

UNITED STATES OF AMERICA
BEFORE THE
DEPARTMENT OF ENERGY
OFFICE OF FOSSIL ENERGY



In the matter of:)
)
CONOCOPHILLIPS ALASKA)
NATURAL GAS CORPORATION)
and)
MARATHON OIL COMPANY)

Docket No. 07-02-LNG

REPLY OF AGRIMUM U.S. INC.
TO ANSWER OF CONOCOPHILLIPS ALASKA NATURAL GAS
CORPORATION AND MARATHON OIL COMPANY

Pursuant to section 590.302(a) of the Department of Energy's ("DOE") regulations¹ and DOE's June 5, 2007 order in the above-captioned docket,² Agrium U.S. Inc. ("Agrium") hereby submits these reply comments on the Answer submitted by ConocoPhillips Alaska Natural Gas Corporation ("ConocoPhillips") and Marathon Oil Company ("Marathon") (collectively, "Applicants") in the above-captioned docket on May 8, 2007.

I. BACKGROUND

On January 10, 2007, ConocoPhillips and Marathon filed an application requesting a blanket authorization to export 99 TBtus of liquefied natural gas ("LNG") from Alaska on a short-term or spot market basis to one or more countries on the Pacific Rim ("Application"). Agrium submitted a Motion to Intervene, Comments, and Protest ("Agrium's Motion to Intervene and Protest") in the above-captioned proceeding on April 9, 2007, in which Agrium urged OFE to deny the Application or, in the alternative,

¹ 10 C.F.R. § 590.302(a) (2006).

² Order Granting Motions to Intervene and Requests to File Reply Comments and Deferring Action on Requests for Other Additional Procedures, FE Docket No. 07-02-LNG (June 5, 2007) (hereinafter, "June 5 Order").

impose a condition on any grant of the requested authorization to preclude exports unless Applicants show that domestic demands for natural gas are being satisfied. On May 8, 2007, Applicants filed an answer (“Answer”) to Agrium’s Motion to Intervene, Comments, and Protest, as well other motions, comments and protests.

On June 5, 2007, OFE issued an order granting all of the motions to intervene that were timely filed in this proceeding, including that of Agrium. OFE also granted the requests for interveners to file reply comments to the Applicants’ Answer.

II. REPLY COMMENTS

Applicants’ Answer seeks to distract OFE from the real issue at hand – that there is a real shortage of natural gas in the Cook Inlet region that will be exacerbated by the proposed export. A number of parties, including Chevron U.S.A. Inc. and Union Oil Company of California (“Chevron”); Chugach Electric Association, Inc. (“Chugach”); Enstar Natural Gas Company (“Enstar”); the State of Alaska (“State”); and Tesoro Corporation and Tesoro Alaska Company (“Tesoro”) (collectively, “Objecting Parties”), have stated significant concerns about the proposed export and have provided OFE with evidence that there is currently a shortage of natural gas in the Southcentral Alaska market. Therefore, OFE should reject the Application, or, in the alternative, should condition the requested export authorization to preclude exports unless Southcentral Alaska demand is being satisfied.

A. Rebuttable Presumption for Granting a Requested Export Authorization is Overcome by Existing Supply Problems.

In their Answer, Applicants claim that section 3 of the Natural Gas Act (“NGA”) creates a statutory presumption in favor of approving an application to export natural gas, and that the Objecting Parties bear the burden of overcoming

that presumption.³ Applicants claim that the Objecting Parties “fail to overcome the statutory presumption that the proposed export is in the public interest.”⁴

A key element in evaluating the public interest is “consideration of the domestic need for the gas to be exported.”⁵ Agrium’s Motion to Intervene and Protest, as well as the other Objecting Parties’ submissions, raise serious questions regarding the sufficiency of the natural gas supply in the Cook Inlet region during the export period. In fact, many of the Objecting Parties have provided evidence that there is currently a shortage of natural gas. This evidence is not based on theoretical postulation – the Objecting Parties have provided real-world examples of the supply shortages.

Applicants’ argument that the supply shortages identified by the Objecting Parties are simply commercial in nature, and that OFE should not interfere in commercial negotiations and should allow the market to take care of Objecting Parties’ issues, is misdirection. Agrium and the other Objecting Parties are not asking OFE to interfere with commercial negotiations among domestic producers and consumers. Rather, Agrium is simply asking that OFE evaluate the domestic supply implications of the proposed export, as required by law.

³ Applicants’ Answer at pp. 11-13.

⁴ Applicants’ Answer at p. 14. NGA section 3 does not, in fact, create a “statutory presumption that the proposed export is in the public interest.” NGA section 3 states, “the [Secretary] shall issue such order upon application, unless, after opportunity for hearing, it finds that the proposed exportation or importation will not be consistent with the public interest.” NGA § 3, 15 U.S.C. § 717b. NGA section 3 simply provides that action on an application for export authorization shall be based on a public interest determination, and that the application shall not be granted if the export is found to be inconsistent with the public interest.

⁵ Delegation Order No. 0204-211, 49 Fed. Reg. 6690 (Feb. 22, 1984). See also Delegation Order No. 0204-127, 54 Fed. Reg. 11436 (Mar. 20, 1989).

B. The Objecting Parties' Natural Gas Supply Problems are Central to the Public Interest Evaluation.

Applicants argue that their Application demonstrates “that Cook Inlet natural gas supplies are more than adequate to satisfy both regional demand and the requested export volumes during the export term.”⁶ Applicants claim that the shortages highlighted by Agrium, Chugach, Enstar and Tesoro are just an indication that “the market is sorting out which entities are economically viable as the era of stranded natural gas comes to end in Cook Inlet.”⁷ Continuing, Applicants claim that these shortages “are reactions to economic factors, [and are] not indicators of natural gas supply shortages.”⁸ Applicants’ views suggest that selling natural gas to unspecified overseas purchasers in lieu of meeting demand of domestic consumers would be acceptable. This view, however, is inconsistent with the public interest test that focuses on “domestic need for the gas to be exported.”

The Objecting Parties, including Agrium, Chugach, Enstar, Tesoro, and Chevron, represent the manufacturing, electric utility, natural gas utility, refining, and gas producer sectors in Southcentral Alaska, all of which have a proven need for natural gas. Their comments in this proceeding demonstrate the existence of supply shortages. The needs of the Objecting Parties are at the core of any consideration of the public interest. The public interest test requires OFE specifically to consider the needs of these parties – their supply problems cannot simply be dismissed as the market sorting itself out.

⁶ Applicants’ Answer at p. 3.

⁷ Applicants’ Answer at p. 36.

⁸ Applicants’ Answer at p. 36.

C. The Public Interest Determination in the Current Factual Circumstances Necessitate the Imposition of Conditions on the Grant of Export Authority.

Applicants argue in their Answer that since “DOE/OFE has never imposed the conditions requested by the State, Enstar and Agrium on Applicants in the past . . . these conditions should not be imposed now.”⁹ Accepting the Applicants’ argument would imply that unless the original export application was conditioned, no subsequent application should ever be conditioned. The gas supply situation in Southcentral Alaska is fundamentally different from what it was when DOE last considered these issues nearly a decade ago. Thus, the mere fact that OFE did not impose conditions in the past is no reason for OFE to decline to impose them now.

OFE must impose conditions when necessary to protect the public interest. While in past proceedings, the evidence of shortage of supply was merely theoretical, Objecting Parties have provided ample evidence in this proceeding of a current shortage of supply, and the fact that if Applicants’ Application is granted without condition, the shortage of supply will only get worse. Where there are regional natural gas supply shortages, such as in the case at hand, the imposition of conditions is not only legitimate, but also is necessary to safeguard the public interests OFE is required to consider and protect when reviewing export applications.

Applicants state that their Application “demonstrate[s] that Cook Inlet natural gas supplies are more than adequate to satisfy both regional demand and the requested export volumes during the export term.”¹⁰ Applicants also state that “there are sufficient natural gas supplies to meet both regional demand and the

⁹ Applicants’ Answer at p. 38.

¹⁰ Applicants’ Answer at p. 3.

export market;”¹¹ that they “strongly dispute any arguments...that there are insufficient natural gas supplies in the Cook Inlet;”¹² that they “have presented evidence to show that there are adequate supplies of Cook Inlet natural gas to meet both regional demand and the foreign export market during the relevant timeframe;”¹³ that “regional demand will not exceed available Cook Inlet supplies;”¹⁴ that the reports filed in support of the Application demonstrate “that there are adequate supplies to meet regional demand in Southcentral Alaska, including field operations;”¹⁵ and that these reports “demonstrate that there are adequate Cook Inlet supplies of natural gas to meet regional demand in Southcentral Alaska.”¹⁶

As outlined above, Applicants state confidently that the proposed export of natural gas will not interfere with continued domestic access to sufficient supplies of natural gas. In contrast, Agrium and other Objecting Parties have presented clear evidence of actual natural gas shortages in the Cook Inlet region that refute Applicants’ assertions. OFE must reconcile these conflicting positions in ruling on Applicants’ Application. One way to do so is to adopt Agrium’s proposed condition that would preclude export if, and only if, there were domestic demands going unmet.

Despite their confident attitude regarding the sufficiency of supplies, Applicants oppose any condition on the requested export authorization. If

¹¹ Applicants’ Answer at pp. 5 and 8.

¹² Applicants’ Answer at n. 21.

¹³ Applicants’ Answer at p. 14.

¹⁴ Applicants’ Answer at p. 14. See also Applicants’ Answer at pp. 41 and 27.

¹⁵ Applicants’ Answer at p. 23.

¹⁶ Applicants’ Answer at p. 38.

Applicants believe that there really will be sufficient natural gas supplies provided to meet both regional needs and LNG exports, then the proposed condition they object to so strongly will impose no restrictions on the Applicants' export activities. On the other hand, if shortages continue or worsen, and OFE has authorized exports (without condition) that exacerbate the domestic supply problems, how will DOE justify its action as being consistent with the public interest? Simply pointing to unproduced reserves in the ground will not provide much solace to the public whose interests the NGA requires DOE to protect. Therefore, if Applicants' request to export natural gas from the Cook Inlet region is granted, OFE must impose conditions to restrict exports if domestic demand for natural gas in Southcentral Alaska is going unmet, as required by the public interest test established by Congress in the NGA.

D. The Proposed Condition on an Export Authorization is Not an Attempt to Use NGA Section 3 to "Take" Natural Gas from Applicants.

Applicants argue that Agrium's claims "are nothing more than an attempt to use the [Natural Gas Act] Section 3 public interest standard to create a right of eminent domain to take natural gas from Applicants' export operations for [its] private use."¹⁷ This statement is simply incorrect.

Agrium's Motion to Intervene and Protest is in no way an attempt to force Applicants to sell natural gas to Agrium. Agrium has not requested, or even suggested, that OFE require Applicants to sell natural gas to Agrium. If OFE conditions the export authorization as requested by Agrium, Applicants would remain free to decide whether to produce gas, whom to sell it to in the U.S., and at what price. The only restriction would

¹⁷ Applicants' Answer at p. 16.

be on exports, and that restriction would be triggered only if there was “domestic need for the gas to be exported.”

Applicants argue, in essence, that they are entitled to do whatever they want with their natural gas, and that any restriction on export would constitute undue market interference.¹⁸ This is essentially an argument that the NGA section 3 public interest test should be read out of existence. OFE should not, and cannot, take such an unprecedented step – exports are to be authorized only if they are found to be consistent with the public interest.

E. Agrium’s Natural Gas Use is a Legitimate Element of Regional Demand in Southcentral Alaska.

In their Answer, Applicants argue that since Agrium uses natural gas to manufacture fertilizer for export, its “natural gas demand is not even a legitimate regional need.”¹⁹ Applicants would like OFE to believe that the export of fertilizer products manufactured from natural gas is no different from the export of LNG. Applicants’ claims are baseless. The Natural Gas Act clearly distinguishes between LNG and other products, such as fertilizer, that are manufactured from natural gas. While the NGA requires Applicants to obtain affirmative approval from OFE before they are permitted to export LNG, there is no such requirement for the export of fertilizer because fertilizer is a domestically manufactured product. Contrary to Applicants’ assertions, Agrium’s demand for natural gas for its fertilizer plant (“Kenai Fertilizer Plant”) is a legitimate element of regional demand in Southcentral Alaska.

The Kenai Fertilizer Plant, located on the Kenai Peninsula in the Cook Inlet region, is one of Alaska’s few major manufacturing operations. It manufactures

¹⁸ Applicants’ Answer at pp. 39-42.

¹⁹ Applicants’ Answer at p. 9.

anhydrous ammonia and urea fertilizer products using natural gas as a key feedstock. Thus, the Kenai Fertilizer Plant is a significant domestic consumer of natural gas produced in the Cook Inlet region.

As a consumer of the natural gas in a constrained market from which Applicants seek permission to export natural gas, Agrium's natural gas use is a legitimate element of demand in the Cook Inlet region to be considered in DOE's analysis. DOE's precedent makes "domestic need for the gas to be exported" a preeminent consideration. DOE's rules and precedents suggest nowhere that use of natural gas for manufacturing purposes, even for manufacturing a product that eventually could be exported,²⁰ is not a legitimate regional demand. Moreover, the Application itself effectively concedes the relevance of Agrium's demand because the Applicants' analysis of regional demand takes Agrium's demands (although inaccurately portrayed) into consideration.²¹

Demand for natural gas to operate the Kenai Fertilizer Plant is a legitimate element of regional demand. Thus, Agrium's demand must be considered when evaluating Applicants' request.

F. Deliverability.

In their Answer, Applicants claim they are not required to demonstrate deliverability under OFE precedent.²² In addition, Applicants state that deliverability responsibilities lie with the utilities, not the Applicants.²³ These statements are again misdirection.

²⁰ Note that, in addition to producing fertilizer products that are exported, the Kenai Fertilizer Plant is the major supplier of fertilizer products in Alaska and provides fertilizer products to the lower 48 states.

²¹ Application at pp. 13-15.

²² Applicants' Answer at pp. 31-32.

²³ Applicants' Answer at p. 32.

While the responsibility of delivering gas to utility customers during peak periods may arguably lie with the utilities, the rates at which gas is produced from the field at any given time are within the control of the producers. It is these production rates (as opposed to the size of reserves) that are critical to the supply side of the public interest evaluation. Theoretical sufficiency of reserves to meet domestic demand is not an appropriate basis for evaluating the public interest in circumstances where there demonstrably are not sufficient supplies of natural gas being produced to meet domestic demand. If there are production shortages, then regional demand will go unmet, and, in such circumstances, the public interest standard will not be satisfied.

G. Further Procedures are Appropriate -- Suggestion for Oral Presentations on Test for Evaluating the Public Interest.

In their Answer, Applicants argue that no further procedures are necessary. Agrium, however, believes that the Applicants' pleadings, and the pleadings of the Objecting Parties, have raised important questions regarding the appropriate test OFE should utilize in judging the public interest in these proceedings. The public interest test in the case at hand revolves around an evaluation of the "domestic need for the gas to be exported," and in particular, whether there are sufficient supplies to satisfy both domestic demand and LNG export demand. The Applicants and the Objecting Parties have conflicting views as to appropriate definition of "sufficient supplies" in this circumstance. Therefore, in order to assist OFE in its decision-making process, Agrium respectfully requests that OFE permit interested parties to make oral presentations regarding the appropriate test to be used.

Pursuant to section 3 of the NGA, authorization of the export of natural gas turns on whether the export is “consistent with the public interest.”²⁴ The legislative history of NGA section 3 indicates that one of Congress’ primary concerns with permitting the export of natural gas was to ensure against impairment of “the sufficiency of the supply of natural gas within the United States.”²⁵ DOE has indicated that a paramount consideration in evaluating the public interest under section 3 is whether the proposed export will leave domestic needs for gas unmet – in particular, whether there is “domestic need for the gas to be exported.”²⁶

Applicants argue that their Application demonstrates “sufficient reserves of natural gas to serve both the LNG exports and the local market,”²⁷ and therefore, their Application should be granted. Applicants further argue that DOE should not consider whether reserves are being or will be produced.²⁸ The Objecting Parties, on the other hand, have provided evidence that current supplies have not sufficiently met regional demands. Thus, a key issue in the public interest evaluation is whether OFE, in considering the sufficiency of gas supplies to meet regional demands, should compare domestic demand to gas reserves or to gas production.

Agrium adamantly disagrees with the Applicants that no additional procedures are required. Based on the development of the record in this case to date, Agrium believes a discussion between OFE and the parties on the test to be applied would best advance the prospects for fair resolution of this matter. In particular, Agrium respectfully requests that OFE permit interested parties to make oral presentations (as provided for in section

²⁴ NGA § 3, 15 U.S.C. § 717b.

²⁵ See H.R. 11662, 74th Congress § 3 (1936).

²⁶ Delegation Order No. 0204-211, 49 Fed. Reg. 6690 (Feb. 22, 1984).

²⁷ Applicants’ Answer at p. 8.

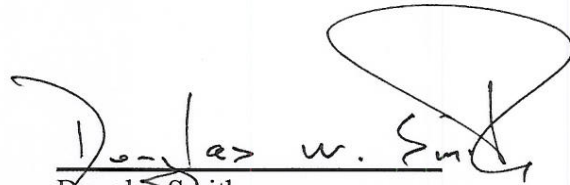
²⁸ Applicants’ Answer at pp. 39-40.

590.312(a) of DOE's regulations) with respect to whether, in considering the sufficiency of gas supplies to meet regional demands, DOE should compare domestic demand to gas reserves or to gas production.

III. CONCLUSION

The issue at hand – regardless of the Applicants' assertions – is that there is an existing shortage of natural gas in the Cook Inlet region that will be exacerbated by the proposed export. Thus, OFE should deny Applicants' requested export authorization or, in the alternative, condition any grant of the requested authorization such that exports are permitted only if domestic demands for the natural gas are being met.

Respectfully submitted,

A handwritten signature in black ink that reads "Douglas W. Smith". The signature is written in a cursive style with a large, looping flourish at the end.

Chris Sonnichsen
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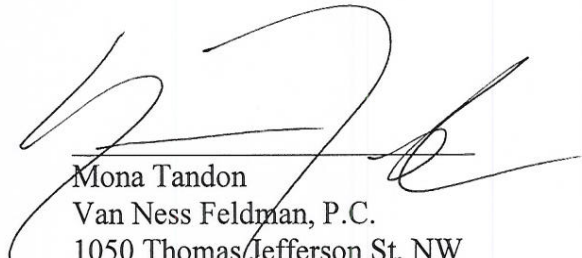
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Dated: June 26, 2007.

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing Reply of Agrium U.S. Inc. to Answer of ConocoPhillips Alaska Natural Gas Corporation and Marathon Oil Company by first-class mail or by email to all parties on the service list for this proceeding.

Dated at Washington, D.C., on this 26th day of June, 2007.



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VERIFICATION

BEFORE ME, the undersigned authority, on this day personally appeared Mona Tandon, who, having been by me first duly sworn, on oath says that she is an attorney for the law offices of Van Ness Feldman, P.C., counsel for Agrium U.S. Inc. in the above referenced matter. She hereby certifies that she has read the forgoing document, knows the contents thereof, and believes that the same are true and correct to the best of her knowledge, information and belief.


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Subscribed and sworn to before me, a notary public, this 26th day of June, 2007.


Notary Public

My Commission expires:

November 14, 2007