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Thank you for the opportunity to testify today. The main message of my testimony is that climate change legislation can fight global warming effectively while protecting consumers if it is designed appropriately.

Fighting global warming requires policies that significantly restrict greenhouse gas emissions, and an emission cap can serve this purpose. Under a cap, the price of fossil-fuel energy products — from home energy and gasoline to food and other goods and services with significant energy inputs — will rise. Those higher prices will create incentives, sometimes referred to as a “price signal,” for energy efficiency and conservation measures and for the development and increased use of clean energy sources. But they will also put a squeeze on consumers’ budgets, and low- and moderate-income consumers will feel the squeeze most acutely.

Fortunately, climate change policies can be designed in a way that preserves the incentives from higher prices to change the way that we produce and consume energy, while also offsetting the effect of those higher prices on consumers’ budgets. Well-designed climate policies will generate substantial revenue that can be used for consumer relief, as well as to meet other critical needs related to climate change.

To capture this revenue under a cap-and-trade system, it is essential that most or all of the allowances or permits used to limit emissions be auctioned rather than given away free to emitters. Giving away, or “grandfathering,” allowances is sometimes portrayed as a way to keep down costs for consumers, but that argument does not withstand scrutiny. If allowances are given away free to firms that are responsible for emissions, the firms and their shareholders will reap unwarranted benefits. The Congressional Budget Office has explained that these firms would receive “windfall profits:” they would be able to charge higher prices for their products due to the effects of the emissions cap but would not have to pay for their emissions allowances. Greg Mankiw, former chair of the Council of Economic Advisers for President George W. Bush, has written in a similar vein that consumer prices will rise regardless of whether allowances are given free to emitters and that grandfathering the allowances would constitute “corporate welfare.” There is little disagreement among economists about this effect.

Protecting low- and moderate-income consumers should be the top priority of consumer relief provisions included in climate change legislation. These consumers are the most vulnerable because they spend a larger share of their budgets on necessities like energy than do better-off consumers and already face challenges making ends meet. They also are the people least able to afford purchases of new, more energy-efficient automobiles, heating systems, and appliances. Middle-income consumers also will feel the squeeze from higher energy-related prices, and they should receive consumer relief as well.

Much of the Center on Budget and Policy Priorities' work on climate change policy has focused on developing concrete proposals to protect the budgets of low- and middle-income consumers in a way that is *effective* in reaching these households, *efficient* (with low administrative costs), and *consistent with energy conservation goals*. With these goals in mind, we have designed a "climate" or "energy" rebate, that would offset the impact of higher energy-related prices on low-income households — who are most vulnerable to these price increases — and middle-income households, who also will feel the squeeze. Such consumer assistance should offset the increases in households' energy-related expenses for an array of items, not just the increases in their utility bills, which will account for less than half of the overall impact on their budgets.

As explained below, we recommend that consumer relief be provided through the tax system and existing benefit delivery systems.¹ Under the proposal we have developed, approximately 95 percent of households in the bottom fifth of the income distribution and more than 98 percent of households in the next two income quintiles would be reached automatically. (With outreach, these figures would go still higher.) Because the rebates would build on existing tax and benefit delivery mechanisms, this approach would not require new bureaucratic structures, and the administrative costs would be low, compared with alternative delivery mechanisms. The size of the energy rebate, and how far up the income scale it would extend, would depend on the amount of funding (i.e., the share of the allowance value) that Congress decided to make available for consumer relief.

This is decidedly preferable to an alternative approach — providing funds to utility companies to artificially suppress price increases in electric bills that otherwise would occur under an emissions cap. Artificially keeping electric bills down would undercut the incentives the emissions cap is supposed to create to reduce electricity use. As a result, this approach would lead to *larger increases in prices for other energy products than would otherwise occur* — *since the use of other forms of energy would have to decline more to meet the emissions cap*. The resulting inefficiency would place some burden on the economy. This approach also would fail to offset increases in energy-related costs other than home utilities, which as noted above, account for the majority of the impact on consumers.

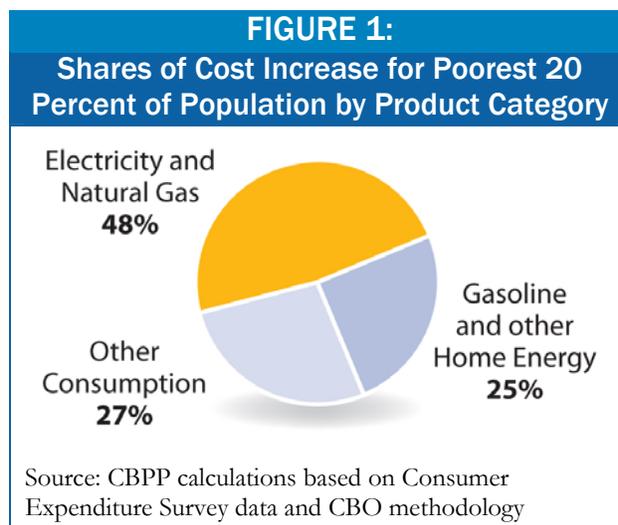
¹ The design for an energy rebate laid out here follows the same principles as earlier work on climate change policy by the Center on Budget and Policy Priorities and incorporates the Center's latest thinking on how to reach as large a percentage of the target population as possible operating through existing, proven delivery mechanisms. For further discussion, see Sharon Parrott, Dottie Rosenbaum, and Chad Stone, "How to Use Existing Tax and Benefit Systems to Offset Consumers' Higher Energy Costs Under an Emissions Cap," Center on Budget and Policy Priorities, April 20, 2009, <http://www.cbpp.org/files/4-20-09climate.pdf>; Chad Stone and Hannah Shaw, "Extending 'Climate Rebates' to Include Middle-Income Consumers," Center on Budget and Policy Priorities, February 19, 2009, <http://www.cbpp.org/cms/index.cfm?fa=view&id=2650>; and Chad Stone and Robert Greenstein, "Why Utilities Are Not Well-Suited to Deliver Relief to Low- and Moderate-Income Consumers in a Climate Bill," Center on Budget and Policy Priorities, February 19, 2009, <http://www.cbpp.org/cms/index.cfm?fa=view&id=2649>.

This testimony provides principles for crafting consumer relief and then describes our proposal for efficiently providing relief to low- and middle-income families.

Guiding Principles for Consumer Relief

In offsetting higher costs for low- and middle-income consumers, we recommend that policymakers follow five basic principles.

1. **Protect the most vulnerable households.** Climate change legislation should not make poor families poorer or push more people into poverty. To avoid that outcome, energy rebates should be designed to fully offset higher energy-related costs for low-income families.
2. **Use mechanisms that reach all or nearly all eligible households.** Eligible working households could receive an energy rebate through the tax code, via a refundable tax credit. Many other households are elderly, unemployed (especially during recessions), or have serious disabilities and are not in the tax system; energy rebates need to reach these households as well.
3. **Minimize red tape.** Funds set aside for consumer relief should go to intended beneficiaries, not to administrative costs (or profits). Accordingly, policymakers should provide assistance to the greatest degree possible through existing, proven delivery mechanisms rather than new public or private bureaucracies.
4. **Do not focus solely on utility bills.** For low- and middle-income households, higher electricity and natural gas prices will account for less than half of the total hit on their budgets from a cap-and-trade system. This is because goods and services across the economy use energy as an input or for transportation to market. Furthermore, about 20 percent of the households in the bottom quintile of the income spectrum — and many in the middle of the income spectrum as well — have their utility costs reflected in their rent, rather than paying utilities directly. Policymakers should structure energy rebates so they can help such families with the rent increases they will face as a result of climate policies, as well as with the higher prices that households will incur for gasoline and other products and services that are sensitive to energy costs.
5. **Preserve economic incentives to reduce energy use efficiently.** Broad-based consumer relief should provide benefits to consumers to offset higher costs while still ensuring that consumers face the right price incentives in the marketplace and reduce consumption accordingly. A consumer relief policy that suppresses price increases in one sector, such as electricity, would be



inefficient, because it would blunt incentives to reduce fossil fuel use in that sector. That would keep electricity demand elevated relative to what it would be if consumers saw electricity prices rise and would place a greater burden on other sectors and energy sources to provide the emissions reductions required under the cap. The result would be that emissions reductions would be more costly to achieve overall and allowance prices would be higher. Consumers might pay less for electricity, but prices would rise more for other items.

Providing Consumer Relief Efficiently and Effectively

To compensate for the effects that climate change legislation has on their purchasing power, we recommend that households be eligible for an energy rebate. The rebate would be based on an estimate of the increased costs that households would face as a result of the reduction in carbon emissions and would vary by household size. (Families with several children generally consume more energy and thus would face larger burdens from increased energy costs than single individuals or couples without children.)

We recommend that the rebate be delivered through three existing mechanisms, with appropriate coordination to ensure that people who both participate in a benefit program and file a tax return — and thus might qualify for a rebate through more than one delivery mechanism — receive the appropriate amount and are not overcompensated.

- **Most households qualifying for a rebate would receive it through the tax system.** For most households, a refundable income tax credit is the most efficient way to deliver an energy rebate. The credit should be provided in paychecks, if possible, through adjustments to employer tax withholding.

A tax-based system alone, however, would leave out a large share of households, particularly the lowest income households. According to the Urban Institute-Brookings Tax Policy Center, 15 percent of U.S. households do not file an income tax return, in most cases because they are not required to. Non-filers include seniors and people with disabilities who do not work and households headed by working-age adults who are jobless for some or all of the year, including some of the nation's poorest families with children.

- **Seniors, veterans, and people with disabilities who receive Social Security, Supplemental Security Income, or veterans' benefits would receive their rebate as a direct payment from the federal agency that provides their benefits.** This is similar to the policy of direct payments to these individuals that was included in the economic recovery legislation enacted in February.
- **State human service agencies would deliver rebates to low-income families.** Households participating in state human service programs such as food stamps, and other low-income households that choose to apply, would receive their monthly energy rebates through the debit-card systems operated by the state human service agencies that administer food stamps and other assistance. Every state in the nation operates such a system, and these systems have proved to be highly effective.

Setting the Rebate Amount

The amount of the rebate would be based on the average dollar impact on the budgets for the group of consumers that policymakers decide should be fully compensated. If policymakers decide that families in the middle of the income scale should be fully compensated for their loss in purchasing power, the rebates could be set at the average purchasing power loss of households in the middle fifth of the income distribution (varied by household size). If policymakers decide to use a somewhat smaller share of the auction proceeds for consumer relief, they could set the rebate amounts at somewhat lower levels, such as the average loss to consumers in the next-to-the-bottom fifth of the income distribution.

The Energy Information Administration would be tasked with determining the annual rebate amounts. That could be done using an approach similar to the one followed by the Congressional Budget Office in estimating how the costs reflected in the total value of the emissions allowances would fall on families in different parts of the income distribution.²

For example, if the rebate were set at the average estimated loss in purchasing power to households in the middle quintile and the emissions cap were set to achieve a 15 percent emission reduction relative to what emission levels would be without a cap, then we estimate that the annual rebates (in 2009 dollars) would be \$700 for a household of one and \$1,300 for a household of three.³ (Due to economies-of-scale factors, rebates for larger households need not equal the rebate for a one-person household multiplied by the number of people in a household.)

I'll now discuss in more detail each of the rebate components.

The Tax Component

Most households receiving an energy rebate would receive it as a refundable tax credit, which would be broadly available to low- and middle-income households. The credit would be available to anyone who files a federal tax return and whose income is below the eligibility limit set for the rebate; tax filers would simply look up the size of their credit in a tax table similar to the one used now for the Earned Income Tax Credit. Like other refundable tax credits, the energy rebate would phase in as income increased over some income range and then would phase out as income rose above a specified income level. The tax credit preferably would be provided throughout the year as an adjustment to employer tax withholding.⁴

² Congressional Budget Office, "The Distributional Consequences of a Cap-and-Trade Program for CO₂ Emissions," testimony before the Subcommittee on Income Security and Family Support, Committee on Ways and Means, U.S. House of Representatives, March 12, 2009.

³ These are CBPP projections following a methodology similar to that used by CBO to estimate the distributional impact of an emissions reduction of this size. These estimates are based in part on past work by CBO and may be revised when CBO updates that work.

⁴ If the tax credit is provided throughout the year via an adjustment to employer tax withholding, some other elements of the rebate proposal described would be modified accordingly. For example, low-income working families that also receive food stamps would not receive a rebate through the human service agency if their employer were adjusting their tax withholding and providing the rebate through their paycheck.

Direct Payments to Federal Beneficiaries

Among those most likely to be missed under the tax-credit mechanism are lower-income seniors and people with disabilities who rely primarily on Social Security or other benefits and are not required to file income tax returns. To reach this group, the most effective policy would be for the Social Security Administration, the Department of Veterans Affairs, and the administrator of the Railroad Retirement program to provide energy rebates directly to people receiving Social Security, Supplemental Security Income (SSI), veterans', or Railroad Retirement benefits. Married beneficiaries would receive the energy rebate for a household of two; individual beneficiaries would receive the energy rebate for a household of one. The recently enacted economic recovery legislation calls for a similar payment to be made to these beneficiaries in coming months. We recommend that the payments to these beneficiaries be made quarterly.⁵

Rebates through the State Human Service Delivery Mechanism

The group that would not be reached through either a tax credit or direct payments from federal agencies such as the Social Security Administration would be very low-income households (primarily families with children) that have very low or no earnings over the year and do not receive Social Security or other similar federal benefits. The best mechanism to reach this group is to provide energy rebates through state human service agencies that already provide food stamp assistance, Medicaid, and other benefits to a broad array of low-income households. States could readily “piggy back” the climate credit onto the existing Electronic Benefit Transfer (debit card) systems that all states use to deliver food stamps and, in most states, other forms of assistance, including cash aid.

State human service agencies already have the infrastructure in place to gather information about families' incomes, evaluate eligibility, and issue payments through their existing EBT systems (which they use for food stamps) or another electronic payment mechanism. Delivering an energy rebate through existing state eligibility systems and delivery mechanisms would be far less costly to set up and administer than virtually any alternative. This mechanism also would ensure that the lowest-income families — the group that would be in the greatest danger of utility shut-offs and that generally has the most difficulty managing money — would receive their rebates on a monthly basis throughout the year.

The Food Stamp Program does especially well in reaching low-income families with children — 83 percent of eligible families with children participate. Poor households that do *not* receive food stamps but that meet the eligibility criteria for food stamps (income below 130 percent of the poverty line and limited assets) and wished to receive the energy rebate could apply for the rebate through their state human services agency.

Coordination Mechanisms

The three-pronged delivery mechanism described here could result in some people qualifying for an energy rebate from more than one source because they participate in one or more of the relevant

⁵ Payments made more frequently than quarterly might be difficult to administer, since these agencies would need to match beneficiary data so they do not provide more than one rebate to individuals who are beneficiaries of more than one program.

programs and/or also file an income tax return. Coordination mechanisms, described in the appendix to this testimony, would be employed to avoid overcompensation.

Rebate Mechanisms Would Reach Nearly All Low- and Middle-Income Families

Approximately 95 percent of households in the bottom quintile of the income distribution would be reached automatically under this proposal, because they already receive SSI, Social Security, VA benefits, or Railroad Retirement, already participate in the Food Stamp Program, or already file an income tax return and have earnings. More than 98 percent of households in the next two quintiles also would be reached automatically.⁶

Why Rebates Are Superior to Other Forms of Consumer Relief

As the foregoing discussion indicates, rebates can be an effective way to deliver consumer relief. They can be provided easily through the federal tax system, agencies like the Social Security Administration, and state human service electronic benefit delivery systems, with no need for new agencies or bureaucracy at the state or federal level. Also, rebates protect households against the loss of purchasing power from higher energy-related prices without blunting consumers' incentives to respond to those higher prices by conserving energy and investing in energy efficiency improvements. Because energy-related products will cost more, households with the flexibility to conserve energy or invest more in energy efficiency will get more value for their budget dollar by taking these steps than by using their rebate to maintain their old ways of consumption. At the same time, rebates help households that can't easily reduce their energy consumption to avoid a reduction in their standard of living.

Other proposals for consumer relief generally lack one or more of these advantages and, in some cases, also pose other serious problems.

Payroll or Income Tax Cuts

Some have proposed using climate change revenues to cut payroll tax rates or individual or corporate income tax rates. Such options would be far less effective than a refundable tax credit in preserving the purchasing power of low- and middle-income consumers.

In its analysis of trade-offs in the design of cap-and-trade legislation, CBO found that if all the revenue from auctioning emissions allowances were used to reduce payroll tax rates, households in the bottom 60 percent of the distribution would get a smaller benefit from the tax cut, on average, than they would lose from higher energy prices.⁷ Those in the next 20 percent would come out

⁶ These estimates use Census Current Population Survey data for 2005 augmented by the Urban Institute's TRIM data, which account for underreporting of certain benefits. A modest fraction of low-income households might not receive the full amount of the rebate for which they qualify. This would happen if a household received a rebate through the human service agency for only part of the year and did not qualify for an additional amount through the tax rebate mechanism. Our analyses show that only 7-8 percent of low-income households would receive less than half of the full rebate amount.

⁷ Congressional Budget Office, "Tradeoffs in Allocating Allowances for CO2 Emissions," April 25, 2007, http://cbo.gov/ftpdocs/89xx/doc8946/04-25-Cap_Trade.pdf; and "Options for Offsetting the Economic Impact on Low-and Moderate-Income Households of a Cap-and-Trade Program for Carbon Dioxide Emissions," letter to the

even and the top 20 percent of the population would get a tax cut that *exceeded* their increase in energy costs. Using all the auction revenues to cut corporate taxes would be even more regressive. In contrast, using auction revenues to provide households rebates that vary by family size but do not increase as income climbs would not have these regressive effects.

The main argument for using climate change revenues to cut tax rates rests on the concept of economic efficiency. Economic analysis suggests that charging firms for emitting pollutants (as under a cap-and-trade system) could dampen economic activity. By cutting tax rates at the same time, policymakers could reduce these economic efficiency losses. But, the economic efficiency gains CBO identifies are modest, and the effect of the tax rate cuts that produce those modest gains would almost surely be to leave low- and middle-income consumers worse off, despite the economic gains, and to cause inequality in the United States to widen further.⁸

A recent study by Resources for the Future reinforces the CBO analysis.⁹ The study finds that the benefits of cutting marginal tax rates would mainly go to upper-income individuals. In contrast, providing rebates to low- and middle-income consumers would result in the best outcome for those consumers.

A reduction in payroll tax rates does not fare as well as a flat rebate on distributional grounds: the size of the benefit from a payroll tax cut is higher for those with higher earnings, and seniors and others without earnings would receive no rebate. The first concern can be partially addressed by switching from a cut in payroll tax rates to a rebate of payroll taxes paid up to a fixed cap. Workers above a certain modest level of earnings would all receive the same size rebate. Workers with very low earnings, however, would receive only a partial rebate, and people with no earnings would still be left out.

Those problems can partly addressed by switching to a refundable income tax credit based on the amount of payroll taxes paid (up to a maximum amount) and making seniors and people receiving federal disability benefits eligible for a similar size tax credit.¹⁰ At that point, the modified payroll tax proposal would look a lot like our proposed low- and-middle-income rebate, although it still would leave out people who lack earnings and are not elderly or have disabilities, such as people

Honorable Jeff Bingaman, Chairman, Committee on Energy and Natural Resources, United States Senate, June 17, 2008, <http://www.cbo.gov/ftpdocs/93xx/doc9319/06-17-ClimateChangeCosts.pdf>.

⁸ For low- and moderate-income consumers not to be worse off under a proposal that uses all of the auction proceeds to lower tax rates, the additional economic activity generated by the tax cut would have to be so great that it raised workers' incomes by enough to increase their after-tax income by more than what they lose due to higher energy prices. Credible estimates of the economic efficiency gains from using climate change revenues for tax-rate reductions show those gains to be very small, however, compared with what would be needed to produce such a result. For example, in the analysis that CBO has relied upon to estimate the efficiency gains under an approach that uses all of the auction proceeds to cut tax rates, the efficiency gains would be equal to only 0.3 percent of GDP. That is far too small to offset the net loss that low- and middle-income consumers would bear as a result of losing more from higher energy prices than they would gain from the reduction in tax rates.

⁹ Dallas Burtraw, Rich Sweeney, and Margaret Walls, "The Incidence of U.S. Climate Change Policy: Where You Stand Depends on Where You Sit," Resources for the Future, September 2008, <http://www.rff.org/News/Features/Pages/ClimatePolicyOptions.aspx>.

¹⁰ Gilbert E. Metcalf, "A Proposal for a U.S. Carbon Tax Swap: An Equitable Tax Reform to Address Global Climate Change," The Brookings Institution (Hamilton Project), October 2007.

who are unemployed during a recession and single mothers with very young children who are temporarily out of the work force. That could be addressed by including our low-income EBT proposal and by making direct payments to people receiving Social Security, SSI, VA, or Railroad Retirement.

Energy Efficiency Programs

Measures to encourage or require investments in economic efficiency are important — they can reduce the overall demand for energy, thereby limiting the size of the hit to consumers' pocketbooks from increased energy-related prices under an emissions cap. Energy efficiency programs are not, however, a credible *substitute* for rebates as a means of addressing the impact of climate change legislation on consumers' budgets.

There are two main reasons for this. First, existing weatherization and other energy efficiency programs currently operate on a small scale and would likely take years to scale up to reach a substantial portion of the population. Until now, the Weatherization Assistance Program, which helps low-income households make their homes more energy efficient through measures such as better insulation and newer appliances, has served only about 100,000 homes a year.¹¹ Even if the program is expanded to the point that it reaches 1 million households a year, which would require a huge buildup in effort, it would take decades just to reach the 38 million low-income households that are eligible for weatherization assistance. Rebates, in contrast, can reach tens of millions of low- and middle-income people immediately.

Second, the commonly discussed energy efficiency programs generally focus on home energy efficiency. As noted, higher home energy costs account for less than half of the loss in household purchasing power that would be caused by an emissions cap. To provide full relief to households, the energy efficiency measures would have to be so effective as to compensate not only for the increased costs in home energy but also for the increase in the cost of gasoline and other products. That is far beyond what is realistic.

Using Utility Companies to Provide Consumer Relief

Some have proposed routing funds for consumer relief through local utility distribution companies (LDCs). While relying on LDCs may seem reasonable at first blush in light of concerns about increased utility bills, this approach is unwise for several reasons.¹²

First, utility companies do not routinely collect information on their customers' incomes. To target assistance at customers within a particular income range, utility companies would therefore have to set up new bureaucracies to collect and audit income information. Covering the large costs of building an infrastructure at each utility company to gather and verify income information for millions of customers would require substantial government subsidies. Such subsidies would pay for an infrastructure that essentially duplicates what public agencies already do. Making households of *all* income levels eligible for utility company assistance would avoid this particular difficulty. But

¹¹ See the LIHEAP Annual Report to Congress for Federal Fiscal Year 2005.

¹² See Chad Stone and Robert Greenstein, "Why Utilities Are Not Well-Suited to Deliver Relief to Low- and Moderate-Income Consumers in a Climate Bill," Center on Budget and Policy Priorities, February 18, 2008.

that approach would spread the funds much more thinly across the population and make it far less likely that low- and moderate-income consumers would be adequately protected from higher prices.

Second, past experience suggests that utility company programs will miss large numbers of consumers. The only existing federal program that delivers assistance to low-income households through utility companies is the “Lifeline” telephone discount program, administered through local phone companies. That program reaches just *one-third* of eligible low-income households.¹³ In addition, the households whose utilities are built into their rents might not receive adequate compensation.

Third, a utility company approach is aimed at electricity and natural gas bills, and hence fails to address the full impact of climate legislation on consumer budgets. With *over half* of the impact of climate change legislation on consumer budgets coming as a result of higher prices for a range of other goods and services, including gasoline and food, relying on utilities to deliver consumer relief would leave many low- and middle-income consumers with a large uncompensated hole in their budgets.

Fourth, routing consumer assistance through utility companies artificially lowers households’ utility bills and blunts the “price signal.” People who do not realize that energy costs are going up will be much less likely to take steps to conserve energy or seek out energy efficiency improvements. A rebate, in contrast, protects consumers’ purchasing power without blunting the incentives created by higher energy prices.

Fifth, establishing a formula for allocating emissions allowances equitably among utilities would pose problems. There are roughly 3,300 LDCs in the electricity sector (plus additional natural gas retail distributors not affiliated with electric utilities), making it extremely difficult to design an appropriate formula. For example, basing the allocations to LDCs on each utility’s share of total electricity delivered or its share of total emissions — the approaches often taken by legislative proposals that rely on LDCs to provide consumer relief — would shortchange utilities that serve a disproportionate number of low- and moderate- income consumers, because their consumers’ per-capita energy consumption is likely to be lower than the per-capita energy consumption of more affluent households.

Sixth, a major obstacle to relying on utilities to deliver consumer relief, either through reductions in consumers’ bills or through energy efficiency measures, is the uneven quality of regulation and enforcement of utilities across the states. Most utility customers are served by investor-owned utilities whose rates and practices are regulated by state public utilities commissions. Regulators have to work closely with the industry they oversee, and states vary considerably in the degree to which the regulators have successfully avoided being “captured” by the industry. In such a heterogeneous regulatory regime, it would be difficult to provide the federal oversight necessary to make sure that the federal revenues from auctioning emissions allowances are used appropriately to protect consumers and invest in cost-effective energy efficiency improvements, rather than being siphoned off in part to overhead and profits.

¹³ Matt Fiedler, “Lessons from The Telephone Lifeline Program,” Center on Budget and Policy Priorities, July 18, 2008. Available at <http://www.cbpp.org/7-18-08climate.pdf>.

Finally — and perhaps most important — this approach would fail to protect consumers effectively and would be inefficient and wasteful. Policies that suppress consumer price increases in the electricity sector, as the utility company approach would do, blunt incentives to reduce fossil fuel use in that sector. That keeps home energy demand for electricity and natural gas elevated and puts a greater burden on other sectors to provide the emissions reductions required to meet the cap. The result is that emissions reductions would be more costly to achieve, allowance prices consequently would be higher, and costs for other energy sources and energy-related products would rise even more. As a result, the overall hit to consumers' budgets would be mitigated only partially by the tens of billions of dollars of allowance value devoted to this rather inefficient approach.

Conclusion

Climate change legislation that limits greenhouse gas emissions need not squeeze the budgets of low- and middle-income families. Well-designed consumer relief can restore to these families the purchasing power they would lose as a result of higher prices for energy-related products. Such consumer relief can be financed with a portion of the revenues from the auctioning of emissions allowances under a cap-and-trade system, leaving significant auction revenues available for other climate-related priorities.

A new refundable energy tax credit, coupled with Electronic Benefit Transfers for the lowest-income households and payments to seniors and veterans from the Social Security Administration and Department of Veterans Affairs, would be the most effective way to provide consumer relief to low- and middle-income households. Other proposed mechanisms suffer from significant flaws and would produce considerably less consumer relief per dollar of cost.

Appendix Coordination Mechanisms

Under the energy-rebate proposal outlined here, three mechanisms would be employed to coordinate the delivery of rebates through the tax code, the Social Security Administration and Department of Veterans Affairs, and state human services agencies.

1. State human service agencies would not provide climate rebates to individuals who receive Social Security, SSI, veterans' benefits, and Railroad Retirement benefits. The state agencies collect and capture detailed information on the sources of income for each household member for benefit eligibility purposes, so they could readily adjust the rebates provided to these households through the Electronic Benefit Transfer system to adjust for those household members who are receiving their rebates through these other programs.
2. At the end of the year, SSA, the Department of Veterans Affairs, and the Railroad Retirement agency would provide a 1099-type tax form to individuals to whom these agencies had made rebate payments and also would provide this information to the IRS. Payments received through the federal benefit programs would, on a dollar-for-dollar basis, offset the energy tax credit for which such individuals otherwise would qualify as part of a tax filing unit for that year.
3. Finally, at the end of the year, state human service agencies would provide information to adults who had received energy rebates through their state EBT system during the year. The information would show the number of months during the year that these individuals received energy rebates. (The same information would be provided to the IRS.) Households that file a tax return would be asked if they had received energy rebates through this mechanism, and if so, the number of months the rebates were received. Any energy tax rebate for which the household otherwise qualified through the tax system would be reduced proportionally, based on the number of months that the filer and/or the spouse had received rebates through the EBT mechanism. For example, if the household head received energy rebates through EBT for six months, the tax unit's energy tax credit would be reduced by 50 percent.

As noted, if the tax rebate is provided throughout the year through an adjustment to employer tax withholding, some modifications to these coordination mechanisms would be made. For example, the system would be designed so food stamp recipients who were employed would not receive a rebate through the human service agency if their employer were providing the rebate through the paycheck mechanism.

Under either scenario, these coordination mechanisms would require some new activities by state and federal agencies. Since the cap-and-trade policies would not become effective immediately and the emissions cap likely would be modest in the first years, there would be lead-time to implement the coordination mechanisms effectively in the period between enactment of the climate legislation and actual implementation of the rebates.