The economic approach is built on the premise that incentives affect behavior. We suggest that an important pathway of influence for economic theory is to infuse incentive-based thinking into the conventional regulatory framework. In a complex policy regime, incentives can be shaped by shadow prices as well as market prices.