7-8-09

Incomplete CBO Estimate Does Not Include All Costs of Cap-and-Trade

On June 19, 2009, the Congressional Budget Office (CBO) released a letter and supplemental report about the American Clean Energy Security Act of 2009.[i] This analysis, which only looked at a portion of the costs of cap-and-trade, is being used by some to deceive the public into believing that this vast economy-altering bill would cost U.S. households only a "net average" of $175 in the year 2020.

In its document, CBO attempts to estimate how government redistribution (by giving away allowances and auction proceeds) will protect taxpayers, including those who were promised by the President that their taxes would not increase by a single dime.[ii] CBO estimates an average gross cost of $890 per household in 2020 with the top quintile paying an average of $1,380.[iii] After a generous assumption of an enormous government run wealth redistribution scheme via auction proceeds and free allowances, CBO projects a net average cost of $175 per household on average, with a middle quintile facing the highest net costs of $340.[iv] That figure, however, is only the budgetary cost of the scheme per household, not a comprehensive economic analysis. Moreover, it examines only one year of the program, a year that CBO optimistically assumes is relatively low cost, and after the expensive transition years.

As a result, CBO's estimate really only captures *some* of the costs of cap-and-trade, as the report acknowledges.

Why CBO's Estimate Is Not Complete:

Relies on a wealth redistribution scheme

- CBO generously assumes "costs would be offset by income or other benefits provided to households as a result of the distribution of the value of the emission allowances."[v]
- CBO's estimate of "net costs" relies on an unusual methodology. Applying CBO's methodology to our current tax structure, it could be argued that hard-earned taxpayer dollars taken directly from an individual's wallet are returned directly to that individual's wallet via government programs, including defense spending, CDC monitoring and NIH research. In other words, the average middle class family shouldn't mind paying taxes because the government will return most of their money in the form of benefits. Even if one agrees with this methodology, the wealth redistribution scheme fully protects only the bottom 20 percent of households from increased energy taxes.[vi]

Does not take into account economic damage (lost jobs and a smaller economy) from higher energy prices

- CBO notes: "The resource cost does not indicate the potential decrease in gross domestic product (GDP) that could result from the cap. The reduction in GDP would also include indirect general equilibrium effects, such as changes in labor supply resulting from reductions in real wages and potential reductions in productivity of capital and labor."[vii]
- CBO's analysis ignores the costs associated with a loss of income and lost jobs. Independent studies have estimated that millions of U.S. jobs would vanish and GDP would shrink. For

example, a study commissioned by The National Black Chamber of Commerce (NBCC) predicted 2.3 to 3.0 million fewer jobs in any given year and wage reductions of $170 to $960 for those who keep their jobs.[viii] The Heritage Foundation predicted up to nearly 2.5 million fewer jobs in the peak year.[ix]

- The NBCC study also predicted lower GDP of $170 billion to $730 billion each year between 2015 and 2050 (1.0 percent to 1.5 percent).[x] The Heritage Foundation predicted similar GDP losses.[xi] The Brookings Institution, which looked at a more generic cap-and-trade bill, predicted a 2.5 percent drop in GDP in 2050.[xii] The EPA, in one of its two models,[xiii] predicted GDP would be as much as 2.05 percent lower and $67 billion to $727 billion lower in any given year it examined to 2050.[xiv]
- The chief actuary for the Social Security Administration has also estimated that the bill would negatively affect cash flow in that program to the tune of $4.7 billion by 2019 because of lower economic growth.[xv]

Does not consider regional and intrastate disparities in energy production and prices

- CBO states that estimates "do not reveal the wide range of effects that the cap-and-trade program would have on households in different income brackets, different sectors of the economy, and different regions of the country."[xvi]
- CBO also admits: "Some regions and industries would experience substantially higher rates of unemployment and job turnover as the program became increasingly stringent. That transition could be particularly difficult for individuals employed in those industries (such as the coal industry) or living in those regions (such as Appalachia)."[xvii]
- Regional differences will be especially dramatic for the electricity sector. This is primarily due to the mix of fuels used in different regions (coal in some, hydroelectric in others) and the formula for the distribution of allowances.

Does not consider energy production transition costs

- CBO says that its year 2020 estimate "does not include the costs that some current investors and workers in sectors of the economy that produce energy and energy-intensive goods and services would incur as the economy moved away from the use of fossil fuels."[xviii]
- Their estimate ignores the first eight years of transition and rosily assumes the economy will have "adjusted to the change in the relative prices of goods and services" by 2020.[xix]
- The costs of the program may be at their lowest in 2020.[xx] Earlier years could capture transition costs while later years would see larger costs as the cap becomes more stringent.

---

[i] "The Estimated Costs to Households From the Cap-and-Trade Provisions of H.R. 2454." Available here: http://www.cbo.gov/doc.cfm?index=10327

[ii] The CBO estimate, however, makes clear that this Cap-and-Tax bill violates President Obama's campaign promise not to raise middle class taxes "one dime" (for those families earning less than $250,000 per year and individuals earning less than $200,000 per year). Given the bill's energy cost increases on a gross scale, all income quintiles (including the lower and middle class) would face higher annual costs up to nearly $1,400 (see CBO Report, p. 16). Even using CBO's application of net costs (i.e. costs after wealth redistribution) only the bottom income quintile is completely protected from tax increases, covering only those households averaging $18,000 per year (see data document http://www.cbo.gov/ftpdocs/103xx/doc10327/HR2454-income_ranges.xls) – a far lower threshold than the President's promise.

[iii] CBO Report, p. 11.

[iv] CBO Report, p. 2.

[v] CBO Report, p. 2.

[vi] CBO Report, table 2, p. 15.

[vii] CBO Report, p. 4, fn 3.

[viii] "Impact on the Economy of the American Clean Energy and Security Act of 2009 (H.R. 2454)," CRA International, May 2009 (analyzing ACESA as of May 15, 2009) ("NBCC Report"), p. 17. http://www.nationalbcc.org/images/stories/documents/CRA_Waxman-Markey_%205-20-09_v8.pdf.
[ix] "Son of Waxman-Markey: More Politics Makes for a More Costly Bill." ("Heritage Study") http://www.heritage.org/research/energyandenvironment/wm2450.cfm.
[x] NBCC Report, p. 21.
[xi] Heritage Study. "Nevertheless, the income (GDP) losses are nearly $200 billion out of the gate and average over $380 billion per year. As the economy recovers and the caps tighten, the detrimental effect of cap and trade gets more and more severe. In the worst years, GDP losses exceed $700 billion per year." (analyzing ACEASA as of May 18, 2009).
[xii] http://www.brookings.edu/events/2009/0608_climate_change_economy.aspx, "Consequences of Cap and Trade," p. 32.
[xiii] EPA uses two models, ADAGE and IGEM. ADAGE's model revealed a very slight increase in GDP in 2015 and 2020, followed by decreases of between .37 percent and 1.3 percent from 2030 to 2050. *See* Appendix of "EPA Analysis of the American Clean Energy and Security Act of 2009, H.R. 2454 in the 111th Congress," 6/23/09 ("EPA Appx"), p. 64. http://www.epa.gov/climatechange/economics/pdfs/HR2454_Analysis_Appendix.pdf.
[xiv] EPA Appx, p. 64. (IGEM model).
[xv] Letter from Stephen C. Goss, chief actuary, Social Security Administration, to Rep. Charlie Rangel, 6/19/2009. ("[I]t is widely expected that enactment of the bill will result in an increase in prices of goods and services and some reduction in real GDP, starting in 2012"; and "For this illustration, we have assumed that the level of real GDP will be reduced by between 1.3 and 2.2 percent by the year 2050 and the level of the Consumer Price Index (CPI) will be increased by between 2 and 3 percent by the year 2050, compared to the levels projected in the absence of the enactment of H.R. 2454.")
[xvi] CBO Report, p. 9.
[xvii] CBO Report, pp. 8-9.
[xviii] CBO Report, p. 8.
[xix] CBO Report, p. 8.
[xx] This is consistent with the results from the Heritage Foundation, which found 2020 to be the year of lowest GDP cost in its analysis. See "CBO Grossly Underestimates Cost of Cap and Trade," WebMemo #2503, 6/24/09. http://www.heritage.org/Research/energyandenvironment/wm2503.cfm.