TESTIMONY BEFORE THE

UNITED STATES SENATE

COMMITTEE ON FINANCE

SUBMITTED BY

RUKSANA MIRZA
VICE PRESIDENT ENVIRONMENTAL
AND GOVERNMENT AFFAIRS
HOLCIM (US) INC.

HEARING ON

INTERNATIONAL ASPECTS OF A CLIMATE CHANGE CAP AND TRADE PROGRAM

FEBRUARY 14, 2008

INTRODUCTION

Good morning Chairman Baucus, Ranking Member Grassley, and Members of the Committee. It is a privilege to appear before you today. My name is Ruksana Mirza and I am the Vice President, Environmental and Government Affairs at Holcim (US) Inc. I am here to testify about Holcim's global experience with cap and trade legislation, and to offer suggestions to ensure that the implementation of a domestic cap and trade program in the United States is not undermined by the displacement of production of energy intensive products to countries with no or, less stringent climate change legislation. I commend you Mr. Chairman, and your Committee, for the leadership you are taking on this very important issue.

I sincerely appreciate the opportunity to speak on this issue, which, if not addressed appropriately, has the potential to result in economic disruption, with no environmental gain. Experience in the EU has shown that without measures to address the transfer of production to countries with lower environmental standards, significant emission reductions cannot be achieved in the domestic energy intensive industry.

HOLCIM IS A RESPECTED LEADER IN THE CEMENT INDUSTRY WITH EXTENSIVE EXPERIENCE IN CO2 EMISSIONS TRADING REGIMES AND INTERNATIONAL TRADE

Holcim Ltd is a worldwide leader in the building materials sector, with over 150 million tons of cement and almost 200 million tons of aggregates supplied annually. Holcim holds majority and minority interests in more than 70 countries on all continents. Holcim Ltd is a leader in sustainable development and for the last three years, has been recognized as the "Leader of Industry" by the Dow Jones Sustainability Index for the building materials sector. Holcim Ltd has extensive experience with CO2 emission trading regimes with 27 cement production facilities in 10 countries in the European Union Emission Trading System (EU-ETS).

Headquartered in Waltham, Massachusetts, Holcim (US) Inc. a subsidiary of Holcim Ltd, is a leader in the US cement industry. Holcim produces and supplies nearly 15 million tons of cement and cementitious products annually to 38 states. We have more than 2500 employees and over $1 billion in annual revenue. Over the last decade, we have invested nearly $1 billion to upgrade and expand our fourteen existing U.S. facilities and are now investing another $1 billion in St. Genevieve County near St. Louis, Missouri, to build the world's largest single cement production line. Still, this massive investment in capacity and efficiency upgrades is not enough to serve the Nation's need for cement, as the industry must import approximately 20 million tons of additional cement to meet the domestic demand. Cement is a critical component of concrete, which is an environmentally responsible building product used to build and repair our country's vital infrastructure, the fuel of economic growth. Nearly 50 percent of our product has an end use in the public sector in roads, airports, bridges, hospitals and schools.

Holcim has four regions in the United States, including the Atlantic coast and southern US, the Great Lakes and Mississippi River system, Texas and Oklahoma, and the Rocky Mountain region. We serve customers in 38 states from 14 plant facilities, located across the country, and from over 60 additional remote distribution sites, or terminals. While this is the first time Holcim has testified before the Senate Finance Committee, I am proud to say we have facilities that employ many of your constituents. Of our fourteen major plants, seven are represented here – for example:

Mr. Chairman, we have one in Three Forks, Montana;
Ranking Member Grassley another in Mason City, Iowa;
A plant in Catskill, New York, Senator Schumer;
A plant in Dundee, Michigan, Senator Stabenow;
A plant in Florence, Colorado Senator Salazar;
A plant in Morgan, Utah Senator Hatch; and,
Our Corporate Headquarters are located in your state Senator Kerry.

Additionally, we have operations in West Virginia, Senator Rockefeller; Arkansas, Senator Lincoln; Washington State, Senator Cantwell; Kentucky, Senator Bunning; Idaho, Senator Crapo and Kansas, Senator Roberts; as well as nineteen other states.

How Cement is made

Cement is produced from various abundant raw materials including limestone, shale, clay and silica sand. These minerals are ground and heated in large rotary kilns to temperatures as high as 3,400 degrees Fahrenheit. The heat of combustion fuses these materials into clumps of an intermediate material called clinker. When the clinker is discharged from the kiln, it is cooled and later ground with a small amount of gypsum to produce the gray powder known as portland cement. Different types of portland cement are manufactured to meet various physical and chemical requirements.

Portland cement manufacturing facilities use an enormous amount of energy. In fact, energy is the largest cost component in the manufacture of portland cement. The domestic cement industry is one of the largest industrial consumers of coal.

THE CEMENT INDUSTRY IS A GOOD EXAMPLE OF AN INDUSTRY WHICH FACES EXPOSURE TO INTERNATIONAL TRADE AND RISK OF CARBON LEAKAGE

The cement industry is experiencing robust growth fueled by sustained moderate economic and population growth. Continued large-scale investment in cement supply will be required to meet the United States' expected future consumption through further investment in domestic plants, import terminals, or both. Such decisions are likely to be made in the context of climate change legislation, sustained high energy costs, and moderate-to-robust economic growth among the world's transitional and emerging

economies, actions which may impact both the availability of cement in the international market and freight costs.

The cement industry has three characteristics that are shared by many other energy intensive industries:

- Its product is a strategic building material that is essential to the development of energy efficient infrastructure. Despite the energy and therefore carbon intensive nature of cement production, cement and concrete contribute significantly to the reduction of overall carbon emissions through their application in the construction of energy efficient buildings and highways. Nevertheless, it is a commodity which sells at about $90.00 a ton, making it impossible for the industry to absorb the significant cost of carbon emissions that would likely result from the implementation of a cap and trade program.

- The demand for cement is expected to grow significantly over the next couple of decades, both in the United States and globally. Domestic consumption of cement is expected to grow by 43 percent by 2030, reaching 183 million metric tons and reflecting a 55 million metric ton increase as compared to 2005's past cyclical peak level.

- Production of cement is highly capital intensive. Costs imposed on the U.S. cement industry by a cap and trade program are likely to discourage the considerable investment necessary to meet our increasing consumption domestically and increase our already significant dependence on imports of this strategic building material.

The potential international competitiveness impacts of a domestic cap and trade program for energy intensive industries such as cement are recognized in a 2005 study published by the Environment Directorate of the Centre of Tax Policy and Administration of the OECD entitled "The Competitiveness Impact of CO2 Emissions Reduction In The Cement Sector" which states:

"Indeed, given the last evolutions of the debate on GHG mitigation, it is clear today that regional rather than global policies will be implemented, at least for a while. Therefore, a distortion of competition may affect countries mitigating GHG emissions through the additional burden of tax policies, emission allowances... Such an asymmetric carbon constraint may of course have an impact on GHG-intensive industries competitiveness (loss of profitability and decreasing market shares, ultimately leading to relocation). Eventually, such fragmented policies might even be inefficient from an environmental point of view, if they generate relocations in countries that are more GHG-intensive because of their technological portfolio and their lack of environmental regulation. The competitiveness impact and the so-called "carbon leakage" due to this distortion is an argument against non global mitigation policy or at least in favour of compensations."

GLOBAL CHALLENGE OF CLIMATE CHANGE

Climate change and energy security are global challenges that will require full participation from all nations and that will represent a function of their technical and economical potential and socio-economic development.

Combining the need to reduce greenhouse gas emissions with economic growth requires improving the carbon and energy efficiency of production, products and consumption in all jurisdictions world wide. Holcim is committed to this effort.

It is clear that socio-economic development, mitigation and adaptation to climate change will require the further development of civil infrastructure and consequently will further increase the global demand for concrete and cement as the construction material of choice.

Socio-economic development of the growing population in developing countries will require construction of infrastructure such as railroads, roads, sewage systems, housing, hospitals and schools. Almost 40 percent of global primary energy consumption is for residential and commercial buildings and 25 percent is for transportation – with both sectors having very significant emission savings potential. However, realizing this potential will require renovation and new construction in more energy efficient buildings, public transport infrastructure and new power plants. Also, adaptation to climate change will require infrastructure works such as flood protection and residential housing to be more resistant to stronger wind forces.

TO BE EFFECTIVE IN REDUCING DOMESTIC AND GLOBAL CARBON EMISSIONS, A DOMESTIC CAP AND TRADE PROGRAM MUST CONTAIN PROVISIONS TO AVOID LEAKAGE OF CARBON EMISSIONS TO COUNTRIES THAT EITHER HAVE NO, OR LESS STRINGENT OBLIGATIONS. THIS CAN BE ACHIEVED BY ADOPTING A SYSTEM OF EQUAL RIGHTS AND EQUAL OBLIGATIONS FOR DOMESTIC PRODUCERS AND IMPORTERS

This proposal aims at **preventing leakage** of carbon emissions to countries with no, or less stringent carbon constraints by creating a **level playing field** between domestic producers and importers that is consistent with the World Trade Organization and the United Nations Framework Convention on Climate Change (UNFCCC).

Under this proposal, the scope of the domestic cap and trade program would be broadened to include both installations for the production and importation of energy intensive products. Import installations would be subject to the same rights and obligations as domestic production, including the obligation for monitoring, reporting and verification of emissions, surrendering of allowances and the ability to trade allowances. Monitoring Reporting and Verification guidelines dedicated to emissions at the site of production outside the United States would need to be developed. The allocation of initial allowances to importers would be on the same basis as for domestic producers.

Importers would be required to provide a certificate of emissions that occurred (at the site of production) for the production of the volume of goods imported into the United States plus the emissions from transport from that site to the import location in United States. The monitoring, reporting and verification rules must be the same for imported and domestically produced goods.

In the event that the importing installation is not able to provide a third party verified certificate of emissions at the site of production, a default emission value would apply. In order to create an incentive for developing countries to develop the capability to monitor, report and verify emissions at the site of production and export, the default emission value would be based on a rate that is higher than the US average. This would pave the way for these nations, particularly the major emitters, towards the adoption of fully comparable domestic climate change programs.

Such a system effectively prevents carbon leakage and places domestic production and importers on an equal level playing field with respect to carbon constraints, notably with similar terms as to the obligation of monitoring, reporting and verification of emissions, the obligation to surrender allowances at the end of each commitment year and the right to comply with the obligations in a flexible way through emission trading.

As such – through the importing installations - the exporting installations not only face the same carbon efficiency objectives but also have the same business opportunities in the event that they produce energy intensive products in a less carbon intensive manner than domestic industry.

Such a concept with equal rights and obligations is clearly non-discriminatory for all concerned players and as a result, is fully compliant with the rules of the World Trade Organization, and the UNFCCC and would allow the measures to take effect at the same time as a domestic cap and trade program.

THE EUROPEAN UNION RECOGNIZES THAT SIGNIFICANT REDUCTIONS IN DOMESTIC AND GLOBAL CARBON EMISSIONS CAN ONLY BE REALIZED IN THE ENERGY INTENSIVE INDUSTRY IF ADEQUATE MEASURES TO PREVENT LEAKAGE ARE IN PLACE

In the current EU Directive which covers the period 2005 to 2012, the issue of leakage is not addressed explicitly. Instead, the Directive speaks to the issue of the distortion of competition in Point 11 of Annex III, which states that National Allocation Plans may contain information on the manner on how competition from countries without carbon constraints is taken into account.

To date, National Allocation Plans have addressed the issue of competitiveness, primarily through the allocation system, whereby installations have been allocated a larger proportion of allowances.

In contrast, the recently published "Proposal for a Directive of the European Parliament and of the Council amending Directive 2003/87/EC" which aims to improve and extend the greenhouse gas emission allowance trading system, to 2013 and beyond, clearly addresses the leakage issue stating:

"The efforts for reduction until 2020 will be more significant than required by 2012. In the absence of comparable constraints for industry in third countries, there may be a risk of carbon leakage, i.e. relocation of production and thereby increasing global emissions."

The EU document goes on to say:

"…an effective equalization system could be introduced to put domestic production and import on a comparable footing. This could be by imposing requirements to importers that would be no less favourable than those to domestic installations, for example by requiring surrender of allowances."

CONCLUSION

As one of the largest producers of cement in the United States, Holcim (US) Inc. offers the following suggestions as the Committee deliberates over the international dimensions of a domestic cap and trade program:

- To remain globally competitive while achieving the environmental objective of a domestic cap and trade program, it is essential that the issue of "leakage" of emissions to countries with less stringent carbon legislation be adequately addressed. Otherwise, we risk economic disruption of local industry, with no environmental gain.

- To ensure that leakage protection measures are compatible with WTO rules and the United Nations Framework Convention on Climate Change, this should be implemented through a system of equal rights and equal obligations among domestic producers and importers. This requires a broadening of a domestic cap and trade program to include import installations.

- Leakage protection measures should take effect simultaneously with a domestic program and should remain in effect until comparable measures have been adopted by exporting nations.

- Including importers in the scope of a domestic cap and trade program creates a strong incentive for companies in exporting countries to adopt the same monitoring, reporting and verification system as domestic producers. This constitutes an important and essential first step for engaging developing countries in a global climate protection framework.

I sincerely thank you, Mr. Chairman, Ranking Member Grassley and Members of the Committee for your time and I again appreciate this opportunity to speak about issues vital to addressing the global challenge of climate change while ensuring the United States remains internationally competitive.

Ruksana Mirza
Vice President, Environmental and Government Affairs,
Holcim (US) Inc.