

Testimony of
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Mr. Chairman and Members of the Subcommittee, my name is Kim Smith, I am here representing the MeadWestvaco Corporation and am a proud member of the Pulp and Paper Resources Council (PPRC). We recognize the strong connection between our jobs and the issues that face our companies when they make business decisions. One of those issues is the cost of doing business and energy costs are top on that list.

The high cost of energy is having a very negative impact on U.S. manufacturers of pulp, paper, paperboard, and wood products. U.S. environmental policies of the past decade have encouraged increased consumption. Energy is the third largest operating cost for the forest products industry. In the pulp, paper, and paperboard sector of the industry, energy makes up 10-15 percent of total operating costs. Since 1972, this industry has reduced its average total energy usage by 17 percent through increased efficiencies in the manufacturing and production process. In addition, it has reduced its fossil fuel and purchased energy consumption by 38 percent, and increased its energy self-sufficiency by 46 percent. Although the industry is nearly 60 percent self-sufficient (using biomass), we also use natural gas, coal, fuel oil, tree bark and purchased electricity to meet the balance of our energy needs.

Annually, forest products companies purchase about 395 billion cubic feet of natural gas. The price of natural gas in 2003 was nearly double the average price for 2002, forcing the industry to spend almost \$1 billion more for the same quantity of fuel. This increased price for natural gas also significantly increases purchased electricity and the price of chemicals needed for our manufacturing operations. Higher natural gas prices have the additional effects of increased transportation costs.

Five years ago, the American Forest & Paper Association conducted research to determine the competitive position of U. S. manufacturers of paper and wood products as compared to our primary international competitors. Energy was the one area where our cost of production was slightly better than our competitors. Today, that situation is just the opposite. While the wellhead price of natural gas hovers between \$6 and \$7 per million British thermal units (BTUs) in the U.S., prices in the rest of the world are noticeably lower. Prices of natural gas our competitors pay in Western Europe are in the \$4 to \$5 range. Prices in Asia are around \$1.50, and in Russia the price for natural gas is less than \$1 per million BTU, putting our industry at a significant competitive disadvantage.

This disadvantage is on top of other competitive disadvantages we face. Our taxes are higher than those of competing nations, and there are unfair trade barriers to the export of our products. The cost of compliance with our nation's environmental laws is higher, and transportation costs are greater than anywhere else around the globe. Government restrictions are also limiting our access to fiber – even though our forestry stock has increased by 39 percent since 1952. If we cannot successfully address these challenges, the public demand for forest products will increasingly be filled by other nations who do not adhere to our high standards.

My company operates in a sector that is a good example of what industry is facing. At MeadWestvaco, more than 23,000 Americans are employed in jobs that allow them to support their families. MeadWestvaco's North Charleston mill, where I have worked for more than 17 years, has been a part of life in South Carolina since 1937. This facility has provided me and many others with the ability to support our families and provide opportunities for our children. Manufacturing jobs are critical to our state and our nation's economic health. MeadWestvaco provides extensive employee benefits, including medical and dental benefits, pension plans, and 401(K) retirement plans. Our government policies should do everything that can be done to preserve these jobs.

In the forest products industry alone, we have lost more than 120,000 high paying manufacturing jobs and closed more than 220 plants since 1997. These are the direct job losses and do not count the substantial multiplier effect of additional service jobs that have been lost as a result of the lost manufacturing activity in these mostly rural communities in America. High energy costs have contributed to many of the plant's closings.

I believe the most important thing the Congress can do to turn around the recent manufacturing job losses is to address the energy and environmental policies that are the root cause for the supply and demand imbalance of natural gas. Congress should enact a new energy policy that promotes the environmentally responsible development of domestic oil and gas reserves and it should revise environmental laws to eliminate the unnecessary bias toward natural gas.

Policies to Promote Additional Supply

While the energy bill passed by the House of Representatives in 2003 made some modest reforms, it fell short of dramatically changing the natural gas supply picture in the near-term. For example, there are significant reserves in the Rocky Mountains that can be accessed in a responsible way with little negative impact on the environment. Congress should enact legislation to reduce the barriers to this supply. In addition, expansion of transportation and infrastructure to bring additional natural gas to consumers from the Rocky Mountains, Alaska, Canada, and from overseas in the form of Liquefied Natural Gas (LNG) is essential to help keep gas prices affordable.

Permitting for new transmission and distribution pipelines takes too long to complete. It can take from two to five years to get the permits necessary for siting and construction of transmission and distribution pipelines and natural gas storage facilities due to unabated litigation. Congress and the Administration should work to minimize the bureaucratic red-tape and to expedite the permitting process for siting and construction of pipelines and natural gas storage facilities. The Department of Interior has recently issued some new regulations that could speed the permitting process. But, ultimately, Congress must act to ensure that bureaucratic process does not prevent timely development of natural gas supply.

Likewise, there are huge reserves in the Arctic National Wildlife Refuge (ANWR). A small amount of exploration and development in ANWR could mean substantial new supply available to meet the demand of a growing economy and provide a rebound for U.S. manufacturing and the many families and communities that depend on these jobs. Congress has approved incentives for building the Alaska Natural Gas Pipeline and must follow through with provisions to ensure it will be built in a timely fashion.

Federal restrictions also limit access to offshore natural gas resources in the Pacific, Atlantic, and Eastern Gulf of Mexico Outer Continental Shelf (OCS). Congress should, as a first step, require a federal inventory of the gas reserves in the OCS. Environmentally responsible technologies exist that could allow additional offshore production without harming the environment; but, first, we must know the extent of the reserves. In the long term, Congress must relax the current restrictions and allow for environmentally responsible access to some of these OCS natural gas reserves.

The September 2003 National Petroleum Council study agreed that one of the biggest potential sources of new natural gas supplies would come from developing OCS resources. OCS resources can be developed safely with minimal impacts to the environment using new, safe drilling technologies. The OCS resources of Maritime Canada are being successfully and safely developed today, and the Government of Canada is reviewing the potential to open offshore Western Canada for exploration and development.

Concepts such as state revenue sharing, increased state authority in leasing decisions, and expanding and equalizing states' boundaries, provide an opportunity to overcome resistance to OCS development. By providing creative incentives to share revenues from developed OCS natural gas resources, states are encouraged to be part of the solution. In fact, by increasing states' authority in leasing decisions, much of the need for the current OCS moratoria could be eliminated.

Additional federal research is also important to bring about potential new longer-term sources of energy and energy-related technologies. Research and deployment of technologies such as clean coal, coal gasification, biomass and gasification of lignin in spent pulping liquors must continue to be pursued. For decades, many paper and wood products mills have provided the majority of their own energy production, running their paper machines using electricity largely supplied by mill-operated, on-site electric generators.

We have embraced energy diversity. The industry has used both by-product biomass fuels (such as lignin in spent pulping liquor, hog fuels, bark, and wood chips) and purchased fossil fuels to produce steam and electricity used in its manufacturing processes. Our mills produce approximately 43 percent of all on-site generation of electrical power in the manufacturing sector. Successful development and full implementation of spent pulping liquor and biomass gasification programs could make our industry a net exporter of renewable electricity — removing some 35 million tons of carbon emissions from the air and generating nearly 22 gigawatts of electricity by 2020.

The introduction of gasification would enable far more efficient power generation via combined cycle or fuel cell prime movers, as well as the production of additional value added products like liquid transportation fuels, hydrogen or even chemicals. In fact, the synthetic gas made from black liquor and biomass gasification could potentially produce 25 million gallons of liquid fuel per day, thereby reducing U.S. dependence on imported oil.

These initiatives entail substantial risk for an already capital-intensive industry. Important R&D remains to be completed to prove the gasification technologies can work without adversely impacting mill operations. Continued cooperation with the federal government is crucial to reducing risk to a level that will allow significant industry participation.

Similar initiatives are underway in the areas of clean coal technology and coal gasification. These technology development programs are essential to creating new and diverse sources of clean energy. Importantly, without guaranteed access to the grid, these new power sources will not be developed and implemented. For this and other reasons, it is critical that Congress maintain existing initiatives for combined heat and power (such as in the Public Utility Regulatory Policies Act), which can be as much as 80 percent efficient in the conversion of input fuel to useful energy.

Additionally, research on new technologies is needed to make inaccessible supplies of natural gas available, and turn projected resources into proven reserves. Many of the nation's existing supplies of natural gas are now in harder to reach areas.

Policies to Protect the Environment and the Economy

The Congress must re-examine current environmental policies that promote the exclusive use of natural gas for power generation at the expense of other fuel sources that can be used in an environmentally sound manner. Significant technology advancements have occurred in the past 20 years to make coal a viable fuel source for power generation that is not damaging to the environment. Environmental rules should be updated to reflect these technological advancements and to encourage a more diverse mix of fuels for power generation and other industrial applications.

Manufacturers are subject to a host of environmental laws that require control technologies that are natural gas intensive. The recent bias in regulations toward environmental control technologies that favor incineration is imposing substantial new demand pressures on natural gas. Let me give you a specific example in my industry. The Pulp and Paper Cluster Rule, which was promulgated in the mid-1990s, requires paper mills to use an incineration technology to burn small amounts of volatile organic compounds such as methanol. This chemical is found in mouth breath in greater quantities than at paper mill fence lines. The technology used is called a "regenerative thermal oxidizer" (RTO), and it runs on a natural gas system. The end result is higher energy costs, higher emissions of SO₂ and NO_x for questionable benefits. For example, in the last two years operating costs to run the technology at one paper mill increased \$1 million per year to \$1.5 million. This increase was directly attributable to natural gas cost increase.

Permitting requirements under the Clean Air Act often prevent fuel-switching, which could in the short-term alleviate part of the industrial demand for natural gas. Allowing flexibility in permitting to accommodate fuel switching under shortage conditions could help in some limited circumstances. As a result, companies are prevented from managing energy costs through the use of other environmentally responsible fuels.

Conclusion

High energy costs, and particularly the high cost of natural gas, threaten the long-term viability of U.S. manufacturing and its contribution to the American standard of living. Since 2000, MeadWestvaco's North Charleston mill has seen energy costs rise by more than a third, making it even more challenging to compete in the highly competitive paperboard industry. Congress can, and should, take action to increase the supply of natural gas and update environmental laws to reflect the technological advances that have occurred in the past decade, and to reduce the bias toward use of natural gas. Research incentives should include demonstration and deployment of technologies, if the goal indeed is to encourage adoption of new technology by industry. Abundant and affordable energy sources are critical to the competitiveness of U.S. manufacturers, to the communities in which they operate, and the Americans they employ. Many U.S. businesses have been crippled by high natural gas prices that are driven in large part by U.S. energy and environmental restrictions. As the economy begins to rebound, it is critically important that Congress act quickly to ensure that government policies promote rather than restrict the responsible development of our nation's abundant supply of natural gas — both onshore and offshore.