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HOW LOW-INCOME CONSUMERS FARE IN THE SENATE CLIMATE-CHANGE BILL

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On June 2, the Senate began consideration of S. 3036, the Lieberman-Warner Climate Security Act of 2008. This is landmark legislation that would establish a cap on U.S. greenhouse-gas emissions — a critical step forward in the fight against global warming. It would do so without endangering future economic growth and prosperity. It is important, however, that lawmakers continue to work to improve the way that climate-change legislation protects low-income consumers, who are particularly vulnerable to the effects of higher energy prices.

“Cap-and-trade” legislation works by limiting the supply of fossil-fuel energy and thereby raising its price relative to other prices, in order to spur conservation and the development and use of cleaner energy sources. Families feel the pinch in their energy and gasoline bills, but a significant part of the impact also comes from the effects that energy prices have on the cost of producing and transporting other goods and services. Those increases have a disproportionate impact on low-income households, whose family budgets are largely composed of basic necessities like energy and food and who are least able to afford increased costs or new investments in energy-efficient cars or home heating systems and appliances.

This is *not* an inherent problem with cap and trade legislation. A well-designed bill can fully shield low-income consumers from the economic hardship that could otherwise result from higher energy-related prices. Moreover, action to reduce greenhouse-gas emissions is essential to reduce the risk of changes in climate that could have significant, and potentially catastrophic, consequences for all Americans, including those with low incomes.

Several years ago, when the congressional debate over cap and trade proposals was in its early stages, the proposals being put forward typically lacked meaningful provisions to shield low-income

KEY FINDINGS

- Well-designed climate-change legislation can allow low-income consumers to play their role in reducing greenhouse-gas emissions without cutting into their budgets, and can thereby avoid deepening poverty.
- The legislation that the Senate will consider this week relies on two primary mechanisms to deliver consumer relief: unspecified tax provisions and programs operated through utility companies.
- The exact amount of assistance that will be available to low-income consumers under these two provisions is uncertain, and will depend on subsequent decisions by the Finance Committee and utility companies.
- Before the legislation is finalized and enacted, a larger pool of resources for consumer relief, greater clarity on the amount provided to low-income consumers, and improvements in the delivery mechanisms used to reach them will be needed.

consumers and gave away large shares of greenhouse-gas emissions allowances to energy companies, rather than auctioning them off and using the proceeds for public purposes such as consumer relief.

The bill coming to the Senate floor this week represents a substantial improvement over many of the proposals advanced in prior Congresses. It recognizes the need to assist low-income consumers, expresses an intent to protect them from the economic impact of higher prices, and contains several specific provisions to move toward that goal. S.3036 also auctions off a larger share of the emissions allowances than was typical of the earlier generation of bills.

Before the legislation is finalized and enacted, however, its low-income provisions will need substantial further improvement. The comprehensive substitute amendment that will be offered to S.3036 provides two primary streams of funding for consumer relief: (1) a trust fund that is intended to finance tax relief to offset the economic impact of higher prices, and (2) resources provided to utility companies to assist their customers, including a set-aside for low-income customers. The exact amount of assistance that will be available to low-income households from these two sources is uncertain. The tax measures are unspecified and will have to be determined later by the Finance Committee. (The Environment and Public Works Committee does not have jurisdiction over taxes and could not write specific tax provisions.) Exactly how utility companies would use the resources provided to them is likewise uncertain. As work on the bill continues, the overall amount of consumer relief, the targeting of assistance on low-income consumers, and the delivery mechanisms used to reach low-income households will need improvement.

Why Is Low-Income Assistance Needed in a Climate-Change Bill?

By restricting the supply of fossil-fuel energy, cap and trade legislation will significantly raise the price of fossil-fuel energy and related products. This is necessary to encourage energy efficiency and greater use of clean energy sources, but it will pose serious challenges for low- and moderate-income households.

Our analysis, using an approach developed by the Congressional Budget Office, finds that even a modest 15 percent reduction in greenhouse-gas emissions would cost the poorest fifth of Americans an average of \$750 a year per household. These households have average annual incomes of only about \$13,000. The \$750 figure is the cost before any action is taken to mitigate these effects and is a measure of what would happen if low-income households were left on their own to cope with the effects of higher energy prices. (It is not an estimate of the impact of any particular legislation.)

Some opponents of cap and trade legislation have claimed that such legislation is inherently harmful to low-income consumers. That claim is false. But to avoid that outcome, a significant share of the allowance value must be set aside for low-income consumers and delivered through effective mechanisms.

Approximately 14 percent (one-seventh) of the total allowance value in a cap-and-trade bill would be sufficient to fund an effective program to prevent low-income households from losing ground.¹ This amount is needed to offset not only the higher cost of home energy — which will account for less than half of the legislation's impact on low-income consumers — but also the higher cost of

¹ A significantly larger amount will be needed if policymakers wish to provide relief to middle-income consumers as well.

gasoline, food, and the wide array of other goods and services that use energy in their manufacture or transport to market.

This 14 percent of allowance value can be accommodated in any cap-and-trade legislation that auctions most or all of the greenhouse-gas emissions allowances, since it would constitute only a small fraction of the revenues the legislation would generate.

Analysis of the Substitute Amendment to the Lieberman-Warner Climate Security Act of 2008

Total Amount of Assistance for Low-Income Consumers

As noted above, there are two primary sources of funding for consumer relief in the bill: tax provisions, which the Finance Committee would craft, and resources provided to utility companies. There also is a small stream of funds, provided through the states, that is designated for consumers who face hardship as a result of high prices for heating oil.

- **Tax provisions:** The bill's tax relief would be financed through a new Climate Change Consumer Assistance Fund, which would equal 3.5 percent of the total allowance value in 2012, and would rise substantially over time, to 15 percent of the total allowance value in 2050. (This is the provision that has been described as the "nearly \$800 billion" fund, which appears to be the total amount of dollars, in inflation-adjusted terms, that would be made available over the 39-year period from 2012 to 2050.) This provision is accompanied by Sense of the Senate language that it "should be used to fund a tax initiative to protect consumers, especially consumers in greatest need, from increases in energy costs and other costs."

The tax provisions could lead to the enactment of a refundable tax credit that would provide significant assistance to low-income consumers over time. The current legislation, however, cannot guarantee this result, as only the Finance Committee can write tax legislation; the Environment and Public Works Committee lacks jurisdiction over it. There will be powerful pressures on the Finance Committee to use a substantial portion of these resources for tax reductions for middle- and high-income individuals, who have been the primary beneficiaries of every major tax bill enacted in the past decade. (Some Senators have proposed that climate-change legislation include such measures as across-the-board individual income tax rate cuts, which would be regressive and provide little or no assistance to millions of low-income Americans.) The current legislation expresses its sponsors' intent that priority be accorded to low-income consumers in the design of the tax provisions, but the tax-writing committees will determine the extent to which that occurs.

- **Utility company funds:** The bill provides 12.75 percent of the allowance value to utility companies that deliver electricity or natural gas, rising to 13.5 percent by 2050. (This is the provision that has been described as the "\$911 billion fund," which is, like the tax figure, a 39-year total.) Of this amount, the bill specifies that 30 percent must be set aside to assist low-income consumers, which is equivalent to 3.8 percent of the allowance value in 2012, and 4.05 percent in 2050. The funding could be delivered either as rebates or energy efficiency interventions or some combination of the two. While some of the remaining 70

percent of the funds could be used to provide additional assistance to low-income consumers, those funds also are supposed to assist middle-income consumers and small businesses, both of which are likely to be strong competitors with low-income consumers for the remaining funds. (Note: if a utility's regulator certifies that less than 30 percent of these funds is needed to mitigate the increase in electricity and natural gas costs for low-income households, utility companies can devote a smaller share of the funds to this purpose.)

- **State funds:** The bill also includes in the funding provided to states (which can otherwise be used for a number of broad purposes) a small set-aside for “protecting consumers of home heating oil in the State from suffering hardship as a result of any increases in home heating oil prices.” In 2012, the amount set aside for these consumers would equal 0.2 percent of the total allowance value. In 2050, it would be 0.5 percent. It is possible that some states could make more funds available for low income relief out of the overall stream of resources the bill provides them, but no significant increase beyond the statutory requirements can be counted on. There will be strong competition for these funds for a variety of other uses, and states will also need resources to address increased budgetary costs for some existing programs as a result of higher energy costs.

How it all adds up: The pool of resources available for the tax provisions starts small, at 3.5 percent of allowance value. If low-income consumers were to get *all* of that, which is unlikely, the total amount of resources available to them in the early years from the *combination* of tax relief plus the guaranteed utility company stream (3.8 percent) and the guaranteed state funding stream (0.2 percent) would be about 7.5 percent of the allowance value. This is about half of the 14 percent of total allowance value that we estimate is needed to protect the low-income population. Low-income consumers might receive somewhat more of the utility company or state stream of funding, but given the competition for resources, any additional amounts are likely to be quite modest.

Delivery Mechanisms Used to Reach Low-Income Consumers

The tax system is an efficient way to deliver funding on a large scale to low-income working families, although it does not generally reach low-income people who are elderly or have serious disabilities or the poorest of the poor. In contrast, relying on utility companies to provide rebates to offset low-income Americans' loss of purchasing power is seriously flawed.

- **Utility company programs will miss large numbers of consumers who could be captured with a better designed delivery mechanism**, including the significant share of low-income households who do not pay utility bills directly because the bills are paid by their landlords (and reflected in their rents). Many other low-income households likely would not be served because most utility companies cannot easily identify which of their consumers have low incomes (other than households facing shut-offs).

The bill includes helpful language affirming that people should be eligible for the utility company-based assistance if they qualify for either food stamps or the Medicare low-income prescription drug subsidy. There will still be substantial challenges, however, in identifying and serving these households effectively through their utility company. History and

experience with other low-income programs suggest that a significant number of households will be missed through reliance on utility companies.

In this regard, it is worth examining the experience of the federal “Lifeline” telephone discount program, which is administered through local telephone companies. States and local telephone companies are encouraged to coordinate the Lifeline enrollment process with the enrollment processes for government-administered public benefits. In practice, however, such coordination is infrequent, and even where it does occur, large numbers of eligible households (in many cases half or more) do not make the transition from participation in public programs to Lifeline participation. The result is that, nationwide, the Lifeline program serves only about one-third of eligible individuals.

- **The utility company approach is aimed at electricity and natural gas bills, but does not cover other price impacts.** The utility company provisions are designed to offset electricity and natural gas bills. Less than half of the impact of the legislation on low-income consumers, however, will be felt in the form of higher home energy prices. More than half of the impact will come in higher prices for a range of other goods and services. The language of the bill suggests that its tax provisions will be the means of assisting consumers with these other costs. Such an approach makes sense for low-income working households. However, millions of low-income Americans, including most low-income elderly people, do not file federal tax returns and likely would not benefit from assistance delivered through the tax code; they need to be reached through other effective means.
- **Masking the true size of utility bills reduces the incentive to conserve.** The best way to encourage conservation is for households at *all* income levels to see the impact of higher energy prices in the bills they incur. Routing assistance through utility companies (and artificially lowering households’ utility bills) will blunt the “sticker shock” of higher utility bills on these consumers, which will make it less likely they will conserve energy or seek out energy efficiency improvements to the same degree. The goal of consumer relief should be to avoid an economic hit on low-income families by restoring their lost purchasing power without subsidizing (and masking the true costs of) their energy consumption.
- Finally, **it will be very difficult to provide the right amount of allowances to each individual electric and gas utility in the nation;** there is no good source of information on the percentage of low-income consumers nationally who are served by each individual utility company. Furthermore, there are 3,300 of these companies that deliver electricity alone, not counting the natural gas companies. The bill allocates allowances based on the share of electricity or natural gas that each company delivers, not on the relative incomes of each company’s customer base. Some utility companies that serve disproportionately low-income populations would likely end up with too few allowances to serve their low-income customers adequately.

These problems lack ready solutions so long as utility companies are used as the main vehicle for delivering consumer assistance. These problems could all be avoided by using the state Electronic Benefit Transfer systems to deliver a straightforward climate rebate. (Every state already uses EBT systems to deliver food stamp benefits and, in about 40 states, other forms of assistance as well, via a debit card.) Such an approach also would entail much lower overhead and other administrative

costs than trying to use utility companies as the delivery mechanism. This is an area where the legislation could be made considerably stronger.

It should be noted that some utility companies operate programs that help their consumers with energy efficiency improvements in their homes. There may be an important role for utility companies in this area. Utility companies are not, however, the appropriate mechanism to deliver consumer rebates or comparable relief that shields low-income households from substantial losses in purchasing power.

It may be desirable to substantially reduce the funds earmarked for utility companies, focus the remaining funds going to these companies on efficiency improvements, and use the freed-up funds for much more effective mechanisms for providing low-income consumer relief. Whether to retain significant funds for the utility companies for energy efficiency improvements — or to fund efficiency improvements through other mechanisms — should depend upon what is the most effective mechanism to secure such efficiency gains.

Energy Efficiency and Mass Transit Investments

The bill makes substantial investments in energy efficiency, mass transit, and other measures designed to reduce Americans' carbon footprints. This is an important goal.

It should be recognized that the energy efficiency programs that exist today operate on a very modest scale. Scaling these programs up to reach tens of millions of American households would require a massive expansion of program infrastructure for which the existing program knowledge base provides comparatively little guidance. Moreover, such a program expansion would inevitably take many years; hiring and training huge numbers of new technicians and dramatically expanding the infrastructure that supports them cannot be done overnight.

Consumers would continue to face the effects of higher energy costs on their budgets while such programs ramped up. Even in the long-term, it is unlikely that one could provide enough assistance in the form of cost-effective energy efficiency interventions to offset most or all of low-income households' loss in purchasing power due to higher energy prices. Consequently, while expanding energy efficiency programs is important and can help low-income households, it should be viewed as a supplement to a rebate-based approach, especially over the longer term. It does not obviate the need for consumer relief, particularly for people with low incomes.

We would note that, if the broad investments that the bill makes in energy efficiency succeed, they will have the effect of reducing overall demand for fossil-fuel energy, which will in turn keep energy prices from rising quite so high and thereby reduce the *dollar* impact of the legislation on households. But the *percentage* of the total allowance value that will be needed to fund an effective policy that preserves low-income consumers' purchasing power will remain at about 14 percent. It will just be 14 percent of a smaller overall dollar amount if the efficiency and alternative energy measures have large effects, because the allowances themselves will not be as costly if efficiency and alternative energy services succeed in moderating increases in energy prices.

Conclusion

Some opponents of climate-change legislation claim that such legislation *necessarily* entails economic hardship for low-income people. This is false. Climate legislation can slow global warming while avoiding negative impacts on low-income Americans. It can also help create new opportunities, such as through “green job” training programs that prepare disadvantaged workers for new jobs in the alternative energy sector (as the Senate bill recognizes by providing a source of funding for these programs).

How low-income households will fare depends on critical decisions about how many resources are directed specifically to low-income people and what delivery mechanisms are used to ensure that these households actually secure the help they need. The current legislation expresses the intent to address these matters and includes various specific provisions to do so. Before enactment, however, substantial further improvement is needed.

How Does S.3036 Compare to the Previous Version of “Lieberman-Warner”?

The bill coming to the Senate floor is a revised version of the bill reported out of the Senate Environment and Public Works Committee in December. The prior version included the following measures to assist low-income consumers:

- Funding (from auction revenues) for LIHEAP and the Weatherization Assistance Program, which was equivalent to about 3 percent of the total allowance value in 2012, growing to 10 percent by 2050.
- An allocation of 11 percent of the allowances to utility companies, with a direction that the funds be used both to assist low- and middle-income energy consumers (with no specific set-aside for the low-income group) and to promote energy efficiency.
- An allocation of 10.5 percent of the allowances to states, which could use these funds for 13 broad purposes, one of which was low-income assistance.

The new version (a substitute amendment to S.3036) makes the following revisions to the low-income consumer provisions:

- (1) It drops the LIHEAP and weatherization funds and adds consumer tax relief. The specifics of the tax relief would be determined by the tax-writing committees.
- (2) It increases the total pool of resources provided to utility companies, adds a guarantee that 30 percent of those funds must be directed at low-income Americans, and adds small businesses to the entities that can receive these funds.
- (3) It retains a broad list of purposes for which the funds allocated to states can be used but adds a small set-aside for assisting consumers who face hardship with their heating oil expenses.

CONSUMER RELIEF IN THE TWO BILLS					
as a percentage of total allowance value					
Lieberman-Warner bill as reported out of EPW			Substitute amendment to S.3036		
	2012	2050		2012	2050
LIHEAP and Weatherization	3%	10%	Tax relief	3.5%	15%
Local distribution companies (utilities)	11%	11%	Local distribution companies (utilities)	12.75%	13.5%
			State heating oil consumer set-aside	0.2%	0.5%
TOTAL	14%	21%	TOTAL	16.45%	29%

As the table above illustrates, funding for *all* consumer relief, not just the low-income part (including the utility company-provided energy efficiency interventions) would have equaled 14 percent of the total allowance value in 2012 under the prior version of the legislation; under the substitute, it would total 16.45 percent.

The amount set aside (or guaranteed) for *low-income* consumers is similar under both versions of the bills, rising from 3 percent of the total allowance value in the committee-reported bill to 4 percent under the substitute. In the prior version of the bill, the low-income guarantee was provided by the LIHEAP and weatherization funds; under the substitute, it is provided by the 30 percent set-aside of the utility company funds, plus the small set-aside from funding provided to the states.