

**UNITED STATES OF AMERICA
DEPARTMENT OF ENERGY
OFFICE OF FOSSIL ENERGY**

_____)
CONOCOPHILLIPS ALASKA)
NATURAL GAS CORPORATION)
AND)
MARATHON OIL COMPANY)
_____)

FE DOCKET NO. 07-02-LNG

ORDER DENYING REHEARING

DOE Opinion and Order No. 2500-A

JULY 30, 2008

INTRODUCTION

In DOE Opinion and Order No. 2500, issued June 3, 2008 (Order 2500), the Office of Fossil Energy (FE) of the Department of Energy (DOE) granted the application of ConocoPhillips Alaska Natural Gas Corporation and Marathon Oil Company (jointly, Applicants) for authority to export on their own behalf or as agents for others up to 99 trillion British thermal units (TBTus) of liquefied natural gas (LNG)¹ on a short-term or spot market basis from facilities near Kenai, Alaska to Japan and/or one or more countries on either side of the Pacific Rim. The authority is for a two-year period commencing April 1, 2009 and terminating March 31, 2011. Order No. 2500 also granted the Applicants' request to vacate an existing blanket authorization to export up to 10 TBTus of LNG, as of April 1, 2009, the effective date of the new authorization.

On July 2, 2008, Chugach Electric Association, Inc. (Chugach) filed an Application for Rehearing of Order 2500. Chugach is an intervener in this proceeding and its Application for Rehearing was submitted on a timely basis in conformity with applicable regulations (10 C.F.R. 590.103 and 590.501). No other intervener submitted a request for rehearing.

For the reasons discussed *infra*, DOE is denying Chugach's request for rehearing.

ORDER 2500

Consistent with applicable statutory and policy standards and relevant precedent, the primary focus of FE's review of the application in Order 2500 was the domestic need for the natural gas proposed to be exported and the availability of adequate supplies to

¹Equivalent to 98.1 Bcf of natural gas.

meet that need. Independently prepared studies, submitted by the Applicants, projected future Cook Inlet natural gas supplies and domestic demand for natural gas in the Cook Inlet region. The studies showed that there would be adequate local supplies of gas to support the proposed export while still meeting estimated future regional demand during the two-year term of the proposed export authorization and beyond. Order 2500 at 47.

A number of interveners, including Chugach, contested an unconditional grant of the application. Chugach contended that the authorization sought by the Applicants should be conditioned on the Applicants first having “made commitments to Chugach sufficient to assure that Chugach’s gas supply and deliverability needs will continue to be met for a reasonable time.” Chugach Electric Association, Inc.’s Motion to Intervene at 4. While Chugach expressed serious concerns about regional supply and deliverability conditions, and maintained that an unconditional grant of the application would have a deleterious effect on its ability to meet the regional need for natural gas, it submitted neither a supply or demand analysis to support its position.

In reviewing the record, Order 2500 noted that there was “undisputed evidence that curtailments have occurred within the Cook Inlet region on peak winter days and that the Applicants have sometimes diverted supplies from their LNG Facility in order to assure service to meet human needs.” Order 2500 at 52. While Chugach, among other interveners, alleged that the curtailments and deliverability limitations related to “a high degree of concentration of economic power in the hands of a few producers of natural gas in the Cook Inlet region...” (*Id.*), the Order stated that “we do not find that the non-settling interveners leveling those charges have attempted to substantiate them in a meaningful way, *e.g.* through the introduction of market concentration studies.” *Id.* The

Order also observed that the same concerns over deliverability limitations resulting in shortages during peak winter periods had been raised in an earlier FE authorization proceeding in 1999 but apparently no corrective action had been taken. This suggested that the situation was not so severe as to require corrective steps and that the market was working without additional facilities.

Order 2500 concluded from the record that “market forces should be allowed to continue to work and there is no basis within the scope of our authority under section 3 of the Natural Gas Act to impose a condition that effectively guarantees that local needs must be met through firm contractual commitments before exports can commence.” Order 2500 at 53. Additionally, Order 2500 found that the type of condition on the requested authorization sought by Chugach “would be onerous and unduly discriminatory because it would single out the Applicants and put them at a competitive disadvantage *vis-à-vis* other producers that do not have to comply with such a condition and are free to sell their gas in either domestic or export markets.” *Id.* Therefore, the Order rejected the condition sought by Chugach.

Consistent with section 3 of the Natural Gas Act, Order 2500 also reviewed a number of additional public interest considerations related to the application. These included the impact on the local economy and other local interests from a grant or denial of the application, international effects, and potential environmental impacts. On balance, the Order found that these factors weighed in favor of granting the application.

CHUGACH'S APPLICATION FOR REHEARING

In seeking rehearing of Order 2500, Chugach makes three principal arguments. The arguments are summarized *infra* along with our response and related findings.

1. Impact of the requested condition on the Applicants. Chugach charges that the Order erred in finding that conditioning the new LNG export authorization on the prior satisfaction of local domestic needs would be onerous and unduly discriminatory to the Applicants because it would single them out and put them at a competitive disadvantage *vis-à-vis* other producers that do not have to sell their gas subject to such a condition. Chugach maintains that there are only three major gas producers in the Cook Inlet region and the two largest are the Applicants which supply some 65% of Chugach's gas and control an even larger percentage of uncommitted Cook Inlet reserves. Chugach argues that "it is not unfair" to single out the Applicants since they voluntarily sought export authorization and that "[i]t is simply logical, not onerous or discriminatory because the Applicants are the Cook Inlet producers best positioned to assure that local domestic needs are met." Chugach adds that if, as the Order found, there is sufficient supply to support both the requested export authorization and local domestic needs, the Applicants should be able to enter into a new contract to meet Chugach's needs. Also, Chugach contends that the condition which it asks DOE to impose on the Applicants' export authorization is a "logical extension..., not a great leap" beyond a Chugach-related volume limitation contained in a settlement in this proceeding between the Applicants and the State of Alaska.

DOE Response: Essentially, Chugach seems to be contending that the extent of the Applicants' market power means that DOE erred in finding a potential for undue discrimination in the event the condition were imposed on the Applicants. We disagree. While it may be true that the Applicants are two of three principal gas producers in the Cook Inlet region and there are no other currently available sources of natural gas in the region, as Chugach alleges, we must also presume in the absence of contrary evidence that the two Applicants do compete with each other and with the third major gas producer in the Cook Inlet region, Chevron USA Inc. and its affiliate, Union Oil Company of California. Also, perhaps more importantly, the Applicants compete in the export market against an undetermined number of gas producers and shippers. If the Applicants were compelled to sign contracts to meet all local demand before engaging in exports, they would be disadvantaged *vis-à-vis* Chevron (locally) and numerous other producers and shippers (internationally). This validates our finding of potential discriminatory impact.

The result of this proceeding might have been different if there had been a demonstration that the extent of market concentration in the hands of the Applicants was causing significant competitive harm to the public interest that could be remedied by imposing the requested condition. But no such demonstration has been made. We hasten to add that to the extent Chugach believes that local market conditions are anticompetitive, other authorities, including the Regulatory Commission of Alaska and the various state and Federal agencies and courts having jurisdiction to enforce antitrust laws, are the most appropriate authorities to hear and to remedy claims of this nature.

Moreover, it is important to note that the decision to grant the application without the proposed condition did not even principally rest on the finding of potential discriminatory impact. Our dispositive findings in this proceeding chiefly related to the evidence of natural gas supply in the Cook Inlet region and the evidence of domestic demand for that gas. Additionally, we considered several other public interest considerations that also weighed in favor of granting the application. Having found that there is adequate supply to meet domestic demand while still permitting the Applicants to engage in their requested export activities, critical findings which Chugach apparently does not challenge on rehearing, and having found that there are other public interest considerations also supporting a grant of the application, which, except as discussed in this order, Chugach likewise has not challenged, we acted accordingly in granting the application without imposing the condition sought by Chugach.

In this connection, we also reject the argument that Chugach's proposed condition should be imposed because it is "not a great leap" beyond the volume limitations that the Applicants agreed to support in order to settle with the State of Alaska. The argument does not support the relief requested. Accordingly, we reject the argument.

2. Market Concentration. Chugach argues that DOE erred in finding that the high degree of concentration of economic power in the hands of a few natural gas producers was not substantiated by "meaningful" record evidence such as market concentration studies.

DOE Response: Chugach's argument is based on the following factual assertion contained in the Order:

While allegations have been made regarding a high degree of concentration of

economic power in the hands of a few producers of natural gas in the Cook Inlet region, we do not find that the non-settling interveners leveling those charges have attempted to substantiate them in a meaningful way, e.g. through the introduction of market concentration studies.

Order at 52.

The quoted statement is a correct factual observation and was not a dispositive basis for the decision to grant the application. Accordingly, it is incorrect for Chugach to suggest by its argument on rehearing that such a factual statement was in error or that it is a basis for granting rehearing. In fact, while Chugach itself expressed a concern in its prior pleadings in this case over a lack of competition in the Cook Inlet natural gas market (Chugach reply at 4-5), it did not introduce a market concentration study. This fact tends to confirm the statement in the Order to which Chugach has objected. As indicated previously, our principal focus in this proceeding has been and continues to be the evidence of natural gas supply in the Cook Inlet region and the evidence of domestic demand for that gas. For these reasons, we reject Chugach's argument.

3. Peak Shaving. Chugach maintains that the Order erred in finding that there was undisputed evidence that the Applicants have sometimes diverted supplies from their LNG Facility to assure service to meet human needs; that the LNG Facility enhances deliverability during the coldest periods of the winter; and that no party provided evidence that this service had not been provided.

DOE Response: In its Intervention at page 11, Chugach refers to "one occasion in January [2007] when deliveries to the [Applicants'] LNG facility were curtailed in order to meet the domestic needs of customers." Chugach's argument on rehearing thus contradicts its own prior factual representation. Nor have we identified other pleadings in this proceeding which challenge the essential accuracy of the fact that supplies have

sometimes been diverted from the Applicants' LNG Facility to meet human needs.

Accordingly, we reject Chugach's argument.

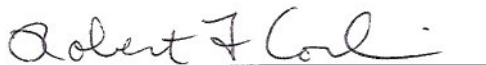
Additionally, insofar as Chugach contends that there was no real enhancement of deliverability because the diverted gas would have been available if the volumes hadn't been otherwise destined for delivery to the LNG Facility, we do not agree. It is just as likely that the same volumes might have been contracted for delivery to other customers and, therefore, not available for diversion. It was principally the fact that the volumes were due to be delivered to the Applicants' LNG Facility that gave the Applicants the ability to divert the volumes.

4. Other Arguments. All other arguments raised by Chugach in its Application for Rehearing not expressly addressed above are hereby rejected.

ORDER

Pursuant to section 3 of the Natural Gas Act and for the reasons set forth above, Chugach's Application for Rehearing of Order 2500 is hereby denied.

Issued in Washington, D.C. on July 30, 2008.



Robert F. Corbin
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Office of Oil and Gas Global Security and Supply
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