

Brussels, Tuesday 30 June 2009

**To: US SENATE**

**CEPI comments on**

**'The proposal to clarify the types of fuels that qualify for the alternative fuels tax credit and eliminate from eligibility fuel derived from the processing of paper and pulp'**

**CEPI fully supports the proposal from Senators Baucus and Grassley to close the alternative fuels tax credit loophole and urges the US Senate to put an end to it as soon as possible to restore fair competition and a level playing field between the US industry and its competitors.**

There are indeed growing suspicions and even some evidences that further to the adoption of the fuel tax credit in the US:

- ***Some pulp & paper companies are able to lower their prices and are doing so;***
- ***Some pulp & paper companies are tempted to take less downtime, re-starting some idle mills or switching their production to market virgin pulp production;***
- ***EU-US trade flows start being distorted.***

**These behaviours lead to clear market distortions and constitute unfair competition.**

**In most of the largest European pulp and paper producing countries, the companies do not receive any subsidy for their production of black liquor / bio-energy or green electricity** and in the countries where such support schemes exist, these subsidies are granted under restrictive conditions, and are of an amount that cannot be compared with what the US Fuel Tax Credit scheme allows!

As a consequence of this loophole, one can see the start of **an escalation with the adoption of the Pulp and Paper Green Transformation Program by the Canadian government on 17 June**. This program intends "to provide pulp and paper mills with one-time access to C\$1 billion in funding for capital investments that improve the energy efficiency of their facility and encourage production of alternative energy from forest biomass". Pulp mills located in Canada producing black liquor between January 1st and December 31, 2009 are eligible for funding. Mills will receive funding based on C\$0.16 / litre – \$0.53 / gallon, i.e. very close to the US level - of black liquor produced until the C\$1 billion in funding is fully allotted. The funding can only be used by pulp mills for capital investments to improve energy efficiency or increase production of alternative energy.

**Without a clear signal from the US and a quick decision regarding the exclusion of any fuel derived from the processing of paper and pulp from the Fuel Tax Credit scheme, one can expect other national initiatives and protectionist measures to be announced in the coming weeks to offset the benefits received by the US pulp and paper industry.**



**Prices: *Some pulp & paper companies are able to lower their prices and are doing so – see Annex I***

Newsprint: in the 2<sup>nd</sup> quarter of 2009, prices have been pulled down – by 120 USD / tonne on the East Coast and up to 150 USD / tonne in some locations. Boise Inc. – a company that has some integrated kraft pulp production benefiting from the US fuel tax credit - started offering standard newsprint at 430 USD / tonne in June, a price that is considered by most newsprint producers in the US to be below cash costs. This represents a 24% lower level than current average newsprint price.

**Capacity management: *Some pulp & paper companies are tempted to take less downtime, re-starting some idle mills or switching their production to market virgin pulp production – see Annex II***

Downtimes: less downtime taken in the US during the 2<sup>nd</sup> quarter of 2009 than in most of the competing countries

Regarding market pulp production, most of the downtimes taken in North America have been registered in Canada. Only 23% of the total market pulp downtimes have been registered in the US against 77% in Canada. For information, US market pulp production represents about 45% of North America total market pulp production (Source: RISI).

Some southern US producers of kraft paper are expected to take less downtime because of the fuel tax credit.

Re-start: some idle mills have been re-started in the US

Domtar announced on 10 June that it would reopen one of its closed mills in the US by the end of June, adding close to 400,000 tonnes of hardwood pulp on the market, while it has simultaneously closed one mill in Canada. Domtar has benefited from the fuel tax credit for a few months already.

Switch: some companies decided to switch their pulp production

Some US companies like SFK have decided to switch production towards chemical pulp rather than de-inked pulp (pulp made of recovered paper). SFK has decided significant downtimes through July at its market de-inked pulp mills, though it has planned no downtime at its chemical pulp mills.

**Trade: *EU-US Trade flows start being distorted***

Imports: EU imports from the US have increased, while imports from other countries have been reduced significantly

During the 1<sup>st</sup> quarter of 2009, the EU27 imports of woodpulp from the US have increased by 2% compared to the 4<sup>th</sup> quarter of 2008, although the imports from all the



main suppliers to the EU have seen their numbers decreasing over the same period: Brazil -6%, Chile -8%, and Canada -14% (source: EU DG Trade, COMEXT database). Compared with the same period of last year, the EU27 imports of woodpulp from the US have decreased by 8%, although the imports from all the main suppliers to the EU have seen their numbers decreasing by 2-digit numbers over the same period: Brazil -14%, Chile -14%, and Canada -32% (source: EU DG Trade, COMEXT database).

Exports: EU exports to the US have significantly decreased, though EU exports to other countries have progressed

During the 1<sup>st</sup> quarter of 2009, the EU27 exports of woodpulp to the US have decreased by 39% compared to the 4<sup>th</sup> quarter of 2008, although the exports to all the main EU export markets have seen their numbers increasing significantly over the same period: China +57%, Turkey +14%, Indonesia +97% and India +35%. Compared with the same period of last year, the EU27 exports of woodpulp to the US have decreased by 72%, although the exports to all the main EU export markets (except Turkey) have registered a high growth over the same period: China +43%, Indonesia +43% and India +63% (source: EU DG Trade, COMEXT database).

These developments have been registered though the Euro has weakened against the US Dollar (or the US Dollar has gained strength) over the last months: -5% during the 1<sup>st</sup> quarter of 2009 compared the 4<sup>th</sup> quarter of 2008 and -13% during the 1<sup>st</sup> quarter of 2009 compared with the same period in 2008 (source: European Central Bank). One has also to note that the US currency is widely used on world pulp markets.

**Current EU bio-energy national support schemes: in most of the largest European pulp and paper producing countries, the companies do not receive any subsidy for their production of black liquor / bio-energy or green electricity**

In most of the largest European pulp and paper producing countries the companies do not receive any subsidy for their production of black liquor / bio-energy or green electricity and in the countries where such support schemes exist, these subsidies are granted under restrictive conditions, concern essentially new investments and only the share of the green electricity sold to the grid, are very limited and definitely not of the US magnitude.

In Austria, Finland and France, the pulp and paper industry does not get any financial support for biomass-based energy production. In France, some support to new 'green electricity' investments can be obtained under certain conditions, but not to existing plants. In Spain and Sweden, through some specific schemes such as certificates for bio-based electricity produced and sold to the grid and again under certain conditions, some pulp and paper companies can receive a very limited amount of money per tonne produced (less than 3% of the European average cash manufacturing cost for pulp), which is about 20 to 25 times less than what the US scheme allows!



## Annex I

### Prices: some producers have been able to lower their prices significantly

While contacts indicated that one supplier to the region will try to match the \$430 per tonne price in June, other newsprint producers stated they were unable to compete with prices that were substantially below cash costs for their operations. There has been some speculation that Boise's integrated kraft pulp operation is benefiting from the federal black liquor tax credit, which in turn has lowered costs for the entire mill (which also produces linerboard), allowing such a drastic cut in newsprint prices. Although the DeRidder mill can only supply around 5% of US demand for newsprint, such a low-priced offer on the market will have an impact as fierce competition for orders continue to pressure prices lower at a rapid pace through the summer.

Source: RISI, Paper Trader, May 2009

### Unprecedented second quarter newsprint price declines leave North American suppliers still looking for a market bottom

North American newsprint prices are collapsing at an unprecedented rate in the second quarter and there is no indication that the decline will stop until newsprint manufacturing becomes a loss-making business for many mills.

East Coast producers, who have been forced to bring prices into line with lower West Coast market levels, saw a devastating drop of \$120/tonne or 17% in the past two months.

And in some US locations, prices will drop another \$150/tonne next month.

The price for 30-lb newsprint in May declined to \$585/tonne on both US East and West Coasts, a \$50/tonne month-over-month drop, according to a survey by *PPI Pulp & Paper Week*. The 27.7-lb was \$620/tonne in May, a \$60/tonne decline.

This week, Boise began offering standard newsprint at \$430/tonne and 27.7-lb at \$460/tonne for June deliveries to customers in the five states surrounding the company's DeRidder, LA, mill: Mississippi, Louisiana, Texas, Arkansas, and Oklahoma, contacts said.

Source: RISI, PPI Pulp & Paper Week, 22 May 2009

### U.S. pulp company starts black liquor price war

By Gordon Hamilton 05-22-2009

The second shoe has fallen in the American black liquor tax rebate story: An American pulp and paper company has initiated a price war. And a B.C. company is right in the line of fire.

Kevin Mason, analyst at Equity Research Associates, was the first to report it in a research paper he released Friday. Mason says Boise Inc. has told all newsprint buyers in the five states surrounding its DeRidder, Louisiana mill, that it's dropping the price of its product to \$430 US a tonne. That's \$135 US a tonne, or 24 per cent, below average May newsprint prices of \$565 US a tonne. Boise swears it's not because it is receiving a black liquor rebate. [...] Boise produces black liquor in making pulp for its linerboard plant at the same site.

"The apparent justification for Boise's move is that it needs to run full on newsprint in order to maintain the low-cost performance of its linerboard capacity at that same facility," Mason says. Now, how can it maintain that low-cost performance best, you might ask? Could a tax rebate help? Mason thinks so. "It seems quite likely that the



economics encouraging the full operation at the DeRidder mill are being driven by the alternative fuel tax credits, although Boise claims that this decision was made independently of the tax credits."

Boise's move has set the cat among the pigeons. Mason told me in an interview that some other producers have been forced to match the price. But Richmond-based Catalyst Paper, which has a recycled newsprint mill in Arizona that sells into the same market, can't do it. Catalyst gets no tax credit for its recycled content. It's customers are now going to have to decide what they want: a recycled product or a 24 per cent discount. [...] So how can Catalyst, which is actually producing a real green product, compete?

"The fear now is that this shockingly low price won't be contained to just that region. North American newsprint prices were moving steadily lower toward cash-cost levels, but this recent move by Boise will speed up the race to the bottom," Mason says in the report. "As miserable as this newly proposed pricing is for U.S. producers, it is even more crushing for Canadian mills, especially as the Canadian dollar has climbed sharply over the past couple of months. Canadian mills obviously don't sell into the U.S. South, but as we have seen recently, geographic price-differentials are difficult to maintain in this industry."

SAN FRANCISCO, June 5, 2009 (PPI Pulp & Paper Week) - Sources this week said that the race to a bottom on North American newsprint market prices turned into a sprint, with suppliers desperate for orders quoting what one contact called "predatory prices" and others battling to hold their market share. Longtime industry veterans say they have never seen a market like it, and that "gossip and rumor are rife."

## Annex II

**Downtimes: some producers are tempted to take limited or even no downtime, re-starting some idle mills or switching their production to market virgin pulp production**

North American market pulp downtime - April to June, 2009				
Company	Mill Location(s)	Dates	Grade affected	Total (tonnes)
AbitibiBowater	Fort Frances, ON	April	NBSK	4.000
Alberta-Pacific	Boyle, AB	May	NBSK, NBHK	28.000
Boise <sup>1</sup>	Wallula, WA (partly integrated)	2Q	NBSK	37.000
Canfor Corp. <sup>2</sup>	Taylor, Howe Sound, BC	2Q	NBSK, BCTMP	38.000
Canfor Pulp <sup>2</sup>	Intercontinental, Prince George, BC	2Q	NBSK	20.000
Catalyst Paper <sup>3</sup>	Elk Falls, Crofton, BC	2Q	NBSK, sawdust pulp	150.000
Domtar <sup>4</sup>	Baileyville, ME, Dryden, ON	2Q	NBSK, NBHK	130.000
Daishowa-Marubeni	Peace River, AB	May	NBSK	7.000
Evergreen Pulp <sup>5</sup>	Samoa, CA	2Q	NBSK	48.000
Fraser Papers <sup>6</sup>	Thurso, QE	2Q	NBHK	43.000



International Paper7	Bastrop, LA	2Q	Fluff, SBSK	105.000
Marathon Pulp8	Marathon, ON	2Q	NBSK	48.000
Millar Western9	Whitecourt, AL	April, May	BCTMP	15.000
NewPage	Rumford, ME	2Q	NBHK	30.000
Northern Pulp10	Pictou County, NS	June	NBSK	16.000
Parsons & Whittemore11	Purdue Hill, AL	2Q	SBHK	38.000
SFK Pulp Fund	St. Felicien, QE, Fairmont, WV	2Q	NBSK, MDIP	92.000
Sappi	Cloquet, MN	April, May	NBHK	9.000
Smurfit-Stone12	Pontiac, QE	2Q	NBHK	60.000
Tembec13	Chetwynd, Skookumchuck, BC	2Q	NBSK, BCTMP	68.000
Terrace Bay Pulp14	Terrace Bay, ON	2Q	NBSK, NBHK	123.500
West Fraser15	Quesnel, BC, Slave Lake, AB	2Q	BCTMP	48.500
<b>North American total</b>				<b>1.158.000</b>
<b>Latin American market pulp downtime - April to June, 2009</b>				
Arauco	Valdivia, Constitucion, Licancel, Chile	2Q	Bleached radiata, UBK	31.000
CMPC	Laja, Chile	2Q	Bleached radiata	22.500
Cenibra	Belo Oriente, Brazil	April	BEK	18.000
<b>Latin American total</b>				<b>71.500</b>
<b>European market pulp downtime - April to June, 2009</b>				
Billerud	Sweden	2Q	NBSK	6.000
Botnia16	Kaskinen, Joutseno, Kemi, Finland	2Q	NBSK, BHK, UBK	192.000
Ence	Huelva, Spain	April	BEK	15.000
Rottneros	Miranda, Spain, Rottneros, Sweden	2Q	BEK, BCTMP	41.500
Sodra17	Follafoss, Tofte, Norway, Monstera, Sweden, Folla, Norway	2Q	NBSK, BHK, BCTMP	98.000
Stora Enso18	Norrsundet, Sweden, Uimaharju, Finland	2Q	NBSK, BHK	239.000
<b>European total</b>				<b>591.500</b>
<b>Asian market pulp downtime - April to June, 2009</b>				
Advance Agro	Prachiburi, Thailand	2Q	BHK	14.000
APRIL	Kerinci, Indonesia	2Q	BHK	240.000
Asia Pulp & Paper19	Hainan Island, China	2Q	BHK	300.000
Chung Hwa Pulp	Hualien, Taiwan	2Q	BHK	18.000
Donghae Pulp	Ulsan, South Korea	2Q	BHK	45.000
Indah Kiat, Asia Pulp & Paper	Sumatra, Indonesia	2Q	BHK	45.000
Kertas Nusantara20	East Kalimantan, Indonesia	2Q	BHK	131.000
PT Tel21	Palembang, Indonesia	2Q	BHK	36.000
<b>Asian total</b>				<b>829.000</b>
<b>Combined worldwide total</b>				<b>2.650.000</b>

Source: RISI, June 5, 2009



**Black liquor impact?** Some contacts say that mainly southern US producers of natural "flat" multiwall kraft paper may be taking less downtime because of the black liquor tax credit for kraft pulp producers.

Most US producers registered as "alternative fuel mixers," with KapStone Paper and Packaging, for example, recently reporting a \$23.9 million refund for the first quarter for its Roanoke Rapids, NC, and North Charleston, SC, mills.

Source: RISI, PPI Pulp & Paper Week, May 22 2009

**MDIP impact at SFK mills?** Citing the black liquor funding, SFK Pulp pres/CEO Pierre Cote said on Tuesday that his company's market deinked pulp (MDIP) mills in Menominee, MI, and Fairmont, WV, planned significant downtime through July. He said some of the mills' customers "might see" an opportunity to switch from MDIP to virgin grades because of the fuels funding benefiting virgin pulp lines.

In the first quarter, the Fairmont and Menominee mills were down for 11 and 14 days, respectively, and would be down for 56 and 44, respectively, this quarter, a company executive said. In July, the company expected 31 days of downtime at Fairmont and five days at Menominee, the executive said. The combined capacity of the two mills is 360,000 tonnes/yr.

In contrast, SFK's 375,000 tonnes/yr northern bleached softwood kraft mill in Saint Felicien, QC, planned no downtime in July.

Source: RISI, PPI Pulp & Paper Week, May 22 2009

## **Domtar announces reopening of Woodland pulp mill in Maine, US**

MONTREAL, June 10, 2009 (Press Release) - Domtar Corporation announced today that it will be reopening its Woodland pulp mill in Baileyville, Maine. Approximately 300 employees will be called back for the restart of pulp production, which is targeted to resume the week of June 22, 2009. The mill has an annual hardwood pulp production capacity of 398,000 air dry metric tons.



Domtar announced the closure of the Woodland pulp mill for an undetermined period on March 5, 2009, due to weak global pulp demand, historically high inventory levels and depressed prices. Domtar pulp inventory levels have since been substantially reduced. The timely benefits from the refundable tax credits for the production and use of alternative bio fuel mixtures, and other important conditions, such as stronger global demand, improving prices and favorable currency exchange rates have made the reopening possible. Domtar will closely monitor the mill's profitability, which is critical to maintaining operations.

Source: RISI, Daily News, June 11, 2009

### **Domtar uses black liquor subsidy to reopen U.S. pulp mill**

By Gordon Hamilton, Vancouver Sun June 10, 2009

Domtar Corp. said Wednesday that thanks to the U.S. tax credit on black liquor, it can now reopen a pulp mill in Baileyville, Maine. The mill had been down for almost four months. Domtar, which has mills in both Canada and the U.S., announced the closure of the mill March 5 due to weak global pulp demand. It also closed a pulp mill in Dryden, Ont., around the same time. The Dryden mill remains closed.

Domtar said in a new release that “the timely benefits from the refundable tax credits for the production and use of alternative biofuel mixtures, and other important conditions, such as stronger global demand, improving prices and favorable currency exchange rates have made the reopening possible.” Canadian forestry leaders say the black liquor tax rebate has unfairly advantaged American mills over Canadian mills and is threatening the survival of the Canadian industry.

Kevin Mason, analyst with Equity Research Associates, said the the Domtar start-up is not only putting more pressure on Canadian mills but also on the Canadian government to take some action to counter the massive U.S. subsidy before Parliament’s summer break. Mason estimates it would cost \$1.8 billion to level the playing field between Canadian and U.S. producers. “The longer this continues the more market distortion it creates,” Mason said in an interview. “This (Domtar move) is an obvious restart solely due to the black liquor issue. “At least seven mills are on the bubble of closing in Canada and unless something happens soon, we are going to see a pile of closures.”

### **Skookumchuck mill first B.C. casualty of black liquor subsidy**

By Gordon Hamilton, Vancouver Sun June 11, 2009

Tembec said Thursday it is shutting down its Skookumchuck mill, citing the U.S. black liquor subsidy as a prime cause.

The temporary closure comes while Ottawa considers, but has not acted on, a \$1-billion aid package that could assist mills like the one Skookumchuck, that have a green energy



component to them. Industry leaders say aid is needed immediately as U.S. competitors are now receiving over \$100 million a week from Washington.

The mill is the first B.C. casualty of the black liquor subsidy, which cut production costs by up to 60 per cent for American mills. They are reopening while Canadian mills close. Located north of Kimberley in eastern B.C., the Skookumchuck mill employs 285 people and is already creating enough green energy by burning wood waste in its boiler to provide B.C. Hydro with power to supply 23,000 homes.

“The black liquor tax credit available to U.S. producers was absolutely a factor in this decision,” Tembec president James Lopez said of the decision to shut the mill down.

“It has allowed chemical pulp capacity that would otherwise be uneconomic to either remain in operation or be brought back into production, resulting in a material distortion in the pulp market in terms of both the supply/demand balance and pricing,” he said in a news release.

“In the absence of an offsetting measure to allow Canadian producers to level the playing field, our industry and its employees will continue to pay the price through mill idlings and closures. This inequity must be addressed.” Ottawa bureaucrats have prepared a \$1-billion aid package for the industry to help offset the effects of the U.S. subsidy but it has not gone before cabinet, raising speculation within the forest industry over the political will to implement it. [...] Analysts estimate it will cost \$1.8 billion to offset the impact of the U.S. subsidy. Lazar said anything less than \$1 billion will not be sufficient to keep mills from closing.

The Skookumchuck mill is to close June 29 for at least two weeks.

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