

CLIMATE POLICY: PROTECTION FOR HOUSEHOLDS

Legislation in the U.S. House of Representatives — the American Clean Energy and Security Act of 2009 (ACES) — will reduce Americans' greenhouse gas emissions and the impacts of climate change. One policy change would institute a cap-and-trade system that would for the first time put a price on greenhouse gas pollution. The cap-and-trade is coupled with consumer relief, which is provided directly to low-income consumers and through their utility companies to all home energy users.

Critical points regarding ACES bill

- A June 19 analysis by the Congressional Budget Office (CBO) puts the figure of instituting just the cap-and-trade portion of ACES at \$175 per household in 2020.¹ An Environmental Protection Agency analysis that also takes into account the energy-efficiency measures in the bill, finds lower average household cost estimates: between \$80 and \$111 in 2030.²
- The lowest-income households would see an increase in annual income. The CBO estimates that the poorest 20 percent of U.S. households would see incomes increase by \$40 in 2020 by auctioning a portion of pollution permits and returning the proceeds to low-income households.
- Mechanisms for consumer relief in ACES could be strengthened to benefit even more Iowans.

How are households affected?

A cap-and-trade policy puts a cap on greenhouse gas emissions and requires that polluters of a certain size hold permits for their emissions. Depending on how the cap-and-trade policy is structured, these emitters may be given some permits and will have to purchase additional permits for emitting greenhouse gases. This raises energy costs, which are passed on directly to consumers in home energy prices and indirectly in the prices charged for other goods and services that depend on the more costly fossil fuels.

Why are low-income households deserving of special concern?

Higher-income Iowans would have higher expenses under a cap-and-trade system than low-income Iowans, because they spend more total dollars on goods and services. But, because low-income Iowans consume more energy and energy-intensive goods as a portion of their income — which is already stretched thin — they are more vulnerable than upper-income Iowans to energy price increases. As a result, climate policy must be designed to assure low-income people are not disproportionately affected. ACES includes such provisions to hold low-income Iowans harmless as we address climate change.

Defining Cap & Trade

Current legislation in Congress would introduce a "cap-and-trade" system to discourage greenhouse gas (GHG) emissions and encourage sustainable energy investments.

A cap-and-trade system puts a limit that decreases over time on the amount of GHG emissions and requires those that emit GHGs above a certain level to hold a permit for emissions or to purchase offsets.

By itself a cap-and-trade system would necessarily raise energy prices and the prices of goods based on their energy inputs, in order to reduce the demand for fossil fuels and the release of GHGs.

That is why cap-and-trade systems should and must be coupled with consumer relief particularly for low-income consumers to help us make the transition to a clean energy economy in an economically feasible and equitable way. The ACES bill contains provisions that do protect low-income Iowans.

What are the estimates of consumer cost changes?

Because they did not quantify the substantial benefits of avoiding some of the impacts of climate change, the CBO has provided conservative estimates for cost changes in 2020, after the policy has had time to work in the economy, in 2010 dollars.

According to CBO, the direct and indirect price increases would account for 2.5 percent of the after-tax income for the average household in the lowest income quintile. The 20 percent of households with the largest incomes on the other hand would only expend 0.7 percent of their after-tax income. However, these costs do not account for the consumer relief provisions in the bill, which wipe out most of the cost increase for all households and eliminate cost increases for households in the lowest income quintile.

In dollar terms, considering consumer relief provisions in the bill that allocate the proceeds from selling permits, the poorest fifth of households would actually see an average \$40 increase in their budgets in 2020. CBO estimates a net cost of \$245 for households in the highest income quintile, about \$340 in the next 20 percent, \$234 in the middle 20 percent and \$40 in the second-lowest quintile.

How does proposed House bill address consumer relief?

Consumer relief is provided under ACES with a special focus on low-income consumers. Under the bill, the amount of net gains or costs would vary by income level each year because the value of allowances would change as they become scarcer. The bill specifies that 15 percent of the allowance value must be used for energy rebates and tax credits directly to low-income households.³

ACES also has provisions for relief to all consumers by giving free allowances to utilities and directing utility companies to pass this savings on to residential consumers by holding their home energy prices low. These provisions could be improved by modifying them to resemble assistance to low-income consumers — by auctioning permits and using the proceeds to fund rebates and refundable tax credits. According to Resources for the Future (RFF), a utility-based method of consumer relief does not return as much money to consumers as a direct refund system. RFF estimated that a direct refund would return an average of \$58 to \$145 more to Midwestern consumers than would a utility-based method.⁴

There are other flaws in directing utility companies to keep home energy prices low:⁵

- More than half of consumers' price increases will come from portions of their budget not related to home energy costs, so delivering relief through utility bills leaves a majority of costs out, such as higher gasoline prices and the indirect price increases in other goods and services.
- It relies on states to ensure their utilities provide relief that is effective and well-targeted. Not all state utility regulators are well-positioned to undertake this new and significant responsibility.
- By holding home energy prices lower, this system does not provide the maximum incentive for homeowners to conserve energy, and it drives up prices of other goods and services.

More Iowans could be held harmless or even benefit under ACES if more allowances were auctioned rather than given away and the proceeds from these auctions were given to consumers as direct refunds.

¹ Congressional Budget Office, June 19, 2009: "The Estimated Costs to Households From the Cap-and-Trade Provisions of H.R. 2454."

² Environmental Protection Agency, June 23, 2009: EPA Analysis of the American Clean Energy and Security Act of 2009, H.R. 2454 in the 111th Congress.

³ CBO, June 19, 2009: Ibid.

⁴ Rich Sweeney, Josh Blonz and Dallas Burtraw. June 5, 2009. "The Effects on Households of Allocation to Electricity Local Distribution Companies." Resources for the Future.

⁵ Center on Budget and Policy Priorities, Revised June 3, 2009: "Holding Down Increases in Utility Bills Is a Flawed Way To Protect Consumers While Fighting Global Warming."