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Heritage Analysis of Waxman–Markey Hits Where Others Miss

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On June 26, the House of Representatives narrowly passed climate change legislation designed by Henry Waxman (D–CA) and Edward Markey (D–MA). The 1,427-page bill would restrict greenhouse gas emissions from industry, mainly carbon dioxide from the combustion of coal, oil, and natural gas.

If passed by the Senate, the bill would burden families with thousands of dollars per year in direct and indirect energy costs. Additional thousands of dollars of income would be lost, and the national debt would jump by tens of thousands of dollars per family. Job losses due to Waxman–Markey’s energy restrictions would be in the millions.

How Cap and Trade Works. Waxman–Markey is an energy tax of historic proportions. Called “cap and trade” by its supporters, the bill would limit man-made greenhouse gas emissions by instituting a declining cap on allowable emissions. Electricity producers, petroleum refiners, and natural gas distributors would have to obtain permits, called “allowances,” from the federal government for every ton of CO₂ emissions they produce.

Since the government issues fewer allowances in each subsequent year, the allowance price has to rise to meet demand. That is, the cost of an allowance is a tax, and the tax rises each year. As with any tax, it will ultimately be passed on to consumers in the form of higher energy and product prices. The total value of the allowances (the tax revenue) would be hundreds of billions of dollars per year and will have an aggregate value of \$5.7 trillion by 2035.

This makes Waxman–Markey one of the largest new taxes in history, if not the largest.

In particular, the Heritage analysis projects that by 2035 the economic impacts (in constant 2009 dollars) of this bill are:¹

- Gasoline prices will rise 58 percent (or \$1.38);
- Natural gas prices will rise 55 percent;
- Heating oil prices will rise 56 percent;
- Electricity prices will rise 90 percent;
- A family of four can expect its per-year energy costs to rise by \$1,241;
- Including taxes, a family of four will pay an additional \$4,609 per year;
- A family of four will reduce its consumption of goods and services by up to \$3,000 per year, as its income and savings fall;
- Aggregate GDP losses will be \$9.4 trillion;
- Aggregate cap-and-trade energy taxes will be \$5.7 trillion;
- Job losses will be nearly 2.5 million; and
- The national debt will rise an additional \$12,803 per person (\$51,212 per family of four).

This paper, in its entirety, can be found at:
www.heritage.org/Research/EnergyandEnvironment/wm2580.cfm

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(All of these price and cost increases are above and beyond those expected to occur without the legislation.)

As President Obama said about his cap-and-trade program during the presidential election campaign, “electricity prices would necessarily skyrocket.”² The same applies to many other products as the Waxman–Markey energy tax spreads through the economy as businesses and consumers adapt to higher energy prices.

People would spend more for less energy; build smaller houses and buildings; drive smaller, less safe vehicles; turn their thermostats up in the summer and down in the winter; and divert income to more expensive energy-saving appliances. But savings from these activities and more would not be enough to offset the higher energy costs. The net effect is lower income, higher prices, and fewer jobs.

What Makes the Heritage Study Different. An oft-cited study from the Congressional Budget Office (CBO) claims that the cost of Waxman–Markey would be less than \$200 per year per family, or “a postage stamp per day.” However, the CBO report does not even attempt to measure the impact on national income—an impact estimated to be in the thousands.

Another frequently cited study comes from the Environmental Protection Agency (EPA).³ The EPA makes some very questionable assumptions about how CO₂ caps would be met, especially concerning the growth of nuclear power and the ability to forego industrial CO₂ cuts by paying farmers to grow trees and foreigners to cut their CO₂ emissions

(known as offsets). The magnitude of offsets in the EPA’s latest report is much larger than in their preliminary analysis of Waxman–Markey.

But the factor least understood is the EPA’s use of discounting, a financial tool for comparing costs and benefits that occur at different times. Discounting is a legitimate tool for cost-benefit analysis, but it can give a distorted picture of the magnitude of costs for the period in which they occur.

For instance, the EPA projects that the real cost (adjusted for inflation) to a household of 2.6 people will be \$1,287 lost consumption in 2050. However, after discounting, this figure is reduced to \$140. Here, discounting tells us that \$140 invested at a riskless 5 percent per year will be worth \$1,287 in 41 years. It in no way says that 41 years from now the lost consumption will be \$140.

Since consumption comes after taxes and savings, the \$1,287 is much less than the lost income in the first place. So the EPA cost, with all of its questionable assumptions, is over \$2,700 in 2050 when converted to lost income for a family of four—even after adjusting for inflation.

In short, the EPA and the CBO studies are not comprehensive measures of the economic impact of Waxman–Markey in simple, inflation-adjusted dollars.

In contrast, analyses by The Heritage Foundation and the Brookings Institution—two organizations often portrayed as ideological opposites—study the overall impact of Waxman–Markey on the economy, including the effects of higher production costs and lower economic output. These studies show that Waxman–Markey would lead to significant economic losses—on the order of thousands of dollars

1. See David W. Kreutzer, Karen A. Campbell, William W. Beach, Ben Lieberman, and Nicolas D. Loris, “The Economic Consequences of Waxman-Markey: An Analysis of the American Clean Energy and Security Act of 2009,” Heritage Foundation *Center for Data Analysis Report* No. 09-04, August 6, 2009, at <http://www.heritage.org/Research/EnergyandEnvironment/cda09-04.cfm>. For analysis of other cap-and-trade legislation, see William W. Beach, David W. Kreutzer, Ben Lieberman, and Nicolas D. Loris, “The Economic Costs of the Lieberman-Warner Climate Change Legislation,” Heritage Foundation *Center for Data Analysis Report* No. 08-02, May 12, 2008, at <http://www.heritage.org/Research/EnergyandEnvironment/cda08-02.cfm>.
2. As quoted in Paul Chesser, “Obama’s Plan ‘Necessarily’ Skyrockets Energy Bills,” *Washington Examiner*, May 1, 2009, at <http://www.washingtonexaminer.com/opinion/columns/OpEd-Contributor/Obamas-plan-necessarily-skyrockets-energy-bills-44124402.html> (August 5, 2009).
3. Environmental Protection Agency, “EPA Analysis of the American Clean Energy and Security Act of 2009 H.R. 2454 in the 111th Congress,” June 23, 2009, at http://www.epa.gov/climatechange/economics/pdfs/HR2454_Analysis.pdf (July 25, 2009).

per family per year. Analysis done by CRA International for the National Black Chamber of Commerce comes to a similar conclusion.⁴

Taxing and Spending. The Heritage Foundation analysis exposes Waxman–Markey as a new tax of a historic magnitude. As could be expected, such a large revenue stream has attracted an army of lobbyists seeking a share. (The Center for Public Integrity estimates that over 2,300 lobbyists are involved.⁵)

Congress has obliged—and then some. For the first 15 years (2012–2026) of the Waxman–Markey regime, over 88 percent of the revenue is given to various special interest groups. In fact, more than 100 percent has been promised for the years 2016 and 2017.⁶ So this historic tax increase has been matched by a historic spending spree.

Another Burden on Future Generations. The income losses, the job losses, the tax increases, and the mounting debt all get worse over the coming decades. The Waxman–Markey bill forces a bad deal on a generation that does not have the option to turn it down.

The \$9.4 trillion of lost income, the 2.5 million lost jobs, the \$5.0 trillion of additional national debt, and the \$5.7 trillion in new taxes will buy no more than a 0.2 degree (Celsius) moderation in world temperature increases by 2100 and no more than a 0.05 degree reduction by 2050.

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4. Congressional Budget Office, “The Estimated Costs to Households from the Cap-and-Trade Provisions of H.R. 2454,” June 19, 2009, at <http://www.cbo.gov/ftpdocs/103xx/doc10327/06-19-CapAndTradeCosts.pdf> (July 25, 2009); David Montgomery et al., “Impact on the Economy of the American Clean Energy and Security Act of 2009 (H.R.2454),” CRA International, May 2009, at http://www.nationalbcc.org/images/stories/documents/CRA_Waxman-Markey_%205-20-09_v8.pdf (July 25, 2009); Warwick McKibbin, Pete Wilcoxon, and Adele Morris, “Consequences of Cap and Trade,” Brookings Institution, June 8, 2009, at http://www.brookings.edu/~media/Files/events/2009/0608_climate_change_economy/20090608_climate_change_economy.pdf (July 25, 2009).
5. Center for Public Integrity, “Latest Center Analysis Reveals Explosive Growth in the Climate Change Lobby,” February 25, 2009, at <http://www.publicintegrity.org/news/entry/1187/> (August 5, 2009).
6. Tim Carr, “Waxman-Markey Just Doesn’t Add Up,” The Foundry, August 4, 2009, at <http://blog.heritage.org/2009/08/04/waxman-markey-just-doesnt-add-up/>.