Testimony of Preston Chiaro on behalf of Rio Tinto

Before the Senate Environment and Public Works Committee

Legislative Hearing on S. 1733, Clean Energy Jobs and American Power Act

29 October 2009

Madame Chair and members of the Committee, I greatly appreciate the opportunity to testify today. My name is Preston Chiaro, and I am Chief Executive for Energy and Minerals for Rio Tinto, the largest diversified mining company in the US, and one of the largest diversified mining companies in the world. Our US assets include coal holdings in Colorado, Wyoming, and Montana, copper in Utah, copper projects in Michigan and Arizona, borates in California and talc in Montana and Vermont, as well as an aluminum smelter in Kentucky, with over 15,000 US employees all told.

Rio Tinto believes that emissions of greenhouse gases from human activities are contributing to climate change and that avoiding human caused changes to the climate is an important international goal. The mining and metals sector is exposed both to the effects of climate change and to climate change policies. This is because:

- We produce for the most part commodity products, which are dependant on global markets.
- Our business is very capital intensive, and operations are very long lived investments are typically made looking 20, 30 or more years forward.
- Many of these operations are very energy-intensive, and successfully addressing climate change requires fundamental changes in the way the world produces and consumes energy.

Unmanaged climate change is a threat to our assets, our shareholders, and our employees, and also to civil society and political institutions in many of the countries in which we operate and across the globe. Rio Tinto is supportive of a strong global agreement on climate change. A strong global agreement can provide the economic, social, and political stability, and hence the investment certainty, that allows us to deliver value to our shareholders, products to our customers, and provide jobs to our employees.

As a consequence, our corporate climate policy since 2003 has been to partner with governments in the development of climate policy in all jurisdictions in which we operate, to reduce energy use and GHG emissions in our own operations, and to find low emissions pathways for all of our products. We have engaged both individually and through groups of like-minded stakeholders, such as the US Climate Action Partnership (USCAP) which we joined in 2007, and the Canadian Environmental NGO-Industry Cap and Trade Dialogue, which formed only recently and includes our Canadian aluminum, iron ore, titanium dioxide, and diamond businesses and the Canadian businesses of some of our fellow USCAP companies. Our work through groups such as these allows

us to leverage our views and collectively speak to the center of the political spectrum that is so essential for achieving a sustainable policy solution.

In all of the jurisdictions where we operate, we tend to focus on three features of climate policy that need to be addressed at both a national level and in a global context. A global framework is ultimately essential because the challenges which we would like to address in a US context today are faced elsewhere as well. These features will provide for:

- Accelerating the development and deployment of low emissions technologies. Carbon capture and storage will play a very important role in coal-dependent countries like the United States,
- Minimizing the cost of climate policy through market mechanisms and other cost containment provisions, and
- Avoiding carbon leakage through transitional compensation for energyintensive, trade-exposed (EITE) industry.

Low emissions technologies

The role of technology is to reduce the cost of meeting our future emissions targets. Deployment of existing low-carbon technologies, including nuclear power, energy efficiency, and renewable generation technologies, is absolutely essential but existing technology is not sufficient for reaching the aggressive targets set in Waxman-Markey and that Kerry-Boxer and the Administration advocate. Government incentives for the accelerated development and deployment of low emissions technologies will be critical, including low-emissions energy and industrial technologies. Our advocacy for the funding of low-carbon technologies is not an argument against the level of the targets, which we believe are consistent with the USCAP recommendations and are required in order to address the climate imperative. Rather, the funding of low-carbon technologies is intended to ensure we reach those targets at as low a cost as possible.

Under a climate-constrained world we will have to change the way that we produce and consume energy, and this is no more evident than in the way we use coal, the fuel supplying about half our own electricity and 40 percent of global electricity. The coal challenge faced by the US is the same one faced by coal-dependent economies around the world, although the situation is even more complex for developing countries seeking to provide electricity at low cost to 1.6 billion people currently living without it. Our own commitment to the domestic use of CCS is demonstrated through our company's investments in projects such as the Hydrogen Energy project in Kern County, California. Hydrogen Energy has proposed a new hydrogen-powered electricity generation facility for the Kern County area that, when fully operational in 2016, would store most of its carbon-related emissions.

Coal-based energy will play an outsized role and it provides an important challenge because of the volume of emissions associated with its use. We feel the USCAP coal recommendations stand the best chance of transforming coal into a low-emission energy source. The USCAP recommendations, which are fully reflected in both Waxman-Markey and Kerry-Boxer, include support for carbon capture and storage (CCS) demonstration plants, the development of a regulatory framework for carbon sequestration, financial incentives for deploying up to 72 GW of CCS, and a phased-in performance standard with a mandatory retrofit for all coal plants built this year forward.

Cost containment

A global approach will rely on global carbon markets to transmit price signals for GHG reductions as broadly as possible. In fact, commoditizing carbon is the best path forward to minimize the cost of achieving GHG reductions, as businesses like our own will treat carbon like any other input cost, and seek to reduce that cost. Trading across jurisdictions via integrated markets will help to reduce costs even more, allowing for greater progress towards an overall target. Integrated carbon markets can provide an important vehicle for developing countries to join global efforts to reduce emissions. In particular, we see great mutual advantage from a continent-wide GHG compliance market, beginning with the US and Canada. This larger market will enhance the liquidity of both systems and represents an important step in the direction of developing a strong global framework.

Some observers invariably question whether we should trust markets with such an important task. We believe that we need strong markets in place precisely because it is so important for our efforts to be successful. Markets are unparalleled in their ability to leverage and direct private sector investment, integrate all available information, and help participants to understand market expectations through price signals, share risk, and in the process minimize the marginal costs of reducing GHG emissions. As a commodity producer, we are naturally very comfortable with commodity markets and prefer this approach to government mandates. We feel that the problems with markets are largely known and can be addressed with strong oversight and market regulation. Where markets may fail to address important issues such as carbon leakage, the necessary remedies are well understood, and we stand ready to work with the chairman and the committee to explore these options.

The Kerry-Boxer bill includes many of the key market features that we would like to see such as a broad, inclusive cap and compliance flexibility through banking and borrowing. These and other features in the bill will keep prices from getting so low that they discourage investment or from getting so high that they lead to larger economic dislocation and generalized demand destruction. We also support the bill's widespread access to domestic and international offsets to help contain costs, and the development of rigorous measurement, monitoring, reporting, and verification (MRV) procedures to ensure that offsets are high-quality, and feel that these will ultimately be far more successful at reducing emissions than any arbitrary limitations on the use of offsets.

Transitional compensation for Energy-Intensive and Trade-Exposed industry

The final globally-based policy feature that needs to be in place in US domestic policy is some safeguard against carbon leakage. Carbon leakage is the migration of emissions, jobs, and industry from countries with carbon regulation to countries without regulation. Climate policy leaders in both EITE industry and the environmental community have found common ground in calling for nations to recognize and adjust for first-mover costs in order to prevent leakage. We support the Waxman-Markey and Kerry-Boxer use of output-based rebates for EITE industry, and feel that when a globally level playing field returns, competitive advantage should be on the basis of uncompensated carbon cost.

Because the problem of leakage will diminish as we move towards a strong global framework, the support should be considered transitional in nature, and not viewed as a

permanent solution. In Australia and elsewhere, we advocate for transitional compensation to last until 80 percent of an industry globally is covered by comparable climate policy.

Other Approaches to Markets, Technology, and Preventing Carbon Leakage

We expect to see continued efforts to promote alternatives to the market- and technology-based policies that we see as critical for success, and that likewise some see trade-based measures as a possible solution to prevent leakage. These alternatives are obviously well-intentioned, and appeal to certain constituencies. However, the alternatives fare poorly when projected onto the entire economy, and even worse when projected globally.

Regarding markets, we all realize that it is not sufficient to put a market in place and hope for the best. Markets need a clear set of rules and strong oversight to implement these rules. Congress is well positioned to consider what these rules should look like and provide appropriate jurisdictional oversight.

Others will suggest that command and control methods may be superior at implementing the latest abatement technology. We argue that markets by themselves will tip the private sector's decisions toward low-carbon technologies at lower cost than command and control approaches. Moreover, markets will be more successful than command-and-control at developing the new technologies we need.

To address leakage concerns, there is an alternative proposal for avoiding the loss of energy-intensive and trade-exposed industry to unregulated jurisdictions, called a border adjustment measure. Section 765 of the Kerry-Boxer bill is clearly a placeholder for such a provision. Rio Tinto is highly skeptical of border adjustments' ability to play a constructive role within a global deal. Border adjustments risk protectionism, retaliation from targeted countries, and the risk of protracted WTO litigation. Border measures would not promote freer world trade, or consensus building in global climate dialogues. For that reason, our first preference is for allowance-based rebate measures for preventing leakage.

Conclusions

Rio Tinto will continue to urge governments to negotiate a strong global agreement for addressing climate change. We are pleased that the market-based policy features which we have advocated, including incentives for the accelerated development and deployment of low emissions technologies, a variety of cost containment mechanisms, and transitional compensation for EITE industry are largely present in the Kerry-Boxer bill. We urge you to retain and support these features in any legislation as it works its way through the Senate.