Testimony of
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Before the
U.S. House of Representatives Committee on Resources
Subcommittees on Forests and Forest Health and Energy and Mineral Resources

Joint Oversight Hearing on the
Effects of High Energy Costs on Americas Pulp and Paper Industry

and

The Potential for Expanded Use of Biomass for Energy

February 8, 2006

Chairmen Walden and Gibbons, Ranking Members Udall and Grijalva, and Members of the Subcommittees, my name is Tommy Smith and I am the Mill Manager for Potlatch Corporation's Cypress Bend paperboard mill near McGehee, Arkansas. I sincerely appreciate your time addressing the energy issues within our industry and exploring the possibilities for expanded use of biomass as an energy source for our industry and others.

Let me begin by giving you a brief overview of our industry from my point of view. There are five integrated pulp and paper manufacturing facilities in the state of Arkansas. Two years ago the sixth facility was shut down. In globally competitive markets the survival game for the rest of us has been to remain cost competitive. We have been very successful at the Cypress Bend facility in maintaining our facility assets to remain competitive from a technology standpoint. This has been a major challenge for us since our facility has been operating for almost 30 years. But I am very fortunate because I manage the newest facility in the United States that manufactures products that end up in paper plates, paper cups, and cartons for cosmetics, pharmaceuticals, food, software, and advertising signage for the entertainment industry. In contrast, the most recently built paperboard machine that competes with us started up in China in 2003. We have already seen their new products in some of our customers' plants.

From the southeast corner of Arkansas in the Mississippi Delta, we have competed and won when compared with some of the best in the world in terms of quality and service, and until just a few years ago, cost. Our employees, like many you have heard or will hear today, have competed and won in quality and productivity. In a mill built in 1977 to produce 450 tons per day, we routinely produce on average over 825 tons of paperboard per day with about the same number of workers we had in 1983. Unfortunately, we have had two reductions in force in our salaried work force and reduced the number of hourly workers through attrition since 1999 so that we could remain competitive. Since then, I have worked along with many others at the mill to cut costs from all areas to avoid further reductions in force. Through these cost reduction efforts we have accomplished some amazing things.

One of the most significant challenges we face in our industry, especially at our mill, is the high cost of energy. We have implemented several efficiency improvements to limit these costs, but energy remains a large concern for us. Since 2000 we have cut natural gas usage by 37% while increasing productivity by 14%. We have developed some rather unique operational solutions and invested in several capital projects to accomplish the reductions. I suspect most pulp and paper producers across the industry have made similar major usage reductions.

Unfortunately the reductions have not compensated for the increase in natural gas prices during the same period. In recent months, we have seen prices as high as $15 per MMBTU of natural gas, an increase of over six times the price in 1999. At these high levels, the competitiveness of our mill, and our industry as a whole, is severely limited.

In order for our industry to have an opportunity to compensate for the current and projected increased prices for natural gas, we have to make some fundamental changes. We believe expanding our use of biomass with new technology can provide a solution to our increased energy prices. We need your help to implement those changes.

Higher natural gas prices, coupled with the results of long term energy research projects, have led us to some interesting possibilities. Potlatch is an active member of the Agenda 2020 Technology Alliance, an industry-led partnership of companies, government researchers, and academic representatives. Working with the Department of Energy, USDA and other federal agencies, Agenda 2020 has pursued many successful research, development, and demonstration activities aimed at improving our energy efficiencies in an environmentally responsible manner. Potlatch has worked extensively with

the American Forest & Paper Association (AF&PA) to apply the benefits of the research within our company.

This has resulted in a concept of an integrated biorefinery within a pulp and paper manufacturing facility. In such a configuration, biomass from forest and agricultural wastes would be gasified, and partially used in the pulp manufacturing process instead of natural gas. Additional gases would be liquefied to produce liquid petroleum products or other chemical products. We are in the final phases of completing a feasibility study undertaken with Winrock International, the University of Arkansas at Monticello, the Division of Energy of the Arkansas Department of Economic Development and Agenda 2020 to confirm the economic viability of the project at the Cypress Bend facility. We have also put together an industry-wide advisory team for the study and project implementation, as we believe that this model can be replicated throughout the industry.

Initial indications are that the project could eventually reduce the natural gas usage at the mill by 80% and the electricity consumption by 60%. We believe we can virtually eliminate the need for fossil fuels at our mill by converting more residual forest wastes, agricultural wastes, and energy crops into synthetic gases that can be made into bio-fuels.

The project will meet the requirements of Section 932 of the Energy Policy Act of 2005 which authorizes lignocelluloses biorefinery demonstration projects. It is my understanding there will be two Funding Opportunity Announcements (FOAs) in early 2006 soliciting bids for commercial scale integrated biorefinery research, development, and demonstration projects. We fully intend to submit bids for these funds. However, the availability of the funds is dependent on Congressional funding of the $150 million proposed for the President's Biofuels Initiative, which was included in last week's State of the Union address and the Fiscal Year 2007 budget released on Monday.

This technology has the potential to produce clean, renewable biofuels and support our local and national economy through the combined efforts of agricultural producers, forest products producers, forest and farm landowners and the petrochemical industry. We believe the technology can be integrated into most manufacturing processes that have a high need for heat, such as refining, chemical processing, and steel production. In today's business environment, I do not believe any of the forest product producers have the financial resources to fund the project alone. Support for the project by our congressional delegation, local community, agricultural producers, others in the forest products industry, and other parties in the Arkansas delta region has been truly phenomenal. Our industry needs the support of the federal government, as well.

Thank you for allowing me the opportunity to testify this morning. I look forward to answering any questions the committee may have.