BEFORE THE COMMITTEE ON ENERGY AND COMMERCE,

SUBCOMMITTEE ON ENERGY AND ENVIRONMENT

HEARINGS ON THE AMERICAN CLEAN ENERGY SECURITY ACT (ACESA) OF 2009

APRIL 23, 2009

TESTIMONY OF ROBERT J. MICHAELS, PhD

My name is Robert J. Michaels. I am Professor of Economics at California State University, Fullerton and an independent consultant. I am also Senior Fellow at the Institute for Energy Research and Adjunct Scholar at the Cato Institute. None of today's remarks are the official positions of any of my affiliations or clients.

I hold an A.B. from the University of Chicago and a Ph.D from the University of California, Los Angeles, both in economics. I have performed research, published and spoken on developments in the electricity and gas industries since the 1980s. I have analyzed retail and wholesale competition in a restructured electricity industry, relevant markets and market power in electricity generation, gas pipelines and electric utility mergers, issues in the governance of Regional Transmission Operators, the Federal Energy Regulatory Commission's (FERC) policies on monitoring of regional energy markets, the changing economics of vertically integrated utilities and policy proposals on a national Renewable Portfolio Standard (RPS). I have most recently undertaken research on the economics of a "Smart Grid." My work has appeared in peer-reviewed journals, industry publications including *Public Utilities Fortnightly* and legal publications including *Energy Law Journal*. I have testified before, among others, the FERC, the California Public Utilities Commission, and this Subcommittee's predecessor in 1996. A full biography is attached to this testimony.

I will begin with a discussion of California energy policy, with which I am quite familiar, because California has already begun its own implementations of laws and regulations that resemble those of the American Clean Energy and Security Act. Its experience does not bring optimism about what the bill will produce nationally:

1. California's 2001 RPS law, calls for 20 percent of 2010 power deliveries from renewables. Regulatory uncertainty and opposition to new generation and transmission have left the state with the same percentage of its 2007 power supply coming from renewables as it had in 2001.

2. Per capita power consumption in California has been roughly constant since the mid-1990s, unlike other states where it has risen. Advocates who have credited this achievement to efficiency measures like those in the draft bill have an untenable case. Two major facts explain California's constancy: its buisiness climate has induced massive outmigration of industrial electricity users (whose use is included in the per capita figures), and its restrictive land use policies have substantially increased the number of persons in a typical dwelling unit.

3. Advocates of the bill's and cap-and-trade climate policies frequently cite studies made for the California Air Resources Board (ARB) which purport to show that they will bring the state a net economic stimulus. None was peer reviewed before being made public, and after seeing them all five reviewers were worse than critical. One from the Pew Center on Global Climate Change said that the studies give “the appearance of justifying the chosen package of regulatory measures rather than evaluating it or looking at policy options.” Another from Harvard's Kennedy School of Government said that "the economic analysis is terribly deficient in critical ways and should not be used by the state government or the public for the purpose of assessing the likely costs of ARB’s plans."

4. California utilities have filed a series of cost-benefit analyses of their "Smart Grid" plans with the state Public Utilities Commission. Southern California Edison's original study of smart meters and electronic operations produced a present value net *negative* cash flow of nearly $500 million. Its filing a year afterward found a small positive cost-benefit figure. The difference came from changed assumptions about demand response and an assumption that the company would be able to remotely control air conditioning and appliances in homes and businesses.

Building on the California experience I move on to this panel's subject, "Allocation Policies to Assist Consumers." It is an odd choice of topic because the draft legislation is virtually silent on both allocation and assistance. The breadth of the bill's subject matter and the financial scope of its programs ensure that it will have massive effects on both households and small businesses. There are important uncertainties about its consequences because critical policy details remain unspecified, most importantly

the allocation of emissions allowances. Nevertheless we can infer some consequences, and they are disturbing. Put simply, this is the most profoundly anti-consumer legislation ever brought before a Congress. Its acknowledged purpose is to raise energy prices to all Americans, and in doing so it will make America less competitive in an ever more competitive world. For reasons they can best explain, administration officials including the Secretary of Energy are on record as favoring higher prices.

As important as the higher prices are the proposed policies that will increase them. Every major provision of the bill is at base a tax, and every one of them is called something else. The renewable electricity standard (RES) for utilities is a tax on conventionally produced electricity. The nation is still within reach of competitive power markets that comply with environmental regulations. But a nationwide RES would replace the competition to reduce power costs with a requirement that more be generated from costly "renewable" sources. The most important of these, wind power, remains uncompetitive after decades of subsidies, and produces only when the wind blows. The tax aspect of the RES is cleverly concealed – none of it will appear on the federal books. Instead this bill will force utilities to purchase renewables, leaving state regulators no choice but to fold their costs into the bills of households and businesses who will have no choice about the resources producing their power.

Another tax turns up in the bill's proposed auction of permits (allowances) to emit carbon, after possibly giving some away to politically favored businesses. The official term is auction, but the real term is tax. The easy way to see this is to look at plans for spending the revenue. Details are not yet firm, but those under discussion include consumer rebates, paydown of the deficit, and financing of health policies. The only possible sources for these funds are debt and taxes, and this is a tax. Like other taxes, allowance charges compel business owners to divert funds that could have otherwise been used to operate their firms and employ people. Those who believe that respending of revenue from allowance auctions will create jobs have been conspicuously silent about jobs that will be destroyed in businesses that must purchase them.

The bill's effects start with scarcer and more expensive energy, but hardly stop there. What happens in energy markets will to varying degrees increase the prices of all other goods and services that use energy in their production. The higher prices mean lower standards of living for the American consumers who purchase them. They also mean that American goods become less attractive to foreign buyers than those from competitor nations that are attempting to develop their energy sectors rather than downgrade them.

This bill's entire thrust is to make energy needlessly scarce, and then somehow conclude that this action is good for the economy. Workers who work with more talented workers are more productive than those who labor alone, workers with more advanced equipment are more productive than those without it, and workers with better and more abundant energy sources are more productive than those without them. Workers forced to work with fewer and more costly energy resources produce less, not more. Scarce energy "creates jobs" by making workers less productive so that it takes more of them to get something done. What this bill really will create is not prosperity, but a less productive, less competitive economy with lower incomes, less opportunity, and less wealth to hand on to future generations.

Thank you for the opportunity to testify. I will be happy to answer any questions.