Written Statement for the Record
Submitted by
The American Forest & Paper Association
To
United States House of Representatives
Committee on Ways and Means
Hearing on "Energy Tax Incentives Driving the Green Job Economy"
April 14, 2010

The American Forest & Paper Association (AF&PA), on behalf of its member companies, is pleased to submit this written statement for the record of the Committee on Ways and Means Hearing on "Energy Tax Incentives Driving the Green Jobs Economy" that was held on April 14, 2010.

AF&PA is the national trade association of the forest products industry, representing pulp, paper, packaging and wood products manufacturers, and forest landowners. Our companies make products essential for everyday life from renewable and recyclable resources that sustain the environment. The forest products industry accounts for approximately 56 percent of the total U.S. manufacturing GDP. Forest products companies produce $200 billion in products annually and employ approximately 1 million people earning some $50 billion in annual payroll. The industry is among the top 10 manufacturing sector employers in 48 states.

AF&PA applauds the Committee on Ways and Means for focusing on energy tax incentives as an important way to expand business activity, create and maintain jobs, reduce dependence on fossil fuel and non-renewable energy sources, promote energy efficiency, and sustain the environment for future generations of Americans. As the leading producer and user of carbon-neutral renewable biomass energy, AF&PA and its member companies welcome the opportunity to discuss the important role of energy tax policy in achieving these goals.

In recent years, federal energy tax legislation has sought to encourage renewable energy sources and alternative fuels by expanding production tax credits, providing energy investment credits, enhancing depreciation deductions, and creating new tax-favored financing mechanisms. The growth and importance of these energy tax incentives makes it imperative that such incentives be delivered in a neutral manner that does not favor some energy producers over others or some energy uses over others. Government policies to encourage additional renewable energy should not create winners and losers between existing renewable industries and new power generation. In addition, incentives should be carefully designed to avoid imposing barriers to future innovation.

The forest products industry produces and uses renewable energy for manufacturing operations and is a significant contributor to our country's existing base of renewable energy. On average, forest products facilities meet 65 percent of their energy needs from renewable biomass. Much of that is thermal energy or steam used in our facilities' manufacturing process to dry paper, for example. We also generate 28.5 million MWH annually of biomass-based electricity, which we use to power our facilities, and sometimes to sell to third parties. Through increased efficiencies in the manufacturing and production process, AF&PA members' overall total energy use per ton of production at pulp and paper mills has decreased by 26.6 percent since 1972, and by 11 percent between 1990 and 2006.

Our increasing efficiency and greater reliance on biomass energy also has enabled AF&PA members to significantly reduce the use of fossil fuel and purchased energy, much of which also is generated from fossil fuel. From 1972 to 2006, the fossil fuel component of the AF&PA member mill energy mix decreased by over 55 percent, and the use of both fossil fuel and purchased energy has decreased by 56 percent. From 2004 to 2006, AF&PA members reduced their use of fossil fuels and purchased energy per ton of production by 9 percent.

The forest products industry generates more energy from renewable sources than wind, solar, and geothermal combined. The industry has had limited success in qualifying for renewable biomass energy incentives but has a substantial amount of additional renewable energy capability. As policymakers seek to encourage rapid expansion of renewable energy sources, the forest products industry can and should continue to play an important role in furthering these goals.

We believe a level playing field between new and existing uses of biomass for renewable energy production is critical for manufacturers of paper and wood products to remain competitive in the markets for our products and in our procurement of wood as a raw material. As the demand for biomass-based power increases, AF&PA member facilities must compete with new market entrants for that biomass—the raw material for their products, as well as the source of their own renewable, carbon-neutral power. The ability of new market entrants to qualify for potential new renewable energy tax credits, while existing facilities' biomass-based energy may not, often puts existing forest products facilities at a serious competitive disadvantage.

As discussed below, we believe the Section 45 renewable energy production tax credit should apply to existing facilities for the full 10-year production period and should be expanded to energy produced and used onsite in manufacturing operations. In addition, we believe the Section 48 credit for combined heat and power facilities should be expanded and enhanced.

Section 45 Renewable Energy Production Credit

Section 45 of the federal tax code provides a credit of 1.1 cents per kilowatt hour of electricity generated from open loop biomass that is sold to a third party. Since 2004, forest products companies have been eligible for this similar renewable energy tax credit as wind, solar, and geothermal producers when they sell electricity generated by renewable biomass to third parties. However, those other industries are eligible for a higher credit of 2.1 cents per kilowatt hour. This credit applied to existing biomass facilities for only five years – 2005 through 2009 – compared to 10 years for all other facilities. It's important to note, however, that many facilities were not able to use the existing facility credit because of confusion created by an IRS ruling shortly after the 2004 existing facility credit was put in place. In 2008 the IRS rescinded the limitation, leaving companies with only one year of eligibility; four years fewer than Congress originally intended.

A major component of the electricity generated by forest products companies is used onsite in their manufacturing and processing operations, which has significantly reduced their fossil fuel use. The generation of electricity for onsite use is highly efficient because it avoids transmission and distribution losses compared to electricity that moves across the electricity grid. However, the industry's electricity generated from renewable biomass and used onsite is not currently eligible for the Section 45 tax credit.

The forest products industry seeks two things: 1) to extend the provision that allows existing facilities to benefit from Section 45 and 2) to strengthen Section 45 to include renewable biomass electricity used onsite.

AF&PA member companies believe that all generators and users of renewable energy should be treated the same. There are unintended consequences for the forest products industry from government mandates and incentives for new renewable energy production. Government policies to encourage additional renewable energy should not create winners and losers between existing renewable industries and new power generation.

It's not about getting incentives for doing "business as usual" – it's about treating desired behavior the same across all industries and taxpayers. For example, even though electricity utilities and forest products facilities produce the same kind of renewable energy, utilities get a tax credit for their electricity but forest products facilities do not unless they sell it to someone else. Renewable energy displaces fossil fuel whether it's sold or used onsite, so both uses should be treated the same.

So as new renewable energy generators come online and are able to claim additional tax incentives, existing biomass electricity generators such as those in the forest products industry become disadvantaged by the tax code. This stifles investment and creates disincentives for the industry to continue to increase its already substantial generation and use of biomass. All of this threatens domestic jobs and slows the full realization of domestic energy policy goals. Congress has sent a clear signal that maintaining existing jobs and creating new jobs, particularly in the field of renewable energy, is a priority. It should reaffirm a commitment to net job growth by maintaining a level playing field on tax policy.

Extension and expansion of Section 45 – as proposed in S. 870, H.R. 622, and

H.R. 2528 – will:

1. Encourage more renewable energy projects at traditional manufacturing facilities, thereby supporting existing jobs.
2. Increase energy efficiency since on-site use avoids transmission and distribution losses on the grid.
3. Sustain more than 360,000 jobs: 50,000 pulp and paper mill jobs, 150,000 related jobs associated with other products in the value chain (such as envelopes, shipping containers, or cartons), and 160,000 indirect jobs in supplier industries and local communities….plus an estimated 115,000 jobs (35,000 direct and 80,000 indirect) in the wood products sector.

Section 48 Energy Investment Credit for Combined Heat and Power

One of the most efficient means of utilizing energy is combined heat and power (CHP) or "co-generation." CHP is more efficient because it generates both thermal energy and electricity from the same fuel rather than generating thermal energy onsite and electricity at utility generators remotely. In general, CHP is about twice as efficient at using fuel as is utility technology, emits only half as much greenhouse gas as non-CHP electricity, and reduces transmission and distribution inefficiencies compared to electricity from the grid.

Section 48 of the federal tax code provides a 10 percent investment credit for new CHP facilities with electrical capacity of 50 megawatts or less. To further encourage investment in CHP facilities, we believe the Section 48 credit should be modified to increase the credit amount to 30 percent and remove the 50 megawatt limitation.

Section 48 Energy Investment Credit for Existing Facility Expansion

For both qualified closed-loop and open-loop biomass facilities, the investment tax credit (ITC) is available on the qualified property within the facility where the facility was placed in service in 2009 through 2013. Under IRS Notice 2008-60, where the qualified property is a modification or improvement to an existing facility, the IRS has set forth an 80 percent-20 percent rule for qualification for the ITC. Under this rule, if more than 20 percent of a facility's total value is attributable to older property placed into service prior to the effective date of the ITC provision, then the new equipment at the facility will not be eligible for the ITC. This has proved to be an overly restrictive rule and one that is contrary to the intended purpose of encouraging investments in renewable energy. The 80-20 rule should be repealed to allow expansion and reinvestment in existing facilities to encourage greater, cleaner energy production.

Section 1603 Grant In Lieu of Tax Credit

The American Recovery and Reinvestment Act of 2009 (ARRA) created a new federal government grant program under which a taxpayer can apply to the Secretary of the Treasury for a cash grant of 30 percent of the investment in qualified energy property (10 percent for small CHP, microturbine, small irrigation, certain geothermal) in lieu of the Section 45 and 48 credits. Property must be originally placed in service in 2009 or 2010, or construction of property must begin in 2009 or 2010 and be placed in service before 2014 for biomass facilities and 2017 for certain CHP facilities.

This program is an effective means of encouraging new investment in renewable energy facilities and should be extended beyond 2010. In addition, further clarification of the standards for determining when construction begins is needed.

One method for making the program more efficient would be to align the period of eligibility with existing placed in service dates. That is, the section 1603 program should provide that an eligible property is any qualified property placed in service before the expiration of the particular energy incentive's current placed in service expiration date. Thus, the option to elect the grant in lieu of the credits would be available for biomass facilities placed in service through 2013. This would eliminate the need for the current complex rules for determining when construction begins. Aligning the grant election with existing placed in service dates would both simplify the program and provide a more effective incentive.

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The forest products industry's commitment to sustainable forest management for the wood fiber used in manufacturing, and to renewable energy sources for the generation of electricity from the portion of trees not used in manufacturing demonstrates that a critical balance between maintaining our environment and business activity that creates and sustains jobs can be achieved.

Increasing renewable energy is a laudable and achievable goal, but it should not be at the expense of existing renewable energy production in the forest products industry. The expansion of Section 45 (and Section 48) will encourage more renewable energy projects at our manufacturing facilities, resulting in increased energy efficiency since on-site use avoids transmission and distribution losses on the grid. This will translate into jobs preserved and jobs created across America.

AF&PA and its member companies look forward to working with the Committee to help preserve jobs and expand renewable energy production.

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