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WAXMAN-MARKEY CLIMATE CHANGE BILL FULLY OFFSETS AVERAGE PURCHASING POWER LOSS FOR LOW-INCOME CONSUMERS

Also Reaches Some Moderate-Income Households

By Chad Stone, Sharon Parrott, and Dottie Rosenbaum

On May 19, 2009, the House Energy and Commerce Committee began consideration of the American Clean Energy and Security Act of 2009 (H.R. 2454), introduced by Reps. Henry Waxman (D-CA) and Ed Markey (D-MA). The legislation, which would place a cap on emissions of greenhouse gases to combat global warming, includes important provisions to ensure that the legislation does not increase hardship by making poor families poorer or pushing more people into poverty.

The Need for Low-Income Consumer Assistance

Restricting activities that produce greenhouse-gas emissions is necessary to avoid costly and potentially catastrophic environmental and economic consequences from global warming, but it also raises the cost of continuing to use "dirty energy." Low-income consumers are the most vulnerable to the higher costs arising from climate change policy because they spend a larger share of their budgets on necessities like energy than do better-off consumers, and they already face challenges making ends meet. The Waxman-Markey bill is designed in a way that protects vulnerable households' budgets while still achieving the benefits of reduced emissions.

The Use of Emissions Allowances to Fund Consumer Assistance

Waxman-Markey uses a cap-and-trade system to limit carbon emissions from the burning of fossil fuels and other greenhouse-gas emissions. A cap-and-trade system works by placing an overall limit on carbon dioxide emissions and requiring companies that emit carbon to hold an "allowance" (or "permit") for each ton of carbon they emit.

The bill uses proceeds from the sale of 15 percent of the emissions allowances to reimburse low-income households for the higher costs they will face for energy and energy-intensive goods and services under the bill. This low-income assistance is in addition to relief that would be provided to all consumers, regardless of income, by provisions in the bill that give free emissions allowances to retail gas and electric companies (called local distribution companies, or LDCs) for the purpose of providing their customers with relief on their utility bills.[1]

How Low-Income Consumer Assistance Would Work

Under the Waxman-Markey legislation, low-income households would be eligible for assistance delivered through two mechanisms — a refundable "energy tax credit" and an "energy refund" administered through state human service agencies. The bill would use existing delivery mechanisms — the federal tax code and the electronic benefit transfer (EBT) systems that human services agencies operate in all states — to efficiently provide assistance to these households.

- <u>How the benefit amount would be set:</u> The Environmental Protection Agency would calculate how much, on average, the higher energy prices resulting from the policies used to restrict emissions would reduce the purchasing power of the budgets of households of different sizes in the poorest 20 percent of the population. (This calculation would be based on the market value of emissions allowances and the "carbon footprint" of these households, as derived from government data on consumer expenditures.) The energy refund or tax credit would be set equal to the average loss of purchasing power of these households, after taking into account the consumer relief provided through free allocations to local utility companies.

- <u>Energy tax credit:</u> A refundable energy tax credit would be available to low-income households. The income level at which the credit phased out would vary by marital status and household size, but in general, the energy tax credit would be available to all households in the income range of the Earned Income Tax Credit and would *begin* to phase down at the income levels at which the EITC is completely phased out. For a family of four, for example, the energy tax credit would phase down over an income range of about $45,000 to $49,000.

- <u>Energy refund:</u> The proposal includes a second mechanism in order to reach low-income households that are not in the income tax system. These households include low-income seniors and people with disabilities, as well as very poor families with children. State human service agencies that operate the Food Stamp Program and other low-income benefit programs would provide eligible families with a monthly energy refund. The monthly refund amount would equal one-twelfth of the annual average loss in purchasing power calculated by EPA.

  Households receiving food stamps would automatically qualify for the energy refund, as would low-income seniors and people with disabilities who participate in the Low-Income Subsidy program for the Medicare prescription drug benefit. Other households that apply for the refund and whose income was below 150 percent of the poverty line also would receive a monthly energy refund. The refunds would be deposited in households' bank accounts or delivered through state electronic benefit transfer systems — the debit card systems that states

[1] In a cap-and-trade system, the cost to companies of buying the emissions allowances is a business expense that is passed on to consumers as higher prices, including higher electricity and natural gas bills. Waxman-Markey gives free allowances to LDCs but requires them to use those allowances to benefit their customers, presumably by selling the allowances and using the proceeds to give customers relief on their utility bills. In the bill, natural gas utilities are required to use a portion of their free allowances for energy efficiency programs, but there is no similar requirement for electric utilities. This creates ambiguity about whether and to what degree LDCs can use the proceeds from selling their allowances for energy efficiency expenditures, rather than to directly lower their customers' bills.

use to deliver food stamps, cash assistance, and other benefits — or other approved state delivery systems.

- Avoiding over-compensating households that participate in the energy refund and also file a tax return: If a household receives an energy refund through the monthly state human services delivery mechanism for some or all of a year and also qualifies for an energy tax credit, the energy tax credit would be reduced based on the number of months the household received the energy refund during the year. For example, a family that received an energy refund for six months through the human services agency would see its energy tax credit reduced by 50 percent.

Impact of the Consumer Relief Mechanisms

The consumer refund, in combination with the allocations to utility companies under the Waxman-Markey bill, would succeed in fully offsetting the average loss of purchasing power that low-income households would face, adjusted for household size.[2] The consumer refund also would reach some moderate-income households; the energy tax credit would begin to phase out for most families at about twice the poverty line (as noted above, at about $45,000 for a family of four). Eligible families with income toward the upper end of the eligibility range would receive a refund that partially, rather than fully, offsets their expected loss in purchasing power.

Moreover, the legislation delivers much of this assistance (the energy tax credit and the energy refund) through existing mechanisms that are efficient and effective.[3] By using existing delivery mechanisms, the bill would automatically reach a very large share of low-income families without their having to file new paperwork, and would have low administrative costs.

While the bill would offset the *average* low-income household's increased costs, some of these households — such as those that rent poorly insulated apartments or have inefficient appliances — will face higher-than-average costs. They could have difficulty making ends meet even with the consumer assistance provided in the bill. For that reason, as the legislation moves forward, it could be strengthened further by providing additional funds for the Low-Income Home Energy Assistance Program (LIHEAP), a program that provides energy assistance to low-income consumers and often targets aid on those who face utility shut-offs or other hardships. We recommend devoting an amount equal to 1 percent of the value of the emissions allowances for this purpose.

The consumer relief provisions also could be strengthened by extending the energy tax credit to families with incomes somewhat above the levels at which the tax credit would cut off under the Waxman-Markey bill, so that these families receive more relief from the higher energy prices they will encounter, and by providing somewhat larger energy refunds and tax credits so more low-income families that bear above-average cost increases receive full relief from those costs.

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[2] As other Center on Budget and Policy Priorities' analyses explain, distributing consumer relief through utility companies poses a series of problems. See Chad Stone, "Holding Down Increases in Utility Bills Is a Flawed Way to Protect Consumers While Fighting Global Warming," Center on Budget and Policy Priorities, April 27, 2009, http://www.cbpp.org/cms/index.cfm?fa=view&id=2800.

[3] See Sharon Parrott, Dottie Rosenbaum, and Chad Stone, "How to Use Existing Tax and Benefit Systems to Offset Consumers' Higher Energy Costs Under an Emissions Cap," Center on Budget and Policy Priorities, April 20, 2009, http://www.cbpp.org/cms/index.cfm?fa=view&id=2790.