

Eight Myths about the Waxman-Markey Clean Energy Bill

No bill is perfect. Certainly not one that contains a thousand pages and seeks to overhaul the way our nation uses energy. But many of the recent attacks on the American Clean Energy and Security Act (ACES) proposed by Representatives Waxman and Markey go beyond fact-based policy disagreements and venture more into the realm of mythology. Below is a list of a few of these myths, along with an attempt to set the record straight.

Myth #1. By giving away emission allowances, the bill is less effective at protecting the environment.

Reality: The cap in a “cap-and-trade” system determines its environmental stringency by setting the number of emission allowances that are available. These allowances are equal to the amount of emissions that are permitted under the cap and their number declines over time as the cap is tightened. From an environmental perspective, it doesn’t matter how the emission allowances are distributed. They could be auctioned or freely distributed or any combination of the two. All that matters is the total number of emission allowances that are distributed -- the environmental goal is determined by the cap itself and is not in any way impacted by whether the allowances are auctioned or distributed freely.

Myth #2. The Waxman-Markey bill will cost the average household thousands of dollars in higher energy costs.

Reality: A few widely touted studies purport to show that climate legislation will impose costs of \$1,600 - \$4,300 per household. But a closer look at these studies shows that they do not actually model the key provisions in the Waxman-Markey bill. Others have suggested that the changes required under the bill would not cost consumers any money and in some cases would even save consumers hundreds or even thousands of dollars. These claims also fail to fully account for costs. One study that does specifically model the core elements of the bill concludes that household costs are likely to increase by \$80-111 annually.

The Congressional Budget Office (CBO) testified before a Congressional hearing in May 2009 that household costs would be \$1,600 per household. But this number was based on a CBO study done nine years ago when energy prices and economic growth were very different. Nor did this statement take into consideration the potential to lower costs through the use of offsets and the use of allowance value to reduce household costs as specified in the Waxman-Markey bill. In June CBO released a new analysis that states that costs in 2020 would average \$175 per household and that those households in the lowest twenty percent by income would actually receive a net benefit of \$40 per year. A study by MIT is being used by some to argue that the climate bill would cost \$3,100 per household. But the author of this study has written that this number misrepresents the conclusions of his study and that estimated household costs would actually be far less. Finally, the Heritage Foundation recently issued a memo claiming that the Waxman-Markey bill would cost households \$4,300 annually. But this analysis fails to consider many of the key provisions of the bill including its extensive use of offsets to reduce overall costs and its use of the value of emission allowances to reduce costs to consumers.

Others have claimed that the bill will have no cost impact, but this ignores the very real economic costs of shifting to a clean energy economy. A study of the bill by the American Council for an Energy Efficient Economy concludes that the energy efficiency provisions would save consumers \$750 per household in 2020 and \$3,900 per household by 2030. This study focuses only on the changes in energy use associated with specific energy efficiency provisions and doesn’t include other requirements contained in the bill.



One study that does seek to estimate the costs of Waxman-Markey was released recently by Environmental Protection Agency (EPA). This analysis takes offsets and the use of allowance value into consideration and concludes that costs could be on the order of \$80-111 per household annually for the period from 2012-2050.

Given the limitations of economic modeling, no analysis should be assumed to give a correct answer. But certainly it is critical that any credible analysis that is used in the policy debate should faithfully represent what is actually required by the bill.

Myth #3. The Waxman-Markey bill will significantly increase gasoline prices.

Reality: According to one recently advertised myth, gasoline prices could rise by as much as 77 cents per gallon over the next decade. In fact, EPA projects that under the ACES Act, by 2030 gasoline prices would be only 25 cents per gallon higher – an average increase of less than three pennies per gallon per year. Meanwhile, gasoline prices have swung by more than two dollars per gallon over the last year alone.

Myth #4. The bill creates windfall profits for industries by giving 85% of the total emission allowances available to them for free.

Reality: The bill does not give away most of the allowances freely for industry's benefit. The bill does provide emission allowances to help consumers, workers, businesses and communities transition to cleaner sources of energy. Over the lifetime of the bill, about 80 percent of the total available allowances are used to protect consumers from higher energy prices and for other public purposes such as clean energy research and climate change adaptation efforts. For example, 15 percent of allowances are returned as a rebate to low- and moderate-income households. In addition, over the period covered by the bill, approximately 22 percent of allowances are given to electric utility and natural gas local distribution companies, primarily in the early years of the program, expressly for the purpose of being passed on to consumers to offset higher energy bills. The approximately 20 percent of allowances that are distributed freely to private industry includes about 12 percent for energy intensive industries, oil refineries and merchant coal plants to facilitate their transition to clean energy technologies. But even here provisions are included stating that such allowances should not result in windfall profits. Providing allowances to energy-intensive industries that compete in international markets also has an environmental objective. It prevents emission leakage – the potential for increases in production and emissions abroad from competing companies not facing similar restrictions. The ability to use the value of emission allowances to offset price impacts on consumers and others impacted by efforts to shift away from fossil fuels is one important advantage of a cap-and-trade policy.

Myth #5. The bill relies heavily on a cap-and-trade regime, the same policy approach that was tried and failed miserably in the European Union.

Reality: The European Union (EU) has instituted a cap-and-trade program as the cornerstone of its efforts for reducing greenhouse gas emissions. It began using this mechanism in 2005, starting with a 3 year trial period aimed at developing the institutions required for an effective trading system. This trial period demonstrated the importance of good emissions inventories and the need for consistent rules across all member nations making up the EU. Over time the EU's trading system has tightened its emissions cap and is moving toward greater use of auctions. The EU system has demonstrated that a market price for emission allowances will develop and serve as an incentive for achieving cost effective reductions in greenhouse gas emissions. It is currently effectively reducing emissions at 12,000 sources and enabling cost-effective compliance through the trading of millions of EU allowances. Because of its success, it remains the policy instrument of choice for the European Union.

A detailed experts' review of the initial implementation of the European Union's emissions trading system is available at: <http://www.pewclimate.org/eu-ets>.

Myth #6. The bill creates a new class of unregulated financial derivatives.

Reality: Given the recent problems in the financial sector, due in part to unregulated mortgage-backed derivatives, some have suggested that the market in emissions allowances and the types of financial instruments that could be developed under the bill could lead to the same types of problems. Creating a market that allows companies to hedge against the risk of future price changes can reduce costs over time and help manage the transition to a clean energy economy. What it should not do is create a new unregulated market. The bill contains extensive provisions calling for the Federal Energy Regulatory Commission to monitor and regulate developments in energy markets and for the Commodity Futures Trading Commission to play a similar role in monitoring and regulating derivatives that may develop under any cap-and-trade program.

Myth #7. The bill will result in huge job losses or, alternatively, will create thousands of new green jobs.

Reality: While these statements taken together may in fact be true, either one by itself is misleading. Given the size of our economy and the changes that occur over time, new jobs are constantly being created and existing jobs are constantly being lost. Twenty years ago fewer jobs existed in the telecommunications industry, but there were more in the auto manufacturing industry. This process of job creation and loss will continue whether the Waxman-Markey bill becomes law or not. What is less clear is whether the net impact of the bill on total jobs will be positive or negative. None of the models used to look at economic impacts is well suited for predicting both the number of jobs lost and the number gained. But for those losing their jobs, it is of little comfort that new jobs may be created elsewhere in the economy. The Waxman-Markey bill contains provisions for assisting workers and communities in meeting the challenges of shifting to a clean energy economy.

Myth #8. Regardless of the costs of Waxman-Markey, the benefits in reduced climate change from the bill itself are so small it isn't worth it.

Reality: Climate change is a global problem and will require nations of the world to work together to reduce greenhouse gas emissions. It is true that the United States has recently been overtaken by China as the largest source of greenhouse gas emissions, but the United States still contributes 20 percent of global emissions, so what we do is critically important. It is also true that if the United States acts alone, we cannot solve climate change. The key point is that all major emitting nations must contribute to those efforts and the bill both lays out what actions domestically the United States would pursue, while also providing a framework which encourages other nations to act. Nor is the United States alone in moving forward in this process. Other nations are at various stages of developing and implementing national programs and all are also actively engaged in international treaty negotiations under the United Nations Framework Convention on Climate Change. The reductions from the Waxman-Markey bill are a significant step in reducing emissions from the United States, but should be viewed in the context of what all nations must do to contribute to this global effort to limit climate change.