

**Statement of
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**Submitted for the Record
Committee on Small Business
U.S. House of Representatives
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American Clean Energy and Security Act
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Introduction

My name is Lawrence W. Kavanagh and I am Vice President, Environment and Technology, of the American Iron and Steel Institute (AISI). AISI represents 24 member companies in North America, and our members make 75% of the steel produced in the United States. Prior to the current economic downturn, the industry directly employed approximately 165,000 persons in the United States, supported a total of 1.2 million jobs overall and contributed \$350 billion to the economy annually.

First, let me thank committee members and staff for inviting us to participate in this process. I would like to begin with the steel industry's most important issue-competitiveness:

- The domestic steel industry is the lowest CO₂ emitter among world steelmaking nations as a result of billions of dollars of investment in process improvements;
- The steel industry has reduced energy per ton of steel produced by 33% since 1990, and as a result of this achievement, our processes are pushing against their energy limits as defined by the laws of physics;
- It is preferable, both economically and environmentally, to produce steel in the USA;
- Steel markets are global, which means that customers have the option to purchase steel from countries not adopting similar climate measures, so U.S. manufacturers cannot pass through increased energy costs.

The new green economy will require a major investment in our infrastructure. Steel will be a significant part of that investment. Despite the current downturn, the World Steel Association projects that world steel demand will double by

2050. Much of this steel will form the backbone of any green grid--- for example, generation sources like wind power are much more steel intensive than their fossil-fueled equivalents. The steel for these new energy alternatives should be built here in the United States, the best place to make steel in the world, from an environmental standpoint.

Our ability to stay competitive in the world economy means we need fair and strong trade laws that are rigorously enforced. *The same is true for climate – we need fair climate laws with global reach that can be enforced.* It goes without saying that in a market open to imports, such as ours, any legislation that undermines the competitiveness of U.S. mills will encourage steel production to leave this market in favor of markets with *lower* environmental standards. Such an outcome will necessarily result in *higher* volumes of greenhouse gas emissions worldwide. In other words, any climate change legislation that does not adequately account for competitiveness issues will have precisely the opposite effect from that intended by its supporters. To prevent this unintended consequence, we believe there are fundamental components that must be part of any climate policy to ensure fairness and global reach including:

1. Emission allowances stability: The steel industry has been concerned about energy use and CO₂ emissions for two decades and thus the processes we operate today are very near their limits regarding these two parameters. Therefore, there is very little incremental CO₂ emissions reduction possible until new technology is available. This means that a general pool of free allowances that all energy intensive sectors compete for and that declines in size over time does not work. Steel requires a sufficient and stable pool of free allowances while we work to develop these new technologies.
2. Energy Costs: Domestic climate policy will increase energy costs, a significant competitiveness issue for steel for the reasons noted. Our industry uses coal, electricity and natural gas in great quantities. The increased cost of each of these energy sources, beyond the price of allowances themselves, needs to be offset (e.g., through the direct grant of allowances) in order that our global competitiveness is not harmed.
3. Border adjustment: An effective WTO-legal border adjustment mechanism must be a significant part of any climate proposal to account for the cost burden of more stringent climate policies here vs. our international competition.

The discussion draft addresses these points to varying extents. We would like to bring three key components of the draft to your attention and offer suggestions for strengthening these provisions.

1. Grants of Allowances for Direct Emissions Energy Intensive Manufacturers

This important provision of the bill reflects the authors' understanding of the challenges facing energy intensive industry and we appreciate its inclusion in the bill. However, we believe several changes need to be made including: directly designating steel as a trade-affected industry; stabilizing the pool of allowances so that the overall size is sufficient to support all industries that qualify and ensuring that the size of the pool does not decline until new technologies are available commercially. The full measure of allowances needs to be granted to energy intensive industries, not 85% of the full amount. The energy efficiency of steelmakers today is such that a 15% reduction is not possible and would serve merely as a penalty and not an incentive. Finally, if additional sectors not envisioned by the drafters are included in this same pool of allowances, a 15% allotment will fall far short of providing the necessary assistance for industry.

Regarding availability of new technologies, I want you to be aware that the domestic steel industry is aggressively developing technologies that hold the promise of a dramatic step-change in performance. To that end, the industry is steadily investing in so-called breakthrough technologies. The resulting transformational processes being developed over the next 15 to 20 years could result in a steel industry that is largely carbon-free. Widespread adoption of new technology historically has proven to take from two to three decades in our industry. We are currently supporting breakthrough technology projects at the Massachusetts Institute of Technology and the University of Utah.

2. Energy Price Volatility and Increased Energy Costs

All forms of energy (coal, natural gas and electricity) have the potential to suffer a dramatic increase in cost as a result of climate policy. The bill does not presently address coal or natural gas cost increases and uses power plant emissions to grant allowances as a proxy for electricity cost increases.

Power plant emissions are a poor surrogate for electricity cost increases as they only reflect the component of electricity cost attributable to the price of carbon. Much of the future increased cost of electricity will come from the cost of capital equipment related to any or all of the following: fuel switching, deployment of waste gas capture/regeneration technology, deployment of carbon capture and sequestration technology and deployment of wind, nuclear and other clean energy technologies.

Energy costs are 20% or more of the cost of making steel. It is therefore unmistakably clear that a sharp increase in total energy cost will affect our competitive position in the global marketplace. The bill needs a comprehensive energy impact formula that considers coal, natural gas cost increases and electricity compensates for them for trade-exposed and energy-intensive industries.

We have been advised it is difficult to separate historical market forces for energy commodities from the influence of carbon policy. We believe that sufficient history of regional energy costs exists to readily establish historical averages and ranges to compare against costs after a new climate regime is in place.

3. Border Adjustability

As proposed, the bill has a significant lag before any assessment of comparable action by our trading partners is made. Years pass before any counterbalancing action is taken to adjust for competitive advantages gained in other countries that invest far less in climate policy than domestic manufacturers. Such evaluations of comparable action need to occur at the same time domestic manufacturers are subject to regulation because any time lag offers significant competitive advantage to our competitors. Steel is a very cyclical business and even one or two years of legislated advantage will be enough to damage US producers who are, as noted above, world leaders in reducing CO₂ emissions.

Finally, we are concerned that the bill as written leaves sole discretion to the Executive Branch in determining the continued existence of competitiveness issues, developing country compatibility or job loss. Congress should have a defined role in this critical process before any competitiveness program is phased out.

Conclusion

It is very timely to talk about competitiveness issues as the Committee on Energy and Commerce moves towards reporting out this bill. As recently as eight months ago, our industry was running near full capacity and annually producing more than 100 million tons of steel. Today, we are producing less than one half of that amount as demand for steel and the products that contain steel, such as automobiles and appliances, has crashed. But even as demand has plummeted, imports of finished steel have hardly changed at all in real terms. The result of this behavior by our trading partners is that as a percentage of steel consumed in the United States, imports' share of the domestic steel market has doubled versus

a year ago at this time. Finished steel import market share in March was estimated at close to 30%, with China providing the largest volume of finished imports from offshore. Directly relevant to your climate policy considerations, China's steel industry now accounts for 50 percent of the world's production of CO₂ from steelmaking – approximately equal to all the other steel mills in the world combined. And according to a recent poll, only 18 percent of Chinese companies believe they could do well economically if they adopted sound environmental policies, as reported in a 2009 assessment of environmental regulation of the steel industry in China issued by the Alliance for American Manufacturing.

In light of these practices, legislation must address the anticipated time lag before other nations invest similarly in reducing carbon emissions.

We appreciate the opportunity to appear before your committee and hope that as this process moves along, the House will avoid "one size fits all" solutions. What works in one sector of our economy may not work well in another. In a real sense, whether domestic energy-intensive manufacturers will survive is a "transition rule" issue. So long as everyone has to play by the same rules, the domestic steel industry will compete and thrive. But if our competitors are granted an advantage, steel production will move offshore. The new energy efficient economy will require a lot of steel, the most recycled material in the world. Let's keep making it here in the USA, the best and cleanest place in the world to make it.