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MeadWestvaco

July 13, 2007

David R. Eichenlaub
Assistant Director, Division of Economics and Finance
VA State Corporation Commission
Richmond, VA 23218-1197

Re: Comments in PUE-2007-00049

Dear Mr. Eichenlaub:

MeadWestvaco Corporation (MWV) greatly appreciates the opportunity to comment on the ability of our company to meet the energy efficiency goals included in SB 1416. MWV is a leading global producer of packaging, coated and specialty papers, consumer and office products, and specialty chemicals. MWV operates facilities located in 29 countries, and serves customers in nearly 100 countries in industries such as automotive, beverage, consumer products, healthcare, media and entertainment, and publishing. Through a broad range of complementary businesses, MWV helps the world's leading companies go to market with attractive and high-performance packaging, improve their communications using high-quality and specialty papers and enhance their products with our specialty chemicals. We serve consumer markets with the highly recognized AT-A-GLANCE®, Cambridge®, Columbian®, Five-Star® and Mead® products. We also manage strategically located forestlands according to stringent environmental standards and in conformity with the Sustainable Forestry Initiative® (SFI) program.

The MWV pulp and paperboard mill in Covington, VA., competes in a global paper and packaging market, exporting about 45% of its production to markets outside of the U.S. The mill employs about 1,250 people to manufacture high quality bleached paperboard. This paperboard is converted by MeadWestvaco facilities and many customer facilities into packaging for pharmaceutical, cosmetic, electronic, tobacco and food products, as well as greeting cards and sport cards. Collectively, the mill and the other MeadWestvaco operations employ about 1,610 people in the Alleghany Highlands of Virginia. We have invested $1.7 billion in capital at the mill from 1986 to 2005 and our capital expenditures for 2006 were $28 million. Our capital investments for environmental control over the past 20 years have been $332.4 million. Our 2006 operating cost for environmental control was over $46 million.

MWV, through its membership in the Chicago Climate Exchange, is legally committed to reduce total direct greenhouse gas emissions from its major U.S. facilities by 6% from 2003 through 2010. MWV also participates in the Business Roundtable's Climate RESOLVE initiative and the American Forest & Paper Association's Climate VISION Commitment – both of which have established organizational goals to voluntarily reduce greenhouse gas emissions. These voluntary commitments have required us to focus on energy efficiency as one of the means by which we can achieve these goals.

MWV has a unique perspective on energy policy issues because we both produce and consume significant amounts of energy. On the production side, approximately 60 % of pulp and paper mills' total energy demand today is supplied from renewable biomass, such as wood wastes and by-products of the pulping process. We also use highly efficient co-generation technology which is integrally tied to our manufacturing processes. Companywide, we co-generate electric power both for internal use and for sale to the power grid.

The remaining 40% of our energy consumption must be met through the purchase of significant amounts of energy (e.g., natural gas, electricity, coal); thus, those energy costs are a significant cost driver. Currently, energy is the third largest manufacturing cost for the industry. Any cost increases for these critical fuel sources will have a negative effect on our competitiveness since we are not insulated from global competition and cannot easily pass those costs along to our customers.

Our industry has made great strides not only in energy efficiency, but also in reducing reliance on fossil fuels and purchased energy as well as in the reduction of greenhouse gas emissions. This has been accomplished through specific programs dedicated to making better use of the renewable biomass resource that is derived from all forest products. By way of reference, about 30 years ago these percentages were reversed; we self produced about 40% of our total energy requirements and we purchased 60%. Unfortunately, energy use has also been recently reduced through mill closures and capacity reductions.

U.S. capacity to produce paper and paperboard has been declining approximately 1% a year since its peak in 2000, while worldwide capacity to produce these products outside of North America has grown at an average annual rate of 3.7%. The tendency for capacity to be built abroad while U.S. capacity is contracting would only be exacerbated if the cost of energy to U.S. mills were to increase due to energy efficiency mandates while the cost to our competitors remained unaffected. Much of this new capacity outside the U.S. is being located in developing nations such as China, Indonesia, and Brazil. There is no doubt that a rise in the cost of energy to our industry that is not matched by our overseas competitors would rapidly accelerate the rising trend in imports and domestic job losses that this industry has seen over the past 10 years.

Since early 1997, 136 pulp and paper mills have closed in the U.S., contributing to a loss of 85,000 jobs, or 39% of the industries' workforce. An additional 60,000 jobs have been lost in the wood products industry since 1997. Many of these mills were in rural areas and

served as the major source of employment for the locale. Energy prices were a significant reason for these devastating losses to the U.S. economy. Just two years ago, MWV owned nine domestic pulp and paper mills. At the present time we own four. Recently, uneconomic paper machine capacity was permanently shut down at two of those mills, one in Evadale, Texas and another in Covington, Virginia.

Over the past 30 years, the industry has steadily improved their energy performance. Overall energy use (of both fossil fuels and renewable energy) has decreased by almost 3% between 2000 and 2004. Since 1972, the industry has reduced the total amount of energy needed to produce a ton of saleable paper by 27%. Pulp and paper mills and wood products production facilities are unique in their utilization of renewable biomass fuels, which has enabled them to reduce their fossil fuel use. Between 2000 and 2004, fossil fuel use was reduced by 11 percent. Pulp and paper mill use of total energy derived from fossil fuel and purchased energy sources has decreased by 52% since 1972.

As shown by the statistics cited above, global competition is the greatest disciplinarian of behavior and investment decisions. Investment in energy efficiency is absolutely necessary for us to remain viable in the competitive market for our products. This is especially true given our pledge to reduce our carbon dioxide emissions as this is another focus our major foreign competitors do not have. Over the past five years alone, MWV has voluntarily spent $14.6 million capital dollars on energy efficiency projects at our Covington mill. These projects were selected based upon overall internal rate of return criteria and have resulted in energy use reductions of 672,096 million Btu per year. A sampling of projects includes: thermal load reduction and controls, evaporator improvements, condensate heat capture systems on boilers, boiler high efficiency soot-blower nozzles, and condensate heat recovery on paper machines. Interestingly, the most cost effective energy efficiency projects for the mill did not specifically target electric power use reductions. To the extent the projects improved the efficiency of our boiler complex in the conversion of fuel to steam, we were able to co-generate additional power. We thereby reduced our power purchases, but the overall electric power consumed by the mill did not change.

In fact, as customers demand more stringent specifications for paper products, the technology has advanced and the industry has become more electric intensive. The control necessary to achieve the quality demanded by customers is not attainable by exclusive use of gas fired drying technologies on the paper machines. As a result, modern paper machines have a mix of dryers. Gas dryers are used to dry the sheet across the web width while electric dryers are used for coating drying and for sheet profile control across the web by zones. Covington has replaced some gas dryers with electric powered infrared dryers to deliver the quality to the customer. Other technological improvements have also contributed to an increase in our electric intensity (MMBtu electric per ton saleable product) and a decrease in our steam and other fossil fuel use intensity. Because we expect this trend to continue, it is highly unlikely that our Covington mill can cost effectively reduce our electric consumption by 10% of 2006 levels by 2022, which is the goal specified in SB 1416.

Given our voluntary efforts and financial commitments toward achieving cost effective energy efficiency, we have historically not supported government imposed mandates for energy efficiency or any other program such as demand side management for our class of customer for several reasons. First, we believe we can more cost effectively reduce our energy use ourselves with our own funds rather than relying on and paying for utility sponsored programs which may not be as effective in realizing the expected returns for the dollars expended. Second, we have witnessed in other states that these programs typically are not designed to meet our specific needs as well as our internal projects. Third, a focus on energy efficiency through the use of mandates without considering whether these resources or technologies can be cost effectively obtained as compared to other options for the supply of electric power can cause enormous economic waste. And lastly, the increased costs utilities would pass along to our facility for these programs through the electric power rates would, in many cases, preclude us from being able to invest in the higher value projects which make the most sense for our mill.

We also fundamentally believe that it is not appropriate for Government to impose energy savings requirements on utilities as they are in the business of selling power and unavoidable conflicts arise when they are placed into the business of "not selling power." Government attempts to force utilities into this role leads to the development of perverse concepts such as revenue decoupling. This undermines traditional ratemaking principles by effectively paying utilities for not selling power.

With decoupling, utilities are supposedly compensated for revenue lost when customers' efficiency projects reduce demand. However, measurement and verification protocols often cannot distinguish between lower sales generated by energy efficiency and from other causes. Hence, utilities also are often compensated for reduced power sales due to factors unrelated to efficiency, such as weather that depresses sales, economic downturns, or even customer funded energy efficiency projects.

Because it is difficult to track where savings originate, utilities are often simply compensated for lost revenue in general. Therefore, industrial consumers often lose the financial reward and a primary motivator of efficiency projects—reduced energy bills. For example, if a pulp and paper mill installed more efficient boilers in response to rising fuel prices, it would purchase less power from its utility, and should see lower bills. However, because the utility is to be compensated for the lost revenue, that same mill would end up paying a higher rate on a lesser level of purchases under decoupling, thereby totally undermining the motivation for the investment in the energy efficiency project. We encourage Staff to continue their support for not including lost revenues in any energy efficiency programs which may be developed as was recommended in the Staff Report in Case No. PUE900070 related to demand side management programs which was endorsed by the June 28, 1993 SCC order. This outcome is especially relevant today since the investor owned utilities in Virginia are required by statute to file general rate cases every two years; so it really is only a timing issue on when the utilities recover their costs. In our opinion, by no means should the concept of revenue decoupling be endorsed by the energy efficiency working group for any classes of customers.

Should SCC Staff conclude that the goals established in SB 1416 are achievable, it is highly recommended that industrial customers who have a demonstrated commitment to energy efficiency in their Virginia operations be offered an option to opt out of these new requirements. Facilities opting out should not be required to contribute to the funding of the energy efficiency programs or be able to access any funds from the program. This is especially important for distressed industries such as pulp and paper which are in a difficult competitive situation.

Several other states have recently concluded that to enhance the competitiveness of their industries, the additional costs of mandated energy efficiency programs or demand side management programs should not be imposed upon industrial class customers. This year the Texas General Assembly passed HB 3693 which increases the energy efficiency mandates for commercial and residential customers only and specifically excludes industrial customers from those additional requirements. In a recent Georgia Power rate case (25060 – U) and in a pending settlement of Georgia Power's Integrated Resource Plan proceeding (24505 – U), industrial customers are exempt from and are not responsible for funding Georgia Power's new demand side management programs. The rationale used in each of these examples to provide those exemptions is just as relevant for Virginia's consideration of this issue. To the extent our competitors in other states are not subject to energy efficiency mandates and Virginia manufacturers are, we will be disadvantaged in the marketplace. Therefore, there are economic issues and an overall fairness perspective to consider and weigh into these deliberations.

Through innovative tariffs and by embracing PJM's demand response programs, Virginia electric utilities can encourage customers to reduce their energy consumption when electrical demand is high and power is more costly to produce. In particular, interruptible service, real time pricing (RTP), time-of-use rates (TOU), and multiple account management all reflect an awareness that pricing and rates do matter. Providing appropriate cost-based price signals can be a very cost-effective means by which to influence the consumption patterns of customers. In addition, such tariff options provide a cushion against extreme weather, load forecast error, and unanticipated outages.

In conclusion, the Commonwealth will incur significant costs as we challenge ourselves to become more efficient in our use of electric power. The SCC should be mindful of the international competitive pressures faced by industrial facilities, especially facilities in the forest products industry, as these costs generally cannot be passed though to forest products industry customers. Thus, additional energy efficiency compliance costs will only exacerbate the competitiveness challenges faced by the industry. The SCC staff should ensure cost effectiveness by using the most rigorous tests available as a guiding principle when it debates the design of any mandated energy efficiency or demand side management program. We also urge the SCC staff to consider which customers or customer classes of electricity consumers should be exempt from the energy efficiency requirement based on the health of that manufacturing sector and their demonstrated commitment to self- funding of projects with significant energy efficiency components.

We look forward to working with SCC staff and other working group members to assist in developing the best possible recommendations to the General Assembly regarding the energy efficiency goals for the Commonwealth.

Very truly yours,

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