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April 11, 2013

The Honorable John Kerry
Secretary of State
Washington, D.C. 20520

Re: EPRINC Comments on Draft Environmental Impact Statement on the Keystone XL Pipeline Proposal

Dear Mr. Secretary:

The Energy Policy Research Foundation is a non-profit organization that has published extensive research on developments in U.S. and world energy markets since 1944. We have been called to testify at nearly every session of Congress in the last decade and routinely provide briefings on our research for industry, non-profit organizations, federal, state, and local agencies and Congressional staff. EPRINC has been a source of expertise for numerous government studies and its chairman and president have served on virtually every National Petroleum Council study of oil and gas issues. We welcome the opportunity to comment on the environmental impact statement prepared by U.S. Department of State on the implications of constructing the Keystone XL pipeline.

In response to a 2009 request from U.S. Secretary of Energy Steven Chu, the National Petroleum Council (NPC) issued an extensive report on North American potential to expand oil production. The report's authors, an authoritative group of experts from in and outside the petroleum industry, concluded that North America could raise petroleum liquids output from approximately 10 million barrels/day (mmb/d) in 2010 to over 20 mmb/d by 2035. The majority of the new supply would come from four sources: tight oil, shale oil, natural gas liquids, and oil sands. The NPC identified Canadian oil sands as having the potential to increase North American supply by 3 to 4 mmb/d by 2035.

Although the US currently imports over nearly 2.5 mmb/d of Canadian crude oil through an extensive pipeline and rail network, planned increases in Canadian output will require more crude transportation capacity. Because both Canadian crude production and U.S. crude production have risen in tandem, the pipeline capacity to import Canadian crude is constrained and is lowering wellhead values on Canadian and U.S. crude oil production. Keystone XL is a necessary infrastructure project that will help move Canadian crude directly from Alberta to the Gulf Coast, bringing needed relief to extensive pipeline capacity constraints on both U.S. and Canadian crude pipelines.

The proposed Keystone XL pipeline is an expansion of TransCanada's current Keystone pipeline network and will include sufficient capacity to carry both Canadian oil sands production and up to

100,000 b/d of crude oil from the surging production now taking place in North Dakota (and Montana to a lesser extent), largely from the Bakken formation. Since 2008, production from North Dakota has risen from 100,000 b/d to fast approaching 800,000 b/d today. By increasing crude oil transportation efficiency and allowing Bakken producers to access new refinery markets, the Keystone XL project will have the added benefit of improving wellhead values for oil production from the Bakken formation. Although our research shows that rail shipments will continue to provide an important role in moving crude oil across the North American continent, Keystone XL is an essential piece of new petroleum infrastructure. The mid-continent region of the United States no longer processes waterborne imports; i.e., refiners in the Rockies and mid-continent of the U.S. are processing only U.S. and Canadian feedstock and running at full capacity. New Canadian and mid-continent crude production will have to be shipped to coastal refining centers in the U.S. Keystone XL plays a vital role in adding the necessary infrastructure to move Canadian crude to the U.S. Gulf Coast and help displace waterborne imports from Venezuela and Mexico.

US law requires that any cross border pipeline receive a presidential permit and this authority is delegated to the State Department. Under the North American Free Trade Agreement (NAFTA), no permits are required for shipment of Canadian crude to US destinations by rail, ocean tanker, or even incremental volumes through existing cross-border pipelines. The open border in energy trade between Canada and the United States provides substantial benefits to both countries and has led to highly integrated cross border energy and investment flows.

Technical and environmental reviews of the project have been underway in Canada and the U.S. since 2008. The project required an environmental assessment under a federal law called the National Environmental Policy Act (NEPA). Although NEPA required the federal government to declare national and environmental goals and the establishment of the Council on Environmental Quality (CEQ), the centerpiece of the legislation is the requirement of an extensive environmental assessment of any federal action with a major effect on the human environment. As a result, vetting of the Keystone XL pipeline route has been extensive. During the review process, TransCanada agreed to 57 project-specific requirements, exceeding all U.S. pipeline safety standards, including satellite-linked computerized leak-detection systems and puncture-resistant steel pipe.

Given the established history on U.S.-Canadian energy trade, TransCanada had no real reason to doubt ultimate approval of the project as all previous cross border pipelines had been approved. TransCanada spent more than \$2 billion for steel and related facilities under expectations that the historical relationship in cross-border energy trade would be sustained. The delays in construction have cost TransCanada hundreds of millions of dollars. Towards the second half of 2011, objections to the route were raised by officials in Nebraska over concern that the pipeline crossed “ecologically sensitive terrain” above an important aquifer. Instead of approving the project and letting the legal process play out in Nebraska, the State Department in early November 2011 announced a decision that granting the cross-border permit would be postponed so that further study of a new route could be undertaken. Nevertheless, concerns over the route through Nebraska have now been resolved by state authorities.

Installed cross-border pipeline capacity to ship additional volumes of Canadian crude oil to the U.S. is now limited, and in any case, projected oil sands production growth will eventually overwhelm existing

transport capacity. The Keystone XL pipeline will add over 800,000 barrels/day of new capacity to move Canadian oil sands production to U.S. refineries. Given the high likelihood of continued growth in oil sands production, access to the US market will eventually require a substantial increase in pipeline export capacity. Without Keystone XL or alternative transportation capacity solutions, Canadian producers and government authorities may view full reliance on the U.S. market as too risky and seek alternative destinations.

One alternative is to build a pipeline to the Canadian west coast and ship the blended bitumen to the Far East. Assuming Canada manages to export crude to Asian markets, oil sands development will carry on unimpeded and the U.S. would import the same volume of crude oil and refined products as it would if the Keystone XL pipeline were not built. However, the benefits in U.S. crude oil transportation and processing (refining) efficiencies would be lost.

Although Canada would gain some risk-diversification by opening up sales to markets outside of the U.S., and may require additional export capacity in any case, on balance, further delays in permitting the Keystone XL pipeline would mean a lost opportunity for expanded trade between two stable and reliable allies in which long-term supply arrangements are assured. Such trade arrangements provide a strong foundation for deploying long-term cost saving capital projects, such as pipelines and refinery upgrades. A movement away from pipeline shipments will also bring about an increase in global tanker traffic and a somewhat higher risk for oil spills (shipping point to point in a pipeline is inherently less risky than tanker shipments). Diverting Canadian oil sands output to Asia would likely harm U.S. refining efficiency as the blended bitumen is well matched to the complex refineries on the Gulf coast which have invested billions of dollars in refinery upgrades. These refineries currently purchase around 2 mmb/d of heavy crude oil (similar in quality to Canadian blended bitumen from the oil sands) from Venezuela and Mexico and will continue to do so if projects are postponed or canceled to bring Canadian crude to the U.S. Gulf Coast. Rejecting the Keystone XL permit will not stop the U.S. from importing and using 2 mmb/d of heavy crude oil.

Critics of the Keystone XL pipeline have argued that U.S. consumers should use this opportunity to limit oil sands shipments to the U.S. and instead reduce domestic reliance upon petroleum use. This strategy fails to understand the fundamentals of U.S. petroleum use and supply disposition. The U.S. continues to import large volumes of petroleum and even after accounting for exports of petroleum products, net imports into the national economy remain over 7 mmb/d and forecasts by the Energy Information Administration (EIA) indicate that the U.S. will remain a large net importer of crude oil even under the most optimistic scenario of conservation and use of alternative fuels.

The benefits of the Keystone XL project extend beyond the direct cost savings from the improved transportation economics of shipping blended bitumen from Canada to the United States. U.S.-Canadian trade is a major component of economic activity in both countries. Canada's imports of U.S. goods support millions of U.S. jobs. Trade between the two countries reflects highly integrated ownership patterns and joint economic benefits not prevalent from other suppliers of crude oil to the US. In 2010, trade between the U.S. and Canada totaled \$525 billion and over twenty thousand jobs in the United States are directly dependent on current oil sands development alone.

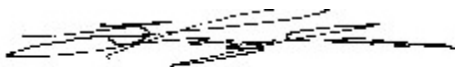
The new pipeline would ensure a stable supply of crude for at least the next 20 years, roughly the length of time to which buyers must commit to ship crude oil via Keystone XL. Given the expected growth in oil sands production, which is likely to rise by as much as 4 mmb/d over current levels, half of U.S. crude oil imports could be sourced from North America in the coming years. Much of the money spent on crude oil purchases from Canada would be reinvested in the United States and contribute to economic growth in both countries.

North America is in the early stages of sustained and large increases in domestic crude oil output from the same hydraulic fracturing technology that set off the shale gas revolution. New crude supplies, combined with the current surge in natural gas production, offer the promise of a renaissance in long-moribund petrochemical processing and petroleum refining industries. The capital now sitting on the sidelines is available and willing to fund profitable projects. However, it will not be deployed if political risk cannot be contained. The construction of the Keystone XL pipeline would send a clear signal to Canadian and U.S. producers that a critical piece of the North American petroleum transportation infrastructure is underway. It would inform investors in Canada, the US, and abroad (including OPEC) that North America is putting into place a key building block for the emerging petroleum renaissance.

The Administration's denial or further postponement of a decision on whether to allow the project to proceed has consequences well beyond the more narrow concerns of increased construction costs and reduced efficiency in U.S. crude transportation and refining operations. It represents a failure to understand the important strategic nature of the U.S.-Canadian trade and security relationship. It undermines confidence that historic and predictable energy trade will be free of political concerns and burdensome regulations. A failure to proceed with approval is a strategic loss for the U.S.

The Administration's endless reviews of the Keystone XL project are not a technical miscalculation in weighing environmental risks versus economic benefits. The Keystone XL pipeline is an important piece of the essential infrastructure for moving higher volume shipments of both Canadian oil sands and North American crude oil to coastal refineries. Failure to approve the project would reflect placing politics above the national interest. If the project is not given permission to proceed, such a decision will also demonstrate a fundamental misunderstanding of the critical role petroleum will continue to play in both the American and Canadian national economies. The U.S. enjoys a highly beneficial strategic partnership with Canada, and petroleum trade is its strongest link. The consequences of harming that relationship will impose high costs on both American security (and the national economy) for years to come.

Sincerely,



Lucian Pugliaresi
President