Powerful Friends and Cozy Relationships Helped Cheniere Cut Through Regulation

By **Peter Mantius**, on May 23rd, 2013

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How They Saved Cheniere from Disaster to Dominate US LNG Exporting

Spencer Abraham, John Deutch, Vicky Bailey, Neil Bush

Five years ago, Cheniere Energy Inc. was losing tens of millions of dollars a quarter and slashing its workforce in half, as crippling debt threatened to force it into bankruptcy. Today it's the undisputed leader in the nation's promising new energy sector: exporting liquefied natural gas, or LNG. That remarkable turnaround followed its industry-leading decision in 2010 to reverse course and export, rather than import, natural gas.

Cheniere's success in executing that costly and risky switch is a direct result of its ability to obtain a unique regulatory status. Federal energy regulators have awarded the company a combination of federal permits — so far withheld from all 20 competitors seeking similar treatment — that have worked like sprinkled pixie dust, attracting major customers and investors to Cheniere and giving wing to its stock.

Among the power brokers who've hitched a ride:

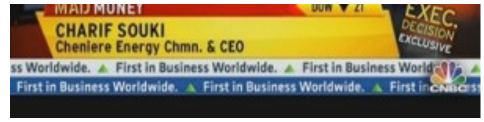
- Spencer Abraham, a former secretary of the Department of Energy (2001-2005), who formed a consulting firm in late 2005 that landed Cheniere as its first major client. That prompted one television stock touter to rate Cheniere stock a "triple buy" as a "pure play on cronyism."
- John Deutch, a former director of the CIA (1995-1996) and recent chairman of a DOE advisory committee on natural gas, who serves as a Cheniere director and holds company stock and options worth $1.7 million.
- Vicky Bailey, a former commissioner of the Federal Energy Regulatory Commission (1993-2000), a former senior deputy to Abraham at the DOE and current Cheniere director with stock and options worth $1.6 million.
- Neil Bush, the younger brother of former President George W. Bush, who served as co-chairman of a company that partnered with Cheniere in 2001 and collected at least $22 million in royalty payments over a decade.

There's no evidence any of the four acted illegally or improperly for the Houston-based energy company. But each has benefitted financially, and each has been in position to wield influence on its behalf with government officials. And Cheniere's bumpy 15-year journey from relative obscurity has been marked by remarkably favorable government treatment.

From 2000 to 2008, Cheniere was committed to building several multi-billion-dollar LNG import terminals in Texas and Louisiana to serve the nation's anticipated need for natural gas. The facilities were in various stages of completion when the import market simply dried up, knocking the company's stock from $40 in October 2007 to $1.12 a year later. The culprit: major new domestic gas supplies obtained from hydraulic fracturing, or fracking, of shale formations.

With his back to the wall, Cheniere's energetic chief executive, Charif Souki, opted to switch from importing LNG to exporting it. It was a brassy idea, given Cheniere's debt load and its need for fresh money (many billions of dollars) and time (four or five years) to build the necessary export facilities. How could Souki possibly beat less-encumbered competitors? He's managed.

The pivot point in the company's turnaround came in May 2011 when the DOE granted Cheniere authority to export LNG to countries without a free trade agreement with the United States. That includes Japan,



Charif Souki

India, China, Korea and most of Europe — the LNG markets that really matter. Permits to export to free-trade countries like Canada and Mexico are automatically granted and therefore far less valuable.

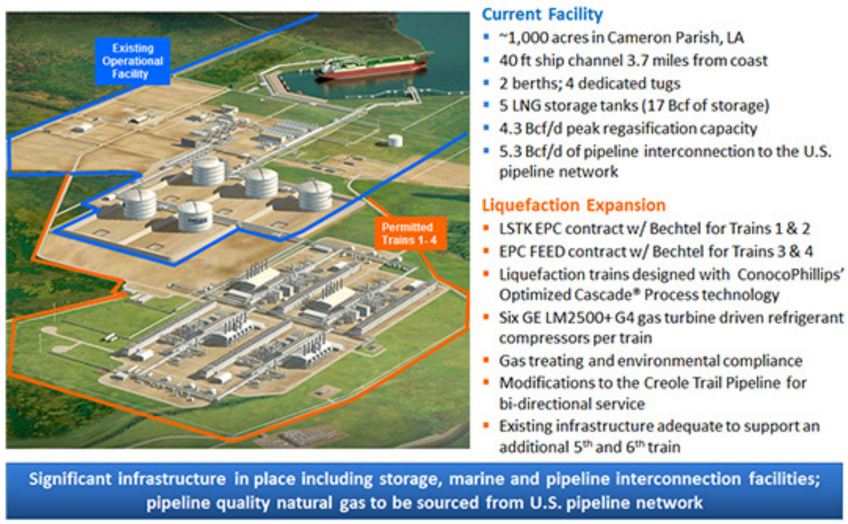
Cheniere was the first to apply for the prized non-FTA export permit, but when other companies quickly followed suit, the DOE slapped a moratorium on approvals. Then on May 17, the DOE ended its moratorium by granting Freeport LNG a provisional non-FTA export permit.

The DOE had processed Cheniere's application in nine months. Freeport's, filed in December 2010, took 30 months. And Freeport still can't begin construction on its export terminal until it clears another challenging regulatory hurdle with FERC.

The DOE's selective favor has provided Cheniere a distinct market advantage, rescuing it from a lingering cash crunch and setting the table for a spectacular run for the company's stock — ticker symbol "LNG."

In August 2010, just before Cheniere announced plans to seek the DOE's permission to export LNG, its stock traded at $2.41. Just after the permit was bestowed, the stock had surged to $11.56, a 380 percent gain.

With the DOE permit in hand, the company quickly signed 20-year LNG contracts with groups in the United Kingdom, Spain, India and Korea to export LNG from its Sabine Pass, La., terminal on the Texas border along the Gulf Coast.

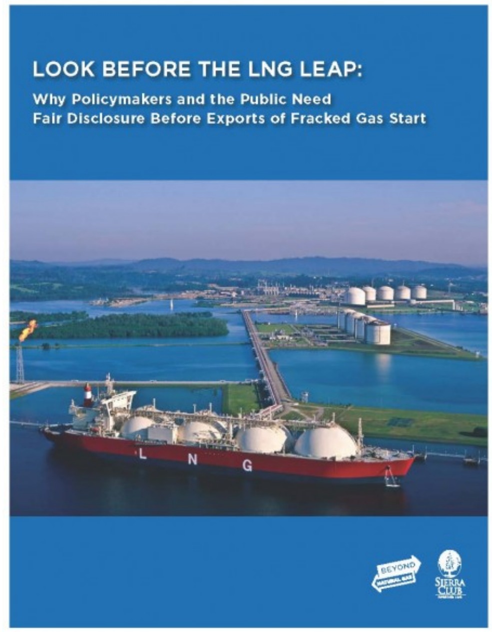


Sabine Pass Project

The Sabine Pass export facilities weren't built yet — or even financed — and they couldn't be finished before 2016. But the DOE permit and the new foreign commitments provided Cheniere extraordinary momentum. Bechtel signed a $3.9 billion construction agreement, and the Blackstone Group stepped up with a $2 billion lead investment — a good start toward the more than $5.6 billion needed for the first construction phase.

Cheniere also needed a site permit from FERC, the lead environmental regulator for LNG terminals. That green light arrived like clockwork in April 2012 and allowed the company to avoid risky and costly delay.

In order to bestow that accommodation, FERC had to reject arguments by the Sierra Club and others who demanded a full environmental impact statement, or EIS, on the project. The commission opted instead for a shorter review known as an environmental assessment after concluding that it was not "reasonably foreseeable" that billions of dollars in LNG exports from Sabine Pass would simulate domestic gas drilling using the environmentally disruptive fracking process. FERC's denial of compelling evidence of a link between LNG exports and new fracking flew in the face of analyses by the U.S. Energy Information Agency and several private firms.



Craig Segall, a Sierra Club attorney, said federal regulators have turned a blind eye to the fracking boom's potential threat to water and air quality. As the DOE weighs whether to allow exports of up to 45 percent of current domestic gas production, it has so far deferred to FERC and "refused to disclose, or even acknowledge, the environmental consequences of its decisions.

"The DOE needs to change course," Segall wrote in a recent Sierra Club analysis.

If FERC's decision to waive an EIS for Sabine Pass stands as a precedent in handling other LNG export applications — including Freeport LNG's — it could have profound implications for federal policy on fracking, not to mention climate change.

Those energy policies are the purview of Deutch, 74, who joined the Cheniere board in 2006. Two weeks before the DOE granted Cheniere its crucial LNG export license, DOE Secretary Steven Chu picked Deutch to chair a new advisory panel to study fracking's role in the shale gas boom and to recommend ways to frack more safely and cleanly.

Deutch, an emeritus professor at the Massachusetts Institute of Technology, already had a running start on the issue. That same month, MIT released a landmark study called "The Future of Natural Gas." Deutch had served on the study group that prepared it.

The MIT report concluded that natural gas was a clean-burning "bridge fuel" to a future dominated by renewable energy sources. It found that fracking's environmental impacts were "challenging but manageable." It did not call for federal regulation of the process, and it downplayed fracking's release of methane, a potent greenhouse gas. The study viewed the emerging worldwide LNG trading market as a positive development, although it did not explicitly recommend unlimited U.S. exports of LNG.


Ernes tMoniz

Critics of the MIT study noted that it was sponsored primarily by an affiliate of Chesapeake Energy, one of the nation's leading frackers and a speculator in land leases for future drilling. They noted Chesapeake's hand in framing the research and that the study's results often dovetailed with the company's positions.

Even so, the MIT study — along with the findings of the DOE's Deutch-led advisory panel on fracking — may be the best approximation available of the national policy for developing and marketing natural gas. President Obama indirectly endorsed the MIT work in early March when he nominated its lead author, MIT physics professor Ernest Moniz, to replace Chu as his Secretary of Energy. Moniz was sworn in as the nation's new energy chief May 21.

In recent weeks, both Moniz and Deutch have come under fire for their financial ties to the energy industry. Moniz has since quit an advisory board for a private equity partnership — run by Deutch's son — that invests in energy projects.

Responding to questions about his potential conflicts, Deutch wrote in an email to the DCBureau: "All of my business relationships, including my position as a director of Cheniere, were disclosed to the DOE prior to my appointment as chair of the Secretary of Energy Advisory Subcommittee on unconventional gas. All members of the subcommittee had relationships that contributed to their knowledge and experience in natural gas matters."

Moniz has testified that he plans to continue the agency's deliberate approach toward granting more non-FTA export permits. He promised to consider each of the 19 remaining applications on a case-by-case basis, in the order the applications were received, weighing the national interest each time.
Meanwhile, as its competitors are held at bay, Cheniere races ahead with construction of Sabine Pass export facilities capable of handling 2.2 billion cubic feet of gas per day by 2016.

That's roughly 3.5 percent of all U.S. natural gas production. If every pending export project were to get the green light — and many in the energy industry and the media argue that they should — LNG exports would near half of current domestic gas production.

Souki has said he considers it likely that some, but not all, his potential competitors will finish their projects. “It’s not going to be a monopoly,” he said in a TV interview in January. “Other people see this is something that makes sense. There is so much gas in the United States and so much demand on a global basis, that there is no limit to how much can be exported.”

But challenges will weed out competitors. “Unless you’re ready to spend $100 million and two years in planning, you’re not going to have anything,” Souki added.

Aside from Freeport LNG, three other groups are waiting in the wings as likely Cheniere competitors, but they still need DOE and FERC permits:

- Dominion Cove Point LNG, a $3.4-$3.8-billion project by the utility Dominion on the Chesapeake Bay in Maryland.
- Cameron LNG, a $6-$7-billion project by Sempra Energy in Hackenberry, La.
- Golden Pass, a $10 billion project by ExxonMobil and Qatar Petroleum International on the Texas shore of the Sabine River, a few miles from Cheniere’s Sabine Pass terminal.


Patricia Outtrim

Roughly 20 federal and state agencies get involved in LNG terminal projects, Patricia Outtrim, Cheniere’s vice president for government and regulatory affairs, told a Senate panel May 21. “An LNG project can take up to three years, and a sponsor must spend up to $100 million for compliance to receive all necessary permits. The vast majority of these costs are spent during the FERC process.”

The Sabine Pass terminal already has facilities, completed in 2008, to import up to 4 billion cubic feet per day. Construction on the export facilities began last summer.

Before natural gas can be sent off by ocean tanker it must be purified, cooled to -160 C and liquefied. Cheniere has authorization from FERC to build four liquefication units, or trains, at Sabine Pass and it has applied for permission for build two more.

Souki has expressed hope that the company is now on firmer ground with its export contracts than it was with its old import agreements. Planned import deals evaporated between 2006 and 2008. This time Souki’s export deals with the UK’s BG Group PLC, Spain’s Gas Natural Fenosa, Korea’s KOGAS and India’s Gail provide Cheniere with revenue topping $2.5 billion a year for 20 years.

The company did not respond to an emailed question about whether Cheniere needs to meet certain construction or financing schedules in order to collect that promised revenue. The company’s new bet is that the fracking boom will provide ample domestic gas supplies to keep U.S. natural gas prices far below other world markets indefinitely. Today, U.S. gas sells for roughly $3.50 per thousand cubic feet, while prices in Europe top $10 and prices in Asia often top $15.

That wide gap, and Cheniere’s unique position to exploit it, has driven the company’s stock above $30. But even if U.S. gas prices rise and world prices drop, shrinking or erasing the arbitrage opportunity, Souki can count on the four large fixed-price contracts, along with more recent deals with France’s Total and the UK’s Centrica.

A Cheniere official said Souki would not agree to be interviewed or to answer emailed questions. “As Charif is traveling, he will not be available for an interview,” media specialist Diane Haggard said in an email May 22. “He is really the only person who would be able to respond to your questions, so I am unable to provide another candidate for an interview.”

Souki, 60, was born in Lebanon and educated in the U.S. (Colgate and Columbia universities). Fluent in Arabic and French, he worked as an investment banker before co-founding Cheniere as an oil and gas exploration company in 1996. He once told an interviewer that the name Cheniere is derived from “chene,” the Acadian word for oak — such as those that grow in the Louisiana marshes near Sabine Pass.

During the late 1990s, the company pumped a few gas and oil wells in the Gulf of Mexico.

The election George W. Bush in 2000 opened up new opportunities in the energy industry, and the new president mentioned his interest in seeing LNG storage and import facilities developed. That energized a host of speculators who began scouring the Texas-Louisiana coastline for sites on deep channels that could accommodate 1,000-foot LNG tankers.

Both Cheniere and Crest Investment Co. — Neil Bush’s company — set their sights on Quintana Island, a long skinny strip connected by a bridge to the mainland near Freeport, Tex. Souki prepared far more diligently than Crest for actual LNG development. He’d hired a team headed by Charles Reimer, who’d run a major LNG plant in Indonesia, and took a plan to the local harbor commission.

Despite Crest’s relative lack of experience or preparation, it drew the commission’s nod for a three-year lease option to build an LNG facility on Quintana.

At the time of the competition for rights to Quintana Island, Neil Bush’s role in Crest wasn’t widely known. But details emerged in a sworn deposition Bush gave in 2003 divorce proceedings. According to The Los Angeles Times, Bush testified that he served as “co-chairman” of Crest and was paid about $60,000 a year for working “maybe three or four hours a week” on miscellaneous consulting tasks.

Neil Bush, now 58, is one of former President George H.W. Bush's five children. He's the younger brother of George W. Bush, the 43rd president, and Jeb Bush, former governor of Florida and possible 2016 Presidential candidate. Neil Bush has been involved in a wide variety of businesses over his career. In 1991, his business reputation was tarnished when the federal Office of Thrift Supervision cited his role in the $1.3 billion failure of Silverado Savings and Loan in Colorado. As a Silverado director, the OTS said, Bush had "multiple conflicts of interest" with developers seeking loans from Silverado.

Jamal Daniel

Years later, when Crest was pursuing Quintana Island, the public face of the company was Jamal Daniel, a Syrian-born Houston businessman who grew up in Lebanon before moving to Geneva, Switzerland, after high school. According to the LA Times, local harbor commission memos described Daniel as a friend of Spencer Abraham, the new president's Secretary of Energy. Like Crest's Daniel and Cheniere's Souki, Abraham has family roots in Lebanon.

In June 2001, Crest traded its Quintana lease option to Cheniere for Cheniere stock and guaranteed royalty payments to Crest ranging from $2 million to $11 million a year.

An internal memo specified that Cheniere would be responsible for project operations while Crest would "handle the political permitting side," according the LA Times's 2004 report. House Majority Leader Tom DeLay of Texas and Abraham's DOE office urged FERC to approve LNG import plans at Quintana, the newspaper added.

Neil Bush did not respond to phone and email messages seeking comment.

In 2003, Cheniere sold a majority interest in the Quintana Island project to Michael Smith. The company retained a 30 percent interest in Freeport LNG until 2010, when it sold that stake for $128 million. But complex obligations related to the "Crest Royalty" remained on Cheniere's books until they were finally resolved in 2012, according to the company's annual report.

Today, Smith and ConocoPhillips share control Freeport LNG. In an October 2012 interview with the Houston Business Journal, Smith expressed frustration that the DOE hadn't given his company the prompt permitting treatment Cheniere received.

"It would be completely unfair that one company (Cheniere) has the exclusive right to export (to non-free-trade agreement countries) from the United States," he told the HBJ. "I think it's a little unprecedented. But if that happens, then we would have to try to export to free-trade countries — there are just not a lot of free-trade countries who are in need of LNG."

As Cheniere began to disengage from Freeport in 2003, it focused on building giant import terminals at Sabine Pass, Corpus Christi and another site in Louisiana. In December 2003, it filed with FERC for regulatory approvals.

At the time, more than a dozen companies were in the process of announcing plans for large LNG terminals. While the demand for the import projects was high, local resistance and regulatory hurdles raised development costs and risks. Projects on the East and West coasts faced longer odds than those on the Gulf Coast, where the oil and gas industries are more widely accepted.

Environmental issues even snagged ExxonMobil. In the face of heavy local resistance in November 2004, the industry giant withdrew its plans for an LNG import terminal in Mobile Bay, Ala.

Cheniere pressed on and worked hard to win local support at Sabine Pass in particular.

"Our message to Washington," Cheniere President Keith Meyer told the Houston Business Journal, "is that we know there is resistance on the East and West coasts to some of these projects, but the nation needs this supply. So don't let that resistance frame the debate or determine the way all of these projects are addressed."

FERC
FEDERAL ENERGY REGULATORY COMMISSION

Cheniere had the right touch. FERC delivered the permit in December 2004, just under a year after Cheniere had filed its application. Anticipation of that approval supercharged the company's stock. The week before it filed its FERC application, shares sold for $3.48. By the time FERC delivered, shares had rocketed to $32.35.

During the year that FERC was considering Cheniere's application, buzz about LNG imports was building. In February 2004, Abraham, nearing the end of his term as Secretary of Energy, gave the keynote address at a Houston energy conference touting LNG as the next great global energy industry.

Abraham resigned at the end of the first Bush-Cheney term. Several months later, he founded The Abraham Group, a Washington, D.C.-based energy consulting group. In October 2005, a day after he unveiled his new venture, Abraham announced that Cheniere had hired his group to review its LNG options.

News that Cheniere had employed Abraham drew raves from Jim Cramer, host of CNBC's 'Mad Money' stock tip show. Cramer declared that investors could bet on Abraham to "work the Spencer magic" and deliver the necessary government permits. Give it 18 months, Cramer said in the segment that included his crack about the "pure play on cronyism." Seven years later, the Abraham Group's website still includes an article on Cramer's gushing commentary.

While DOE and other agencies have roles in approving LNG terminals, a 2005 law gave FERC the lead role in addressing environmental issues.

Cheniere wasted little time in adding an experienced FERC hand to its board of directors. When Vicky Bailey joined the board in March 2006, she brought eight years of experience — virtually the entire Clinton Administration — as one of FERC's five decision-making commissioners. Bailey had also worked for Abraham as a senior DOE official in the Bush Administration.

By the end of 2006, FERC had nearly tripled the permitted LNG import capacity of both Sabine Pass and Freeport LNG's Quintana Island, in which Cheniere still held a 30 percent stake. And it gave another Cheniere LNG terminal project, Creole Trail in Louisiana, approval to begin construction.

While there's no evidence Bailey did anything to obtain those FERC approvals, they easily fell within the 18-month window Cramer had allowed for "the Spencer magic."

Bailey declined to comment. Efforts to interview Abraham were unsuccessful. An official at his consulting firm accepted emailed questions but did not respond by the stated deadline.

In spite of the new FERC permits, the company's shares began feeling headwinds after hitting an all-time high of $43.72 in April 2006. Perhaps investors began to question the strength of import demand. In any case, work on the Corpus Christi and Creole Trail terminal projects slowed or halted.

Still, Souki managed to rekindle shareholder excitement the following winter by spinning off the Sabine Pass project into a tax-advantaged master limited partnership, apparently the first one ever allowed by the IRS for an LNG terminal. Cheniere kept 88 percent control of the publicly traded new entity, Cheniere Energy Partners. And Cheniere's stock nearly matched its record high in the months after the MLP's initial public offering in March 2007.

The excitement continued two months later when Cheniere sponsored a springtime Washington, D.C., summit on LNG hosted by The Abraham Group. It drew former Federal Reserve Board Chairman Alan Greenspan and luminaries from LNG leaders Qatar, Algeria and Trinidad & Tobago.

But by then the LNG import market was turning inexorably against the company. The fracking-powered shale gas boom took hold in 2008, driving down prices and killing demand for imported gas. That April the company announced that it was laying off roughly half its work force. Cheniere's stock fell like a rock, hitting a low of $1.12 that fall amid the general market collapse.

Stuck with more than $2.5 billion in debt and lacking major customers, Cheniere began hearing whispers of bankruptcy from financial analysts at Moody's and Standard & Poor's.

Souki himself pulled no punches in his April 27, 2009 letter to shareholders, saying: "Our challenge this year will be to correct our balance sheet. The company is too leveraged for the new capital market environment in which the world exists today. Management will focus on deleveraging the company."

But those days are ancient history now. Souki and Cheniere are back on top. The company's market value has soared past $6.5 billion, and the value of Souki's shares are climbing toward $300 million.


Majida Mourad

Meanwhile, Cheniere has named long-time Abraham aide Majida Mourad to vice president for government relations. Like Souki and Abraham, Mourad has Lebanese roots. She once held senior positions with Abraham's U.S. Senate campaign in Michigan, with his office at DOE and with The Abraham Group. Abraham himself has continued to promote the economic benefits of exporting LNG as well as the engine that drives it: the fracking of shale gas formations.

Last fall, a chorus of opinion piece writers touted the economic benefits of fracking shale gas. The group included MIT's Deutch, New York City Mayor Michael Bloomberg, fracking pioneer George Mitchell, New York Times columnist David Brooks and Pulitzer Prize-winning energy analyst Daniel Yergin.

Then in December, a DOE-commissioned study by NERA Economic Consulting concluded that LNG exports would be a net economic benefit to the nation. It downplayed concerns that exports would drive up domestic gas prices and shift wealth from consumers to energy investors. Instead, the report concluded that the more LNG exports, the more net benefit to the economy.

While the study triggered widespread criticism for its methodology and conclusions, Abraham was quick to praise it. In an opinion piece for the Financial Times, Abraham and Bill Richardson, Secretary of DOE under President Bill Clinton, touted both gas drilling and LNG exports as an economic and foreign trade bonanza.


Sen. Ron Wyden

Sen. Ron Wyden (D-Ore.), chairman of the Senate Energy and Natural Resources Committee, is one who isn't sold. At a Senate committee hearing May 21, he noted that only five years ago the smartest people in the energy industry were certain the U.S. would be importing gas indefinitely — that is, until they "suddenly changed their minds."

In his opening remarks at the hearing, Wyden said, "The current application process for approval of LNG export terminals may not properly reflect these larger economic challenges I've described. I am not convinced that that application process is right for these times."

Moniz said he's listening, promising that his analysis won't stop with NERA's conclusion that unlimited LNG exporting is all good. "Everything's on the table until I have done my analysis," Moniz testified. "That's my commitment to Chairman Wyden."

Peter Mantius

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