



Alerts & Publications

Department of Energy Approves Second Application for LNG Exports to Non-Free Trade Agreement Countries

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The U.S. Department of Energy (DOE) signaled its continuing support—at least for now—of exports of liquefied natural gas (LNG) from the United States by conditionally granting a request by Freeport LNG Expansion, L.P. and FLNG Liquefaction, LLC (collectively, Freeport) for a license to export LNG to countries that are not parties to a free trade agreement (FTA) with the United States requiring national treatment for trade in natural gas.

By issuing this conditional authorization on May 17, 2013,[1] DOE ended a two-year hiatus since it issued its first conditional authorization for LNG exports to non-FTA nations.[2] DOE used the intervening period to consider the cumulative economic impact of LNG exports, including commissioning two economic studies and collecting and considering public comments on these studies.[3] This authorization was issued just several days before the installation of a new Secretary of Energy, Dr. Ernest Moniz, on May 21, 2013. While it is unclear whether Secretary Moniz—a professed advocate of President Obama’s “all of the above” energy strategy—will change DOE’s policy regarding LNG exports, the changing of the guard at DOE may lead to some delay in processing additional applications.

Freeport still needs to obtain authorization from the Federal Energy Regulatory Commission (FERC) before it can construct the additional facilities needed at its existing LNG import terminal on Quintana Island, Texas, to liquefy natural gas and deliver it to marine vessels for export. Once FERC completes its environmental analysis and issues an order to Freeport, DOE will issue a final order (as compared to the conditional order it issued on May 17) addressing the environmental aspects of Freeport’s request for export authorization. It is likely that DOE’s order in *Freeport* and the subsequent FERC and DOE orders regarding Freeport’s LNG export application will be subject to requests for rehearing and potentially for judicial review. Meanwhile, as processing of the Freeport export proceeding progresses, other applicants seeking authorization for LNG exports to non-FTA nations will await anxiously to see how DOE and FERC address the issue of the cumulative impacts of LNG exports on natural gas supplies and prices and on the environment.

[LNG Export Approvals under the Natural Gas Act](#)

As discussed in more detail in our prior Client Alert sent on January 7, 2013, Section 3 of the Natural Gas Act (NGA)[4] requires companies seeking to export LNG from the United States to obtain approvals from both DOE and FERC.[5] These agencies are required to approve export applications unless the exports are found to be inconsistent with the public interest.[6]

DOE’s public-interest review of proposed natural-gas exports focuses on the economic and energy security aspects of the exports, while FERC’s review focuses on

environmental impacts.[7] In the case of exports to countries with which the United States has FTAs, the NGA deems the exports to be in the public interest and mandates that applications for export be granted by DOE without delay.[8] Applications for exports to non-FTA countries require a more substantive review by DOE.

Freeport LNG Export Proposal and DOE Approval Process

Freeport previously received authorization from DOE in February 2011 to export, over a 25-year term, up to 1.4 billion cubic feet (Bcf) per day of LNG from its existing LNG terminal to nations with which the United States has FTAs.[9] DOE's recent order in *Freeport* has the effect of allowing Freeport to use some or all of that same 1.4 Bcf of authorized exports, over a 20-year term, to supply LNG to nations with which the United States does not have an FTA. Specifically, the *Freeport* order will allow Freeport to export LNG to Japan, which does not have an FTA with the United States—Freeport has announced publicly that it has entered into tolling agreements with two Japanese natural gas and electric utility companies, Osaka Gas Co. Ltd. and Chubu Electric Power Co., Inc., to liquefy natural gas at Freeport's facility in Texas.[10] In addition, Freeport has announced an agreement with BP Energy Co.[11] As a condition of DOE's export authorizations, Freeport is required to file copies of its contracts with DOE within 30 days of execution.

Only one of the parties that intervened in the Freeport LNG export proceeding at DOE, the American Public Gas Association (APGA), protested the application. Many individuals, companies, and other entities filed comments in response to DOE's two general economic studies; DOE entered the studies and the comments into the administrative record of all pending applications for export to non-FTA nations, but DOE's consideration of these comments did not expand the list of parties to those applications beyond the parties who had filed formal interventions in those proceedings. As a result of its status as an intervenor, APGA should have standing to request rehearing, and potentially to seek judicial review, of the *Freeport* order, but it is not clear that any of the people, companies, and other organizations who filed comments in response to the two DOE-commissioned economic studies have any such standing.[12]

In its *Freeport* order, DOE responded to some of the major arguments raised by opponents of approval of LNG exports to non-FTA nations as follows:

- DOE recognized that some sectors of the economy would benefit from LNG exports more than others, and that some sectors of the economy could suffer negative impacts, but DOE determined that its public interest review should focus on the “economy as a whole, without privileging the commercial interests of any industry over another” and that decisions regarding allocation of natural gas among various industries were best left to the market to resolve.[13]
- DOE rejected for similar reasons arguments that the distributional consequences, as between natural-gas companies and their owners relative to consumers, outweighed any benefits of exports.[14]
- DOE “seriously” considered the economic impacts of higher, and potentially more volatile, domestic natural-gas prices, but took into account mitigating factors such as ample current supplies of natural gas and evidence that exports would encourage additional natural-gas production.[15] DOE found that the estimates of natural gas supply provided by its economic studies were reasonable and that, in light of these supplies, the authorization would not be expected to adversely affect the availability or price of natural gas to domestic consumers so as to negate the economic benefits of the authorization.[16]
- DOE rejected as “unlikely” the suggestion that its authorization would lead to a large number of parties entering into long-term contracts under which LNG would be exported even when it would be more profitable to sell the natural-gas in the United States.[17]
- DOE agreed with comments that financing for construction of LNG facilities and purchases of natural gas for export may come from foreign direct investment but did not find that foreign sources of capital would reduce the economic benefits or be inconsistent with the public interest.
- DOE recognized that the response of dominant LNG producers, such as Qatar, to exports of LNG from the United States may affect the level and price of U.S. exports but relied on the results of its second economic study to conclude that, even if key LNG exporting regions do not increase their exports above current levels (leading to relatively higher price impacts in the United States), the United States still would reap economic benefits.[18] DOE further relied on the economic studies to conclude that

LNG exports would not cause U.S. domestic natural gas prices to increase to the level of international prices (*i.e.*, to oil-indexed prices).[19]

- DOE also considered the international consequences of its action, finding that its authorization is consistent with U.S. commitment to free trade and to improving energy security for many U.S. allies and trading partners.[20]

In approving the Freeport application, DOE demonstrated a general predilection in favor of exports and reaffirmed its adherence to the principle, as set forth in its guidelines established in 1984, that “the market is the most efficient means of allocating natural gas supplies.”[21] However, DOE stated that it will continue to monitor market developments and that it will adopt “a measured approach” in reviewing other applications for LNG exports, including consideration of “the cumulative impacts of each succeeding request for export authorization.”[22] For example, DOE reserved the option to consider limits on the total volume and timing of LNG exports it may eventually authorize as it considers other applications.[23] DOE previously stated that it first will process the applications for LNG exports to non-FTA countries for which applicants have commenced the pre-filing process at FERC as of December 5, 2012, in the general order in which DOE received the applications, and then it will process other applications in the order of receipt. Shortly after being sworn in as the new leader of DOE, Secretary Moniz stated that he made a commitment to the Chairman of the Senate Energy Committee, Ron Wyden of Oregon, that he will review the studies regarding the impact of exports on domestic natural gas supplies and prices before acting on additional export applications.[24]

Freeport LNG’s FERC Application

Freeport and several subsidiaries filed an application with FERC on August 31, 2012 seeking authorization under Section 3 of the NGA to site, construct, own, and operate its proposed LNG export terminal. A number of individuals and organizations, including the Sierra Club, filed motions to intervene and protests in response to Freeport’s application. FERC’s environmental review in connection with that application is ongoing.

Conclusion

Consistent with the conclusions of the economic reports that DOE had commissioned and reviewed over the past two years, DOE found in the particular case of the Freeport application that exports of LNG in the amounts proposed by Freeport were consistent with the public interest. This is not the end of the story for Freeport, however, since it still needs to obtain environmental clearance from both FERC and DOE, and it may face further challenges on rehearing or in the Court of Appeals. Moreover, even though Freeport has lined up contracts for much of its capacity, it will need to secure financing for its project to the extent it has not already done so. According to press reports, Freeport plans to start construction of its project in the third quarter of 2013 and to begin operations by 2017.[25] The amount of investment required is reported to exceed \$10 billion; ConocoPhillips and an individual are the equity owners of Freeport, and the two Japanese utility offtakers reportedly have invested in a portion of the project.[26] Much can happen over the next four years that could affect the prospects for this project.

In addition, DOE and FERC’s actions on additional applications pending their review will depend in part on how their orders issued in response to the Freeport (and the earlier Sabine Pass) LNG export applications hold up when reviewed on rehearing and in response to petitions for judicial review. The agencies will need to address arguments that they should consider the cumulative impacts that additional LNG exports may have on the environment as a result of additional U.S. domestic production activities associated with such exports, including the impact of hydraulic fracturing techniques. It remains to be seen whether the ultimate limit on LNG exports from the United States will be set primarily by the market or whether there is a role for government—whether for economic or environmental reasons, or both—in setting this limit.

[1] *Freeport LNG Expansion, L.P.*, DOE/FE Order No. 3282 (May 17, 2013) (“*Freeport*”), available at <http://energy.gov/sites/prod/files/2013/05/f0/ord3282.pdf>.

[2] See *Sabine Gas Liquefaction, LLC*, DOE/FE Order No. 2961 (May 20, 2011), available at

http://www.fossil.energy.gov/programs/gasregulation/authorizations/Orders_Issued_2011/ord2961.p

[3] Please see our previous Client Alert for a discussion of the economic studies commissioned by DOE. *Department of Energy Study Boosts Prospects for U.S. LNG Exports, but Challenges Remain* (Jan. 7, 2013), available at

<http://www.omm.com/department-of-energy-study-boosts-prospects-for-us-lng-exports-but-challenges-remain-01-07-2013/>.

[4]15 U.S.C. § 717b.

[5]Section 301(b) of the Department of Energy Organization Act, 42 U.S.C. § 7151(b), delegated the NGA Section 3 authority to the Secretary of Energy. See also Section 402(f), 42 U.S.C. § 7172(f). The Secretary of Energy subsequently delegated to FERC the authority to approve or disapprove the construction and operation and siting of particular facilities for natural gas exports. See DOE Delegation Order No. 00-044.00A (May 16, 2006), available at <http://www.ferc.gov/industries/electric/indus-act/siting/doe-delegation.pdf>. The Under Secretary of Energy delegated to the Assistant Secretary for Fossil Energy the Secretary's approval authority with respect to natural gas exports other than those delegated to FERC. See DOE Delegation Order No. 00-002.00M § 1.16 (Aug. 27, 2012); DOE Redelegation Order No. 00-002.04E (Apr. 29, 2011).

[6]15 U.S.C. § 717b(a).

[7]DOE also considers the environmental aspects of an export application in compliance with the National Environmental Policy Act (NEPA) by serving as a cooperating agency in the environmental review conducted by FERC with respect to the construction, operation and siting of facilities and by conditioning its approval of export applications upon satisfactory completion of FERC's review and on an issuance by DOE of a finding of no significant impact or a record of decision pursuant to NEPA.

[8]15 U.S.C. § 717b(b)(2). The United States has such FTAs with Australia, Bahrain, Canada, Chile, Colombia, Dominican Republic, El Salvador, Guatemala, Honduras, Jordan, Mexico, Morocco, Nicaragua, Oman, Panama, Peru, Republic of Korea, and Singapore. The United States has free trade agreements with Costa Rica and Israel that do not require national treatment for trade in natural gas. Trunkline LNG Export, LLC, DOE/FE Order No. 3252 at n.3 (Mar. 7, 2013), available at

http://www.fossil.energy.gov/programs/gasregulation/authorizations/Orders_Issued_2013/ord3252.p

[9]Freeport LNG Expansion, L.P., DOE/FE Order No. 2913 (Feb. 10, 2011), available at

http://www.fossil.energy.gov/programs/gasregulation/authorizations/Orders_Issued_2011/ord2913.p

Freeport received DOE authorization for export of an additional 1.4 Bcf/day of LNG to FTA nations in February 2012. Freeport LNG Expansion, L.P., DOE/FE Order No. 3066 (Feb. 10, 2012), available at

http://www.fossil.energy.gov/programs/gasregulation/authorizations/Orders_Issued_2012/ord3066.p

Freeport has an additional application pending before DOE for export of those same additional quantities of LNG to non-FTA nations.

[10]Kelly Rizzetta, 2 Japanese Cos. Sign on to Freeport Liquefaction Project, LAW360 (July 31, 2012), <http://www.law360.com/articles/365286>.

[11]Natalie Rodriguez, BP, Freeport Strike 2-Year LNG Export Deal, LAW360 (Feb. 12, 2013), http://www.law360.com/articles/414743/bp-freeport-strike-20-year-lng-export-deal?article_related_content=1.

[12]See 10 C.F.R. § 590.501 (providing a right for "parties" aggrieved by a DOE action to request rehearing; "parties" includes the applicant and other persons who have intervened in a proceeding).

[13]Freeport at 72-73.

[14]Id. at 75.

[15]Id. at 111-112.

[16]Id. at 82-83.

[17]Id. at 91.

[18]Id. at 93-94.

[19]Id. at 101.

[20]Id. at 111.

[21]Id. at 112.

[22]Id. at 112-13.

[23]Id. at 113-14.

[24]Associated Press, Moniz, sworn in as energy secretary, delays action on LNG exports while he studies data, WASH. POST (May 21, 2013), http://www.washingtonpost.com/business/mit-physicist-moniz-takes-over-as-energy-secretary/2013/05/21/05f18a00-c22d-11e2-9642-a56177f1cdf7_story.html.

[25]Rodriguez, supra note 11.

[26]See Ownership, FREEPORT, <http://www.freeportlng.com/ownership.asp> (last visited May 21, 2013); Keith Johnson & Ben Lefebvre, U.S. Approves Natural-Gas Export Plan, WALL ST. J. (May 18, 2013), <http://online.wsj.com/article/SB10001424127887324767004578489130300876450>

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