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Government Agencies Would Need $16.6 Billion in New Tax Revenue to Buy Carbon Allowances Under Global Warming Legislation

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By Edwin Mora

(CNSNews.com) - A new Government Accountability Office (GAO) study says that all levels of government – federal, state, and local – will have to come up with a total of $16.6 billion in additional revenue to purchase carbon allowances, if cap-and-trade – to allegedly combat global warming -- is enacted into law. Experts say this could prompt increases in taxes.

This is the second government report to estimate that the proposed climate-change legislation, formally known as the American Clean Energy and Security Act of 2009, will eventually cost consumers more.

A Congressional Budget Office (CBO) study published on June 19 revealed that the House cap-and-trade bill, passed by a 219 to 212 vote on June 26, would cost an estimated $175 per household every year.

Cost estimates from the Environmental Protection Agency (EPA) on cap-and-trade legislation are lower -- at $80 to $111 per household.

The cap-and-trade bill, in general, places limits (a cap) on how much carbon and greenhouse gases companies can emit. If they exceed that limit, they can purchase ("trade") carbon credits to compensate for their over-emissions.

John Stephenson, director of natural resources and environment for the GAO, in written testimony for an Aug. 4 Senate Finance Committee hearing, said that state, local, and federal governments would be financially liable if cap-and-trade is imposed.

Stephenson testified about the GAO's assessment of how emission-allowances and revenues produced by a cap-and-trade measure should be allocated.

"According to one study, governments produce approximately 13 percent of U.S. carbon dioxide emissions, and the allowance consumption associated with these emissions could cost governments an additional $16.6 billion," Stephenson said.

Brian Johnson, federal affairs manager for Americans for Tax Reform (ATR), a free market policy group, explained that state governments may have to raise their tax rates to buy carbon permits.

"In order for the states to raise this money [for carbon allowances], they're going to have to increase utility costs and/or just increase direct taxes on their citizens," Johnson told CNSNews.com. "There's going to be no way to raise these funds without doing that."

"You've got something like 36 states that get 80 percent or more of their energy from carbon-based sources, so they're going to be really hit by something like this in order to have the proper allowances," he said. "I mean, they'll necessarily have to raise taxes. I don't see any way around it."

Jerry Taylor, a senior fellow at the Cato Institute, a libertarian think-tank, agreed with Johnson that state taxes would be raised to generate funding for carbon allowances, adding that states are "generally" constitutionally bound to "balanced budget requirements."

"They can't borrow as freely as the federal government can," he said. "They can borrow some, there are ways around these balanced budget requirements. But, generally speaking, they have to tax what they spend."

Adele Morris, policy director of the climate and energy project at the Brookings Institution, a center-left think tank in Washington, D.C., told CNSNews.com that to cover high energy costs the federal government would potentially have to appropriate additional funds.

"It's possible that, yes, the government would have to have some kind of appropriations in order to buy [allowances]," Morris said.

"Even if they don't buy allowances, it's [climate-change legislation] going to include higher costs," she said. "So it's going to have [to have] appropriations to fund those higher costs."

The higher costs that result from the climate legislation are going to affect all levels of governments, she explained.

"The government is a big user of energy and that means everything from our fleet vehicles and the fuel they use to the heating and lighting of buildings that the government uses," Morris told CNSNew.com.

"In those expenditures, part of the carbon price is going to be passed along to the government, just like it would any other enterprise, and that's going to be across-the-board in all federal government activities -- and not just the federal government for that matter, it is going to be state and local governments as well," she said.

Morris said one option for governments – especially the federal government – faced with the question of how to raise revenue to offset energy costs might be to raise deficits.

"One option is to raise revenue, another option is to cut spending, another option is to raise debt," said Morris.

However, she also said: "One important reaction would be to conserve energy and that would be to invest in more energy-efficient buildings, lighting, and vehicle fleets and I think that's a very important response from governments."

Currently, lawmakers are considering either auctioning the allowances, handing them out for free, or a combination of both (free and purchased). The House bill initially gives away most of the allowances and would sell just a few of them, which could result in revenue shortfall, according to Johnson.

“If they allocate the free allowances, that’s just cap-and-cap -- you know, there’s no trade there,” explained ATR’s Johnson. “There’s no economic driver and the government wants to be able to set the market and set the price for these.”

In his written testimony, Stephenson suggested that auctioning permits would generate the most revenue, which could be used to off-set costs for the federal government, among other things.

“Given the revenue generation potential of auctions, many experts we consulted as part of a prior study suggested that a cap-and-trade program should maximize the level of auctioning,” said Stephenson.

However, according to Jerry Taylor, offset-cost benefits posed by selling carbon permits would only be felt at the federal level, isolating state and local governments.

“The sales of the permits will be done by the federal government,” Taylor said. “So if you’re talking what state and local government would have to spend, that would not be offset by any permit sales because the permit sales aren’t being conducted by state and local governments, [they are] being conducted by the federal government, unless the revenues were recycled back to state and local governments somehow, which would not be in the House bill.”

Stephenson of the GAO said, “Placing a price on emissions is likely to raise the cost of production of many goods and services. The size of the impact will depend on the price of allowances, as well as the ability of producers to substitute less emission-intensive processes and inputs.”

In June, the CBO revealed that the cap-and-trade bill would generate $45 billion by 2019 in revenues if a portion of the allowances were auctioned. Annual revenues from allowances could reach between $30 billion and $300 billion by about the same year, according to earlier CBO estimates.

Unless the climate bill exempts governments from having to buy allowances, state, local, and federal governments will need $16.6 billion to buy permits.

“The $16.6 billion figure that you mention was provided to illustrate the effects of a cap-and-trade program on government expenditures,” Stephenson told CNSNews.com in an e-mail.

The study, which was written by Terry Dinan of the CBO, was based on the assumptions of a 15-percent cut in emissions and an allowance price of $100, Stephenson added.

“The CBO projects the allowance price under the Waxman-Markey [climate-change] legislation to be much lower, starting at $15 in 2011 and growing to $16 in 2019,” he told CNSNews.com.

“As a result, government expenditure on emissions’ allowances or reductions is also likely to be much lower, although the CBO does not estimate a specific figure in its analysis,” he said.

Economists favor the auction approach because it is transparent, said Stephenson.

“For example, many economists favor auctioning because of its transparency and because it discourages behaviors motivated by a desire to gain free allowances, such as ‘baseline inflation’,” he said. “This occurs when a firm attempts to boost the number of allowances it receives by increasing its emissions prior to the outset of a cap-and-trade program.”

The Senate may take up the energy bill when it returns from its August recess.