DOE TAKES CONCRETE STEPS TO STREAMLINE PERMITTING AND REASSURE GLOBAL LNG MARKETS

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U.S. LNG Alert

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Recently, the U.S. Department of Energy ("DOE") took two bold actions that strongly reaffirm the Trump Administration's support for U.S. LNG exports and provide reassurance to the global LNG market regarding the sanctity of DOE approvals of liquefied natural gas ("LNG") exports.

First, on June 11, 2018, the Office of Fossil Energy within DOE issued an updated study analyzing the potential Macroeconomic Outcomes of Market Determined Levels of U.S. LNG Exports ("2018 LNG Export Study"). This study continues DOE's practice of commissioning economic studies that consider the potential impacts of exports of U.S.-sourced natural gas as LNG to foreign trading partners.

Then on June 20, 2018, DOE published a Policy Statement Regarding Long-Term Authorizations to Export Natural Gas to Non-Free Trade Agreement Countries ("Policy Statement") [2], which addresses concerns that industry stakeholders have raised regarding DOE's past assertions of authority to modify or revoke certain LNG export authorizations. Both developments are positive developments for the U.S. LNG industry and demonstrate the agency's commitment to supporting the LNG export sector in the United States.

The 2018 LNG Export Study confirms DOE's previous findings that LNG exports create net benefits for the U.S. economy as a whole, stating that across "the entire range of scenarios, we find that overall U.S. economic output is higher whenever global markets call for higher levels of LNG exports, assuming that exports are allowed to be determined by market demand." [3] However, unlike previous economic studies contracted by DOE, the 2018 LNG Export Study does not set an upper limit of LNG export volumes. Instead, the 2018 LNG Export Study considers export scenarios that allow market forces to determine the quantity of U.S. LNG exports to non-Free Trade Agreement ("non-FTA") nations. This market-centric approach is consistent with decades of DOE precedent related to LNG imports and exports.

The 2018 LNG Export Study signals a move away from the volume-specific approach the agency's previous analyses have used. It is possible that DOE will use this study to inform all of its future authorizations for LNG exports to non-FTA nations, even beyond the 25 currently pending non-FTA applications. This new approach streamlines the DOE permitting process and removes some regulatory risk associated with the DOE LNG export permitting process.

DOE has posted the 2018 LNG Export Study to each of the 25 pending dockets for LNG exports to non-FTA nations. DOE will accept comments regarding the Study's methodology, results, and conclusions until 4:30 pm Eastern time on July 27, 2018 [4]. This comment period presents an opportunity for interested stakeholders to present their views to the agency.

In the June 20 Policy Statement, DOE clarifies its position regarding its authority to modify or revoke certain LNG export authorizations. Although DOE maintains that the U.S. Congress has granted the agency authority to modify or revoke its previous LNG export authorizations, DOE asserts in the Policy Statement that it understands the weight of this revocation authority and that the agency "does not foresee a scenario where it would rescind one or more [LNG export] authorizations" for exports to countries without a free trade agreement with the United States. In contrast to the 2018 LNG Export Study, DOE is not accepting public comments on the Policy Statement, although it is possible that interested stakeholders, especially those opposed to U.S. LNG export projects, will present their opposition to the agency. Therefore, it is important for interested parties to monitor this situation closely and consider engaging with DOE as events develop.

Please contact our team if you would like to discuss options for engaging with DOE on these matters.

BACKGROUND

Under Section 3 of the U.S. Natural Gas Act ("NGA"), DOE and the Federal Energy Regulatory Commission ("FERC") share jurisdiction over regulating the export of natural gas from the United States [5]. More specifically, DOE regulates the export of the natural gas commodity, including LNG exports, while FERC regulates the siting, construction, and operation of LNG import and export facilities. The NGA also distinguishes between natural gas exports to nations that have a free trade agreement with the United States requiring national treatment for trade in natural gas ("FTA nations") and exports to non-FTA nations, which are nations without such a free trade agreement and with which trade is not prohibited. Section 3(c) of the NGA automatically deems natural gas exports to FTA nations, including LNG exports, as consistent with the public interest and such applications must be granted without modification or delay [6].

By contrast, NGA Section 3 creates a rebuttable presumption that LNG exports to non-FTA nations will be consistent with the "public interest." Because the statute does not define the elements of the public interest standard, DOE has interpreted the public interest standard to include economic factors, as well as international impacts, security of gas supply, and environmental impacts.

FINDINGS OF THE 2018 LNG EXPORT STUDY

Since 2012, DOE has commissioned four studies analyzing potential economic impacts of LNG exports. The first two studies, undertaken in 2012, were in tandem: (1) a study by the Energy Information Administration ("EIA") that considered the potential impacts of LNG exports on U.S. energy markets, focusing on domestic consumption, production, and prices [7]; and (2) a study by NERA Economic Consulting that analyzed the potential macroeconomic impacts of U.S. LNG exports on the domestic economy [8]. These 2012 studies considered the impacts of LNG exports of up to 12 billion cubic feet per day ("Bcf/d"). In 2014 and 2015, DOE followed a similar bifurcated process, with EIA [9] and two other contributors, Rice University's Baker Institute and Oxford Economics [10], considering up to 20 Bcf/d of total annual export volumes.

Thus far, we have only seen the macroeconomic element of the 2018 LNG Export Study. It is unclear whether DOE will issue a microeconomic element as well. A brief summary of the Study follows below.

To assess the likelihood of different levels of U.S. LNG exports and to analyze the impacts of different export levels on the U.S. economy, NERA conducted the 2018 LNG Export Study using two probabilistic models.

First, NERA used the Global Natural Gas Model (the "GNGM") to estimate the levels of U.S. LNG exports under different domestic and international natural gas market conditions [11]. NERA started by identifying four factors that affect U.S. LNG exports: the (1) supply and (2) demand of natural gas in the United States, and the (3) supply and (4) demand of natural gas in the rest of the world [12]. The 2018 LNG Export Study considers each of these four factors under the three market conditions: high, central, and low [13]. Under the Study's high market condition, there will be no restriction on the use of fossil fuel that is stricter than existing restrictions; under the low market condition, all the countries in the world will adopt aggressive renewable energy policies that discourage the use of fossil energy. The 2018 LNG Export Study uses the central market condition as a referential benchmark [14].

For the supply and demand of natural gas in the United States, NERA based its analysis on the EIA's Annual Energy Outlook for 2017 and a national Renewables Mandate that is in line with California's stringent renewable portfolio standard. For the supply and demand of natural gas in the rest of the world, NERA based its analysis on the EIA's International Energy Outlook for 2017 and the International Energy Agency's World Energy Outlook for 2016 [15]. Using these data sets, NERA constructed a cumulative probability distribution over export levels under different natural gas market conditions and concentrated its analysis on the seven scenarios that are more likely to happen in 2040 [16]. DOE and KeyLogic Systems, Inc., a contributing consultant to the Study, then used a peer review process to refine the initial probability assessments [17].

Using its NewERA model of the U.S. economy (the "NewERA"), NERA provided macroeconomic projections over the 2020 to 2040 time period based on the levels of U.S. LNG exports under different market conditions. Under the NewERA model, all nine alternative scenarios project LNG export levels to be higher than their corresponding reference scenario [18]. The rising U.S. LNG exports will increase:

- Aggregate investment and consumption in the U.S. [19];
- Average U.S. households' welfare [20];
- Natural gas production [21];
- Return to labor and capital by drawing these inputs from other sectors that have relatively lower returns [22]; and
- U.S. GDP by capturing the economy benefits from export revenues, resource income, and additional wealth transfer in the form of tolling charges [23].

Given the projection that the overall U.S. economic output will be higher when the U.S. LNG exports are higher, the Study suggests that the United States should continue exporting LNG without restrictions as long as the global markets demand LNG export [24].

CLARIFYING DOE'S APPROACH TO EXPORT AUTHORIZATION REVOCATION

In DOE's 2011 authorization of the Sabine Pass LNG exports, the first modern non-FTA LNG export authorization, DOE asserted that Section 16 of the NGA provides the agency with authority to "make, amend, and rescind" LNG export authorizations [25]. DOE explained that it intended to monitor U.S. gas supply and demand dynamics and reserved the right to "ensure that the exports of LNG authorized herein and in any future authorizations of natural gas exports do not subsequently lead to a reduction in the supply of natural gas needed to meet essential domestic needs" if LNG exports jeopardized the public interest [26]. DOE has made a similar assertion of revocation authority in each successive non-FTA LNG export authorization.

However, DOE has not defined the circumstances in which it would exercise the revocation authority it asserts. Furthermore, no party has challenged DOE's assertion of this authority in court, leaving the contours of this authority undefined.

Numerous industry participants, from project developers to LNG offtake customers to project financiers, have questioned the scope of this authority and objected to the regulatory risk it creates for LNG export projects, which are highly capital-intensive. DOE has not exercised its authority to revoke a non-FTA LNG export authorization to date, but industry has raised concerns regarding the potential chilling effect that this unclear revocation risk creates for the industry. The Policy Statement is DOE's latest effort to address these concerns.

In its Policy Statement, DOE appears to lightly recommit to its assertion of authority to modify or revoke non-FTA LNG export authorizations, stating that it has the authority under the NGA to take steps to protect the public interest [27]. But DOE expressly notes that it has never modified or revoked a non-FTA LNG export authorization and has revoked an FTA LNG export authorization only once in a "highly unusual scenario." [28]

DOE goes on to state that it "wishes to allay the concerns about existing (or future) export authorizations," confirming its commitment to the LNG export authorizations. DOE explains that it based each of the 29 non-FTA LNG export authorizations it has issued on a "thorough consideration of the public interest" and found that the non-FTA LNG exports will create substantial benefits for the public interest. In particular, DOE notes that its authorizations have found that U.S. LNG exports will create net economic benefits and will provide energy security and environmental benefits to the global community, [29] a point which is further supported by the 2018 LNG Export Study discussed above. DOE asserts further that federal courts have upheld its non-FTA LNG export authorizations, so "[a]uthorization holders, as well as any interested stakeholders, thus should have the utmost confidence in the validity of [DOE's] LNG export authorizations for the full term of each non-FTA order." [30]

DOE concludes by recognizing the importance of the regulated community's investment-backed expectations, noting the substantial investments in infrastructure and natural gas supplies that LNG exporters and their customers have made [31]. The agency states that although it will take the actions it deems "necessary or appropriate" to implement Congress's mandates under the NGA, DOE "remains committed to the durability and stability of the export authorizations it has granted under the NGA, as well as to supporting the approved export of U.S. natural gas around the world." [32]

IMPLICATIONS

The 2018 LNG Export Study represents a positive shift in DOE's approach to analyzing the potential economic impacts of LNG exports on the U.S. economy. By removing the volumetric limits from the analysis and reducing the likelihood that future iterative studies will be needed, DOE is taking an important step in streamlining its LNG export permitting process.

Assuming that DOE finalizes and accepts the findings in the 2018 LNG Export Study, the study's conclusions eliminate an one factor that DOE might have used as a basis to modify or revoke a non-FTA LNG export authorization. With the 2018 LNG Export Study's findings of net macroeconomic benefits at all levels of LNG exports, DOE is much less likely to deem domestic natural gas market dynamics as a key factor in determining whether to modify or revoke a non-FTA LNG export authorization. The Policy Statement should help the global LNG industry to understand the scope of DOE's asserted authority better, despite the agency's tacit endorsement of the prior administration's views on the agency's authority to revoke.

More broadly, the 2018 LNG Export Study signals that the DOE under the Trump Administration is ready to authorize additional non-FTA LNG export applications to further the Administration's “Energy Dominance” agenda [33]. The Policy Statement represents a similar signal, removing a measure of regulatory risk from the DOE process and committing to allowing market forces, and the contracts that substantiate those market forces, to guide the agency's LNG export decisions. This approach encourages industry participants to develop all LNG export projects that the global natural gas market will support.

As noted above, DOE will accept public comments on the 2018 LNG Export Study until 4:30 pm Eastern time on July 27, 2018. Interested stakeholders should consider engaging in this process by filing comments on the Study. Likewise, stakeholders should monitor the response to the Policy Statement, including any comments submitted to DOE, and consider engaging as appropriate.

Notes

[1] The authors appreciate the assistance from Yaomin Pan, a 2018 Summer Associate with K&L Gates, in researching and drafting this piece.

[2] DOE issued a pre-publication version of the Policy Statement prior to formal publication in the Federal Register, which is available here: https://www.federalregister.gov/documents/2018/06/21/2018-13427/policy-statement-regarding-long-term-authorizations-to-export-natural-gas-to-non-free-trade (hereinafter “Pre-Publication Policy Statement”).

[3] NERA Economic Consulting, *Macroeconomic Outcomes of Market Determined Levels of U.S. LNG Exports* 14 (June 7, 2018), https://fossil.energy.gov/app/docketindex/docket/index/10 (“2018 LNG Export Study”).

[4] Study on Macroeconomic Outcomes of LNG Exports, 83 Fed. Reg. 27,314 (June 12, 2018).

[5] 15 U.S.C. § 717b(3)(a).

[6] 15 U.S.C. § 717b(3)(c).

[7] Energy Information Admin., *Effect of Increased Natural Gas Exports on Domestic Energy Markets 1* (Jan. 2012), https://www.energy.gov/sites/prod/files/2013/04/f0/fe_eia_lng.pdf.

[8] NERA Economic Consulting, *Macroeconomic Impacts of LNG Exports from the United States 3* (Dec. 2012) https://www.energy.gov/sites/prod/files/2013/04/f0/nera_lng_report.pdf.

[9] Energy Information Admin., *Effect of Increased Levels of Liquefied Natural Gas Exports on U.S. Energy Markets* (Oct. 2014), https://www.eia.gov/analysis/requests/fe/pdf/lng.pdf.

[10] Oxford Economics, et al., *The Macroeconomic Impact of Increasing U.S. LNG Exports* (Oct. 29, 2015), https://www.energy.gov/sites/prod/files/2015/12/f27/20151113_macro_impact_of_lng_exports_0.pdf (note that the 2015 study considered one scenario that examined exports of up to 28 Bcf/d).

[11] 2018 LNG Export Study at 14.

[12] *Id.*

[13] *Id.* at 14-15.

[14] *Id.*

[15] *Id.*

[16] 2018 LNG Export Study at 64. These scenarios are within one-standard deviation interval around the mean export level in 2040. NERA estimates that there is a 68% probability that U.S. LNG exports volumes will be within

a one-standard deviation interval. *Id.* at 16.
[17] *Id.*
[18] *Id.* at 62.
[19] *Id.* at 74-76.
[20] 2018 LNG Export Study at 65-67.
[21] *Id.* at 77-78.
[22] *Id.* at 69-70.
[23] *Id.* at 67-68.
[24] *Id*. at 14.
[25] *Sabine Pass Liquefaction*, LLC, DOE/FE Order No. 2961 at n. 45 (2011).
[26] *Id.* at 32-33.
[27] Pre-Publication Policy Statement at 3.
[28] *Id.* at 4. DOE points to the case of the Louisiana LNG project, where the project developer functionally abandoned its project and stopped responding to communications from DOE. *Id.* at 4-5.
[29] *Id.* at 6.
[30] *Id.*
[31] *Id.* at 6-7
[32] *Id.* at 7.
[33] Statement from Sec. of Energy Rick Perry on DOE's Regulatory Review Report to the President (Oct. 25, 2017) https://www.energy.gov/articles/statement-secretary-energy-rick-perry-doe-s-regulatory-review-report-president.

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