Cited as "1 ERA Para. 70,116"

Phillips Petroleum Company; Marathon Oil Company (ERA Docket No. 82-04-LNG), December 14, 1982

DOE/ERA Opinion and Order No. 49

Order Amending Authorization of Phillips Petroleum Company and Marathon Oil Company to Export LNG from Alaska

I. Background

On May 10, 1982, Phillips Petroleum Company (Phillips) and Marathon Oil Company (Marathon) 1/ filed a joint application with the Department of Energy's (D0E) Economic Regulatory Administration (ERA), pursuant to section 3 of the Natural Gas Act (NGA), to amend an existing export authorization granted by the Federal Power Commission (FPC) on April 19, 1967, to Phillips and Marathon in FPC Docket Nos. CI67-1226 and CI67-1227, 37 FPC 777 (1967), to export LNG to Japan for sale to Tokyo Electric Power Company, Inc., and Tokyo Gas Company Limited. The initial authorization by the FPC covered a fifteen-year period ending May 31, 1984. By their joint application, Phillips and Marathon request the ERA to extend the term of the current authorization for a term of five years, through May 31, 1989, and to allow authorized quantities of LNG which have not been delivered or will not be delivered in a particular year to be delivered during a subsequent year in the extended five-year term or during a maximum seven-month make-up period beginning June 1, 1989. Phillips and Marathon seek to continue the annual volumes of LNG previously authorized to be exported, 50.57 trillion Btu.

The initial sales agreement dated March 6, 1967 (Basic Agreement), expires on May 31, 1984, and contains an option to renew the arrangement by mutual agreement between June 1, 1981, and June 1, 1982. Pursuant to this option, the parties have entered into an Amendatory Extension Agreement dated April 15, 1982 (Amendment) which would continue the export for five additional years through May 31, 1989.

Under the Basic Agreement, the parties were to ship additional LNG in excess of contracted annual volumes as soon as reasonably possible during the remaining term of the agreement when necessary to make up for under-deliveries caused by circumstances beyond the reasonable control of the parties. No other make-up provisions appear. The Amendment modifies the Basic Agreement to provide that any annual volumes of LNG not delivered under either the basic agreement or the Amendment in a given year may be delivered as soon as

possible thereafter in subsequent contract years or during a maximum seven-month period beginning June 1, 1989.

The current price of these LNG exports under the Basic Agreement, as amended March 24, 1982, delivered to the flange connecting the unloading piping of the LNG tankers with the piping of Tokyo gas, is determined by a base price of 592.8 U.S. cents per MMBtu indexed in accordance with a formula based upon changes in the weighted average of the official Japanese Government Selling Prices of the top twenty crude oils imported by Japan. Application of the formula resulted in a price delivered in Tokyo of approximately $5.76 per MMBtu in April, 1982.

Phillips and Marathon own, or control either directly or indirectly (through subsidiaries), the gas reserves and liquefaction plant in Alaska and the LNG tankers associated with this project. In each instance, Phillips' share of ownership and control is 70% and Marathon's 30%. No alterations or additions to existing facilities are anticipated during the period of the extension. Therefore, the pipeline transportation, liquefaction, storage facilities, and export point will be the same as previously authorized.

In their application, Phillips and Marathon assert that, for the past twelve years, this project has continually improved both the economy of the State of Alaska and the United States' balance of payments with respect to Japan. They state that the LNG exported from Alaska by them has been an important and reliable source of energy for their Japanese customers,2/ and that its continued exportation will be extremely beneficial to United States-Japanese relations. The applicants further assert that the continuation of this export will affect favorably the United States' balance of payments by providing annual revenues of almost $300 million or more for an additional five years and represents one of the largest exports of any product from Alaska.

Phillips and Marathon indicate that there will be no national or regional need for this gas over the term of the proposed extension. They state that it is not physically possible to deliver any of this LNG to the Pacific Coast of the lower 48 states because of the lack of any LNG receiving facility there and that it is uneconomic to deliver the LNG to existing United States East Coast or Gulf Coast LNG receiving facilities under present circumstances. With respect to regional need, that is, the possible need for the gas in Alaska, the applicants assert that all of Alaska's natural gas uses are presently being supplied and those for the foreseeable future can easily be satisfied by the available reserves in the Cook Inlet Basin area of Alaska, not including the reserves from which this exported LNG is produced.

On September 15, 1982, the ERA requested additional information from Phillips and Marathon specifically regarding the applicable price for the LNG at the point of exportation. Phillips and Marathon responded on October 14, 1982. Phillips and Marathon stated in response that no true export price for this LNG exists, since the LNG is sold on the basis of a delivered price in Japan. The applicants did make an approximate estimate of the value of the gas at the point of exportation of $3.90/MMBtu. The ERA request, and the response, are part of the record in this case.

II. Intervenors and Comments

On June 3, 1982, the ERA issued a notice of the Phillips and Marathon application to amend their existing authorization to export LNG from Alaska to Japan.3/ The notice invited protests or petitions to intervene in the proceeding from interested persons. The ERA received two petitions to intervene.4/ There is no opposition to any petition. Intervention is granted to all petitioners.

The ERA has not received any request for a hearing, nor does any intervenor oppose the application. Pac Alaska and affiliated companies urged that ". . . ERA grant the application of Phillips and Marathon, without a formal hearing, at the earliest possible date." Pac Alaska, as potential purchasers, processors, transporters, and/or sellers of Alaskan LNG at some future date, having received certificates of public convenience and necessity for the above purposes from the FPC in Docket No. CP75-140 et al., and affiliated companies support the continued exportation of Alaskan LNG for the limited period requested by the applicants. Pac Alaska does not anticipate completion of a California LNG receiving terminal before 1989 and thus cannot provide a domestic market for the Alaskan LNG until then, whereas there is a ready foreign buyer for the gas during the period of extension proposed for this import. Northwest neither supported nor opposed the application. Because of its own past efforts to obtain Alaskan LNG for its service area in Oregon and Washington, and its potential as a source of supply for its future system needs, Northwest asserts that it has a continuing interest in its use.

III. Decision

Sections 301 and 402(f) of the DOE Organization Act 5/ gave the Secretary of Energy (the Secretary) jurisdiction over imports and exports of natural gas pursuant to section 3 of the NGA. This responsibility was delegated to the Administrator of the ERA on October 1, 1977.6/ On October 2, 1979, the Secretary issued two delegation orders delineating the areas of authority between the ERA and the FERC with respect to section 3

applications, and setting forth certain criteria to aid the ERA in executing its responsibilities.7/

The Phillips and Marathon application has been evaluated in accordance with the standards established by section 3 of the NGA, and the criteria set forth in DOE Delegation Order No. 0204-54. Under Section 3 of the NGA, the ERA must determine whether an export is not inconsistent with the public interest. In applying this standard, the ERA has authority to review and determine certain issues including but not limited to national and regional need for the gas, the price proposed to be charged for the gas at the point of exportation, the effect on the U.S. balance of payments, and consistency with relevant DOE regulations or statements of policy.

The ERA has concluded that the proposed extension of this LNG export will not be "inconsistent with the public interest," and the application should be approved. Our decision takes into account the lack of opposition to the extension of the authorization for five years and is based on the following findings. This is an ongoing project that has been successfully exporting LNG without significant interruption since 1969 and contributes favorably to the United States' balance of payments. There is no regional or national need for the gas to be exported, and the price of the export is reasonable.

DOE has determined that, because the proposed extension of this export will use existing pipeline and liquefaction facilities, granting this application is not a major Federal action significantly affecting the quality of the human environment within the meaning of the National Environmental Policy Act of 1969 (42 U.S.C. 4321 et seq. (1976)). Therefore, neither an environmental impact statement nor an environmental assessment is required.

A. Domestic Need for the Gas to Be Exported

A fundamental issue to be addressed in this proceeding is whether there will be a domestic need for the natural gas that the applicants seek to continue to export over the period requested. Analysis of this issue properly focuses on possible need for the gas in Alaska, the applicable region, and in the United States generally. The applicants have furnished ERA with a detailed study by the National Economic Research Associates, Inc. (NERA), to support their contention that there is no domestic need for this gas.8/ No party to this proceeding has contested the applicants' position on domestic need for the gas to be exported or furnished the ERA with any information that would conflict with the NERA study. The ERA therefore relies on the record, as discussed below, to support its decision that there is no domestic need for

the gas sought to be exported over the period requested.

1. Regional Need

The applicants have asserted that Alaska will not need this gas within the five-year extended contract period. As of January 1, 1982, the proven reserves of natural gas in the Cook Inlet Basin area alone were approximately 3,592 Bcf, while the 1981 annual sales of gas from the area (including this export) were 176 Bcf.9/ Therefore, at recent rates of production, proven reserves in the area constituted a 20-year supply to serve Alaska's needs. Existing proven gas reserves in the area are sufficient to meet a projected minimum annual demand of 197 Bcf for gas in the 1980's (including the proposed export), a 12 percent increase over 1981 demand.10/ These projections allow for normal growth in demand and extraordinary factors that may affect demand, such as possible new gas-powered generating facilities supplying a potential new electrical transmission intertie with Fairbanks, and increased residential and commercial use of gas caused by the possible establishment of a new State capital in Willow, Alaska.

Accordingly, there is no need for this LNG within the Alaskan region now or during the proposed extension period.

2. National Need

There is no national need for the Alaskan LNG proposed to be exported over the period requested. This Alaskan LNG cannot be delivered at a reasonable price to purchasers in the lower 48 states, principally because of the lack of any receiving facilities on the Pacific Coast and the high costs of shipping to the East and Gulf Coasts for the foreseeable future.

Pac Alaska has applied for authorization from United States regulatory agencies to transport LNG from Alaska to a receiving and regasification terminal in California to serve West Coast markets. Proceedings to authorize the siting of the receiving terminal are still pending before the FERC in Docket Nos. CP75-140 et al. Because of the substantial delay in this project, no receiving terminals for LNG presently exist on the West Coast, and none are likely to be constructed during the period proposed for the export in this case.11/ There is also no pipeline available to transport gas from the Cook Inlet Basin area to any of the lower 48 states. There is, therefore, no means available to transport to the West Coast any of the gas proposed to be exported.

Although there are LNG receiving terminals on the United States Gulf and

Atlantic Coasts, no U.S. flag LNG carriers can pass through the Panama Canal. No pipeline connects the Cook Inlet Basin with any of the lower 48 states. Therefore, delivery of this gas to the only possible market for it in the lower 48 states would require the passage by LNG carriers from Alaska south around South America and north again to the Gulf or Atlantic Coasts, a voyage of at least 20,000 miles.12/ The costs for transportation of gas in this manner, when added to liquefaction and regasification costs, would make the gas unmarketable.

In light of the above, we conclude that there is no national need for this gas over the course of the extended authorization.

B. Price

The price of the LNG under Article 9 of the Basic Agreement between the parties, as amended, was $5.76 per MMBtu delivered to the Tokyo Gas Flange, Tokyo, Japan, as of April 1982. This price is based upon a base price of 592.8 cents per MMBtu as adjusted by a formula indexing that base to the weighted average of the Government Selling Prices (GSP) in U.S. dollars per barrel weighted by the 1981 volumes for the top twenty crude oils (ranked by descending volumes) imported into Japan during calendar year 1981.

The formula by which Phillips and Marathon determine the applicable price for any given month is expressed as follows:

$$\text{Price for calendar month} = 592.8 \; \frac{\text{Av. GSP (Month Prior to Calendar Month)}}{34.48}$$

We have examined the delivered price of $5.76 per MMBtu, the formula utilized in calculating the price, and the estimated value of the LNG at the point of exportation, and determined that the price is reasonable.13/ The price and the related pricing formula represent an agreement between a willing seller and buyer as to an appropriate price to be charged for this LNG export which is marketable in Japan, the importing country.14/ ERA needs continuing information to monitor this changing price and to ensure that it remains reasonable. We will therefore require quarterly reports to be filed on the price of this export, which should cover the period since April 1982 when the Amendment was executed. Should the applicants wish to alter the pricing formula, they must seek ERA approval before any change becomes effective.

C. Balance of Payments

The dollar value of this export (about $300 million per year) represents a positive contribution to the overall balance of payments picture, as well as to bilateral trade between the U.S. and Japan. Specifically, $300 million represents an offset of roughly 1 percent of the U.S. overall balance of trade deficit of $28.668 billion in 1981 (projected), and an offset of about 22 percent of the U.S. bilateral trade deficit with Japan of $14.491 billion in 1981 (projected) .15/

D. Additional Conditions

With respect to take-or-pay and make-up provisions, Phillips and Marathon have asked us expressly to authorize them to export, on a best-efforts basis, any annual volumes of LNG not delivered under the Basic Agreement or the Amendment during the remainder of the extended contract term, including the seven-month period beginning June 1, 1989. Provisions to this effect are included in the Amendment in a new Section 6.3 to enable the parties to be more flexible and responsive to changing market conditions. Since the quantities of LNG which have not been delivered during the term of the Basic Agreement are small (20,722 MMBtu over 13 years--less than 4 percent of the total contract quantity from its start through May 31, 1982), the applicants assert that their delivery in accordance with the new provisions will have no impact on the export operations.

The applicants are requesting no substantive change in the take-or-pay and make-up provisions and no increase in the total volumes authorized to be exported. Our approval of Phillips' and Marathon's requests will improve flexibility and response to market changes under the contract and is not inconsistent with the public interest.

Order

For the reasons set forth above, pursuant to section 3 of the Natural Gas Act the ERA hereby orders that:

A. The export authorization previously granted Phillips Petroleum Company (Phillips) and Marathon Oil Company (Marathon) by the FPC, in the Order Authorizing Exportation of Liquefied Natural Gas and Dismissing Application for Permit, issued April 19, 1967, Docket Nos. CI67-1226 and AI67-1227, is hereby amended by extending the export authorization for an additional five years, until May 31, 1989, and for a maximum seven-month make-up period beginning June 1, 1989. The maximum annual quantities of LNG that may be exported for sale to the Tokyo Electric Power Company, Inc., and the Tokyo Gas Company Limited during the five-year extension shall not exceed

the following, except as authorized in Paragraph B below:

June 1, 1984, to May 31, 1985, and each of the subsequent four years: 50,570,000,000,000 Btu.

B. The above-referenced order is further amended to allow Phillips and Marathon to export any volumes of LNG authorized for export which have not been delivered or will not be delivered in a particular year during a subsequent year in the five-year extension ending May 31, 1989, or during the seven-month make-up period beginning June 1, 1989.

C. The above-referenced order is further amended to establish the following price terms. The LNG that is the subject of this authorization shall reflect a delivered base price of 592.8 U.S. cents per million Btu effective April 1, 1982, subject to change in accordance with the pricing formula in Article 9, Subsection 9.1(a) of the Thirteenth Amendatory Agreement, dated March 24, 1982:

$$\text{Price for calendar month} = 592.8 \; \frac{\text{Av. GSP (Month Prior to Calendar Month)}}{34.48}$$

WHERE: Av. GSP is the average of the Government Selling Prices (in U.S. dollars per barrel) weighted by the 1981 volumes for the top twenty crude oils (ranked by descending volumes) imported into Japan during the calendar year of 1981.

D. Effective in January 1983 and in the month following the end of each calendar quarter thereafter, Phillips and Marathon shall file a quarterly report with the ERA reflecting their applicable monthly sales price to Tokyo Electric Power Company, Inc., and Tokyo Gas Company, Limited, delivered at the Tokyo Flange for each month of the preceding quarter. The January 1983 report shall reflect, on a one-time basis, monthly prices from April 1982 through December 1982.

E. The petitions for leave to intervene filed by Pacific Alaska LNG Associates, Pacific Gas and Electric Company, Southern California Gas Company, and Northwest Natural Gas Company are hereby granted, subject to such rules of practice and procedure as may be in effect, provided that their participation shall be limited to matters affecting asserted rights and interests specifically set forth in their petitions for leave to intervene and that the admission of such intervenors shall not be construed as recognition by the ERA

that they might be aggrieved because of any order issued by ERA in this proceeding.

Issued in Washington, D.C., December 14, 1982.

--Footnotes--

1/ In March 1982, United States Steel Corporation completed its acquisition of Marathon, which was restructured on July 10, 1982. These corporate changes will have no actual impact on the export of LNG considered herein.

2/ There have been only insignificant interruptions in the supply of LNG for export to Japan that have caused less than 4% of the volumes contracted for not to be delivered since 1967. Phillips-Marathon Application at 15-16.

3/ 47 FR 25177 (June 10, 1982).

4/ Petitions of Northwest Natural Gas Company (Northwest), dated July 12, 1982 and a joint petition from Pacific Alaska LNG Associates (PacAlaska), Pacific Gas and Electric Company (PC&E), and Southern California Gas Company, (SoCal Gas), dated June 25, 1982.

5/ Pub. L. 95-91 (1977), 42 U.S.C. Secs. 7151 and 7172(f).

6/ DOE Delegation Order No. 0204-4, 42 FR 60725 (November 29, 1977).

7/ DOE Delegation Order Nos. 0204-54 and 0204-55 (44 FR 56735, October 2, 1979). These superseded two other DOE Delegation Orders, No. 0204-25 (to ERA) and 0204-26 (to FERC), both dated October 17, 1978 (43 FR 47769, October 17, 1978).

8/ The National Economic Research Associates, Inc. (NERA), An Economic Analysis of the Proposed Extension of the Phillips-Marathon Contract with Tokyo Gas and Tokyo Electric, May 1982 (NERA Study), furnished as Appendix A to the application of Phillips and Marathon.

9/ NERA Study at 4, 12.

10/ Id. at 33.

11/ Pac Alaska petition at 2-4; Application at 11; and NERA Study at 17.

12/ We note in comparison the distance to Japan from Alaska is approximately 6,000 miles.

13/ In previous proceedings, the ERA established a policy that the price of gas exported from the United States should equal that of imports of gas from the same country. There is no natural gas or LNG imported into the U.S. from Japan with which to compare this export. Therefore, the policy is not applicable and need not be considered in this case. (See El Paso Natural Gas Co., DOE/ERA Opinion and Order No. 18, August 21, 1980, ERA Docket No. 78-15-NG, 1 ERA Para. 70,513, Federal Energy Guidelines).

14/ Application at 10, 13; NERA Study at 15, 38-42.

15/ NERA Study at 43 and 44.

OFFICIAL SERVICE LIST

PHILLIPS PETROLEUM COMPANY

AND

MARATHON OIL COMPANY

ERA DOCKET NO. 82-04-LNG

APPLICANT REPRESENTATIVES

PHILLIPS PETROLEUM COMPANY Mr. John Horn
Manager, Natural Gas and LNG
Sales Division
Gas and Gas Liquids Group
Phillips Petroleum Company
Bartlesville, Oklahoma 74004

Kenneth Heady, Esquire
Vice President and General Counsel
Phillips Petroleum Company
Bartlesville, Oklahoma 74004

MARATHON OIL COMPANY Mr. S.C. Sandusky
Manager, Natural Gas Division
Marathon Oil Company
539 South Main Street

Findlay, Ohio 45840

C.O. Robinson, Esquire
Associate General Counsel-Production
Marathon Oil Company
539 South Main Street
Findlay, Ohio 45840

J.F. Bell, Esquire
Jones, Day, Reavis & Pogue
1735 Eye Street, N.W.
Washington, D.C. 20006

PETITIONS TO INTERVENE

PACIFIC ALASKA LNG ASSOCIATES E. R. Island
PACIFIC GAS AND ELECTRIC COMPANY Michael D. Gayda
AND Attorneys at Law
SOUTHERN CALIFORNIA GAS COMPANY 810 South Flower Street
Los Angeles, California 90017

Keith C. McKinney
Pacific Alaska LNG Associates
810 South Flower Street
Los Angeles, California 90017

Harry W. Long
Pacific Gas & Electric Company
Law Department
P.O. Box 7442
San Francisco, California 94120

NORTHWEST NATURAL GAS COMPANY Robert M. Johnson, Esq.
30 Northwest Natural Gas Company
Suite 1900
200 Southwest Market Street
30 Portland, Oregon 97201

Justin R. Wolf, Esq.
1625 K Street, N.W.
Washington, D.C. 20006