The Carbon Leakage Prevention Act (H.R. 7146)

Output-Based Allowance Allocation for Emissions-Intensive U.S. Industry

Rep. Jay Inslee (D-WA) and Rep Mike Doyle (D-PA)

Introduction

If Congress passes a cap-and-trade policy to reduce domestic greenhouse gas emissions, there is some concern that doing so would have adverse economic impacts on U.S. industry. In particular, the competitiveness of energy intensive U.S. manufacturing could be compromised if our major trading partners do not establish comparable climate policies. The chief concern is that such conditions would lead industrial firms to divert new investments and production to manufacturing facilities located in countries without commensurate regulations, leading to domestic job loss and substantial increases in greenhouse gas emissions abroad, a phenomenon commonly referred to as "carbon leakage."

However, a well designed cap-and-trade program can reduce the competitive disadvantage and avoid the carbon leakage problem through targeted measures for certain domestic U.S. industrial sectors, in conjunction with complimentary efforts by the Administration to address the core problem of uneven (carbon) costs through international climate change agreements.

As a stop-gap measure, through output-based emission allowance distribution, The Carbon Leakage Prevention Act would temporarily level the carbon playing field for U.S. manufacturing facilities until essential international climate agreements have been successfully negotiated.

Section-by-section:

Sec. 1 Short Title
Sec. 2 Findings
Sec. 3 Purposes
To distribute emission allowances to certain manufacturing facilities in eligible industrial sectors to prevent carbon leakage while also rewarding innovation and facility-level investments in efficiency upgrades and performance improvements.

Sec. 4 Definitions
The term “output” means the total tonnage, or other standard unit of production, produced by a manufacturing facility. [note: since this is drafted as an amendment to a generic, comprehensive, economy-wide cap-and-trade bill, several general “placeholder” definitions are also necessary.]

Sec. 5 Distribution of Emission Allowances to Certain Energy-Intensive Manufacturing Facilities
Up to 15% of total emissions allowances available, under the cap, are distributed annually to eligible manufacturing facilities.

To minimize carbon leakage caused by a domestic climate policy, the EPA Administrator determines which manufacturing facilities should be eligible for free allowances through a rule based on an assessment of some key factors. Such factors include the carbon emissions intensity of industrial processes and how readily producers can pass along additional costs to customers.

In general, emissions allowances are distributed to eligible facilities on an output basis, with compensation provided for both direct and indirect compliance costs. For direct compliance costs, allowance distribution is calculated by multiplying a covered facility's output by the sector average tonnage of greenhouse gas emissions per unit of output. Similarly, for indirect costs passed on by utilities, allowance distribution is calculated by multiplying a covered *or uncovered* facility's output 1) by the "emissions intensity" of each facility's electric power supply and 2) by the sector average electricity use per unit of output [note: natural gas is assumed to be regulated at the point of combustion and any free allowances distributed upstream, to electric power providers, may be deducted from the indirect allocation provided under this provision].

To avoid over compensating the most efficient plants and to preserve the overall integrity of the program, owners or operators of facilities performing at the sector average would be reimbursed for 85 percent of their direct and indirect compliance costs.

Sec. 6 Reports to Congress

Every 2 years the Administrator reports to Congress, in consultation with the Commerce Secretary, the Energy Secretary the Secretary of State and the U.S. Trade Representative about the impact of carbon leakage on domestic industry the extent to which this provision is addressing the problem.

Sec. 7 Modification or Elimination of Distribution of Allowances to Energy Intensive Manufacturing Facilities

Depending on how international negotiations, agreements and other governmental activities are playing out, one of two things could happen. The President could find that the competitive disadvantage caused by our domestic climate policy has reduced, so compensation under this program may be limited accordingly, pursuant to an administrative rulemaking. Alternatively, the President may make a determination that the competitive disadvantage casued by domestic climate policy is no longer significant, in which case compensation delivered under this provision is eliminated.