Testimony of Jeffrey W. Hopkins
On behalf of Rio Tinto

Before the Senate Environment and Public Works Committee

Hearing on Economic Opportunities for Agriculture, Forest Communities, and Others in Reducing Global Warming Pollution

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Madame Chair and members of the Committee, Rio Tinto greatly appreciates the opportunity to testify today. My name is Jeff Hopkins, and I am a principal adviser on energy and climate policy 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 and the Powder River Basin of Wyoming and Montana, copper in Utah, copper projects in Michigan and Arizona, borates and talc in California and Vermont, and an aluminum smelter in Kentucky. We work hard to be the resource developer of choice, from the mineral exploration phase to mine closure and beyond.

Rio Tinto has had a climate change policy position since 1998, further revised in 2003, which recognizes and accepts the conclusions of the Intergovernmental Panel on Climate Change that emissions of greenhouse gases (GHGs) resulting from human activities are contributing to climate change, and acknowledges that reducing these emissions is an important international goal. Our corporate strategy for achieving this goal involves three basic tenets. First, we encourage governments in all the jurisdictions in which we operate to take action to reduce emissions. In the US this is exemplified by our participation in the US Climate Action Partnership (USCAP), a group of 25 businesses and five NGOs that last January released its *Blueprint for Legislative Action.* Second, we take a proactive stance at our own operations to reduce greenhouse gas emissions. Our thresholds for new investments take into consideration the eventuality of US and global agreements to reduce GHGs thereby ensuring our projects are developed in such a way that they will earn a fair return even in a carbon-constrained world. Third, we develop low emissions pathways for our products. Many of our products, such as

copper, aluminum, uranium, and borates, have positive GHG emissions attributes over their life cycle but nearly all are energy-intensive in production. Our thermal coal production is used in electricity generation, and emits high levels of carbon in use, but when paired with carbon capture and storage technology will allow for a drastic de-carbonization of US and other global electricity supplies.

The committee might ask how our attention to policy advocacy with governments, improving our own energy efficiency, and reducing the life-cycle emissions of our products fit with offsets, the subject of today's hearing.

But first, what is an offset?

An offset is a reduction in GHG emissions from an unregulated (i.e. uncapped) portion of the economy. Simply put, a cap and trade bill would require all regulated sources to submit allowances for their emissions, in order to demonstrate compliance with the regulation. There are a fixed number of allowances (the number of allowances is equal to the cap) and an offset purchased from an uncapped sector can be used in place of an allowance for compliance purposes. Because radiative forcing is mitigated equally by reductions from capped or uncapped sectors, the contribution of offsets to reducing overall GHG concentrations is in all senses equivalent to reductions from capped sectors. Reductions in uncapped sectors may be at a lower cost allowing for a more economically efficient emissions reduction. Entities that use offsets serve themselves, by buying a cheaper form of abatement, and serve the whole by relieving pressure on scarce allowances under the cap.

In HR 2454, a bill whose passage Rio Tinto supported and which we hope to continue to improve through the Senate, emissions levels for most of the US economy (84 percent, according to the US EPA) will be regulated by the cap and will, therefore, face a price signal that incentivizes emissions reductions. Offsetting mechanisms create a price incentive to reduce emissions in the non-capped portion of the economy, including agricultural and forest land use activities. International offsets create a funding

mechanism for emissions reductions in countries without carbon regulation, which would otherwise have little incentive to reduce their own emissions, even though these reductions may be relatively cost-effective. Allowing entities in the capped sector to pursue lower-cost reductions wherever they exist will enable us to progress farther and faster towards stabilizing global GHG concentrations. HR 2454 would allow up to two billion offsets to enter into the system, and the presence of these offsets is estimated to reduce the cost of allowances by 89 percent, compared to the case in which only domestic offsets, but no international offsets, are allowed. The US EPA analysis of HR 2454 demonstrates why Rio Tinto and USCAP call for ample offsets to contain the costs of climate regulation. Our objectives to improve energy efficiency at our operations and lower the lifecycle emissions of our products allow us to pursue and capture incremental gains, but the aggressive long-term targets contemplated in the US, the EU, Australia, and Canada absolutely require scalable abatement technologies including carbon capture and storage, which is pre-commercial and not likely to contribute significant amounts of abatement before 2020. Meeting short-term targets, such as the 17 percent reduction by 2020 in HR 2454, will require reliance on a broad portfolio of technologies, including renewable energy sources, some fuel switching, energy efficiency, and ample supplies of offsets, including offsets from domestic and international agriculture and forestry.

Rio Tinto has an offset strategy that is consistent with other Rio Tinto policies. We believe that trading emission reduction credits within jurisdictions in which we operate will deliver maximum value to the company. We hope to develop offset projects related to our core activities or our sustainable development objectives, including our commitment to Net Positive Impact on Biodiversity in the areas where we operate. We further hope to monetize these emission reductions, as well as purchase offsets, in order to reduce our overall compliance costs. We do not plan to meet our emission reductions solely through the use of offsets, and we will first look towards our own abatement opportunities where they are feasible and viable. Due to the energy-intensive nature of our business – supplying essential minerals and metals that meet societal needs and which contribute to improvement in living standards globally – we will never be a *carbon*

neutral business but we are nonetheless determined to find ways to continue to deliver shareholder value in a carbon constrained world.

In summary, we commend the Committee for its attention to the matter of offsets and their impact on overall compliance costs. We have several detailed suggestions on how to improve the legislation compared to the House-passed version (see Appendix). One area that I will highlight is that offset provisions attracted considerable attention in the days leading up to passage of HR 2454. However, this discussion largely was focused on concerns over who will regulate the supply side of the offset market rather than the demand side where we will mostly operate. From our perspective, we have yet to find any areas of disagreement regarding the regulation of offset quality. In particular we, and those organizations with which we speak with most often, agree that offsets need to be of the highest quality and have the strongest levels of oversight. In fact, we broadly agree on the operational definitions of quality criteria that would be used to assure that offsets will be real, verifiable, permanent, and additional to baseline emission levels. Rio Tinto sees delay and incompatibility across multiple country jurisdictions as the chief threats to a workable and effective offset regime, and encourage Congress to direct the Administration to work with international partners to develop offset protocols and regulations to assure the demand side that ample offsets will be available early on in any climate regulation scheme and will be consistent with clean development mechanism and successor agreements.

Other areas where we believe work is needed include enhancing the ability of the strategic allowance and offset reserve program to prevent price spikes, as well as strengthening the applicability of the forest carbon provisions. We look forward to working with the entire committee to further improve the bill and pledge to continue to cooperate with this Committee and others as they complete their work.

Appendix: Rio Tinto Recommendations to Improve the Offset-Related Provisions of HR 2454

These suggestions are offered in the spirit of improving the efficiency without damaging the environmental intent of the program.

1. Section 726 strategic reserve uses an ineffective formulaic (60 percent of rolling average price) approach to control allowance price volatility.
   Problem: Formulaic approach will not address problems related to a dash to gas, when high allowance prices encourage excessive fuel switching and contribute to natural gas price spikes that are damaging to the rest of the economy.
   Solution: Give an independent body discretion to release reserve (offsets first, then future allowances if necessary) to flatten price spikes, in particular those that encourage excessive fuel-switching in electricity generation

2. Section 811 does not allow uncapped methane stationary sources to qualify as offsets; EPA modeling shows that this would increase domestic offset capacity by 45 percent and reduce overall compliance costs.
   Problem: Methane from coal seams and landfill sources are likely to be regulated outside of the cap under a new source performance standard (Section 811), a very lengthy process with an unknown outcome.
   Solution: Instruct the Administration to develop protocols for reducing methane emissions from coal, allowing them to contribute to emissions reductions in the near term.

3. Section 722.d.1.The low limits on offsets will increase overall compliance costs
   Problem: Increase ability to exceed the current offset limit of 2 billion tonnes.
   Solution: Direct the offset integrity board and administrator for domestic agriculture and forestry programs to establish high-quality protocols for offsets.

4. Section 722.d.1.B 'applicable percentage' limit on offset use reduces compliance flexibility for covered entities, increasing their own costs and the costs of the overall program for everybody.
   Problem: A pro-rata, firm-level percentage limit on offset use will bind both aggregate and many firms' offset behavior in ways that reduce the overall use of offsets and raise the costs of the program.
   Solution: Allow entities to transfer and use any surplus remaining in their 'applicable percentage' limit to other covered entities.

5. Section 743 puts in place a requirement that all international offsets require a bilateral agreement with the US.

Problem: Negotiating these agreements will be a lengthy process at the same time that international climate negotiations are occurring.
Solution: The provision already requires EPA assurance that such projects meet the same rigor as reductions from the capped and uncapped US domestic sectors; country agreements aren't necessary. Rather, our international efforts should be focused on identifying project types, such as the forestry sector emissions reductions, that can readily contribute to filling offset pipelines.

6. Section 722.d.1.B puts in place a discount factor for international offsets after 2018, such that a covered entity must hold 1.25 credits to equal 1 allowance.
   Problem: The provision will discriminate emissions reductions by country of origin, reducing the overall effectiveness of the program to reduce costs and encourage international cooperation.
   Solution: Eliminate the discount placed on international allowances.