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Testimony

before

U.S. House of Representatives Committee on Energy and Commerce

Subcommittee on Commerce, Manufacturing, and Trade

Keystone's Red Tape Anniversary: Five Years of Bureaucratic Delay and Economic Benefits Denied

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Submitted by:

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Chairman Terry, Ranking Member Schakowsky, and members of Subcommittee on Commerce, Manufacturing, and Trade, I want to thank you for this opportunity to testify on *Keystone's Red Tape Anniversary: Five Years of Bureaucratic Delay and Economic Benefits Denied*. This is a timely hearing and I welcome the opportunity to testify on this important matter.

I am president of the Energy Policy Research Foundation, a non-profit organization that has published extensive research on developments in U.S. and world energy markets since 1944. We have been called on 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. We have just completed a major assessment of the infrastructure requirements to support continued progress in the production gains from the North American petroleum renaissance. Our research concludes that Keystone XL remains a critical backbone to support building out the crude oil transportation network to deliver rising oil production from North America to major refining centers.

Over the last decade the national economy has grown at an average annual rate of less than 2 percent. We should view this anemic rate of growth as a crisis. While our rate of economic growth has its roots in a range of structural and financial setbacks within the economy, we are increasingly facing regulatory and government policies which are delaying or outright prohibiting a large number of high value-added investments from proceeding. Expanding and efficiently moving rising supplies of North American crude oil to domestic refining centers can provide a much needed boost to economic growth if we can overcome the substantial regulatory and political constraints which place these opportunities at risk. My testimony today will focus largely on the economic opportunity offered by proceeding with Keystone XL and the ongoing economic damage from the endless delays and uncertainty surrounding government approval of this important pipeline.

The North American petroleum renaissance is a remarkable achievement of technological innovation and risk taking. Continued improvements in drilling and production technology are providing access to unconventional oil formations in the United States and the lessons from the unconventional development are also enhancing our capability to extract higher volumes from conventional plays. Crude oil production has increased dramatically in Texas and North Dakota over

the past few years following the application of many of the technologies that brought about a massive turn around in U.S. natural gas production. Production of Canada's Athabasca oil sands is increasing steadily in large part because of advances in heavy oil production technology. Canada, which is experiencing little growth in petroleum consumption and has limited outlets for waterborne exports, is facing growing constraints for moving rising oil sands production into the U.S. market via pipeline (and to a lesser extent by rail).

Production from the U.S. and Canada has added over 3 million barrels per day (mbd) to global oil production since 2008 and excellent prospects for continued growth (Figure 1 & 2). These new supplies came online at the very time oil production centers in North Africa and the Middle East suffered setbacks from political turmoil and international sanctions curtailed Iranian crude oil exports. As a result, rising North American production has limited the growth in world oil prices. Oil prices remain high, but would likely be higher (and our economic growth would be lower) without the advances made in U.S. and Canadian oil production. The North American production surge has likely prevented oil prices from rising by \$20-\$40/bbl over the last two years. Recall that in 2008 when oil prices spiked to over \$140/bbl, the world market had no excess capacity. That is where we would be today without the increase in North American crude oil production and the modest economic growth we've experienced would have been wiped out without this added production. In addition, we should view the economic benefits of the petroleum renaissance through a North American lens (Figure 3). The U.S. and Canadian energy markets are highly integrated and U.S. payments for Canadian crude oil, a reliable and stable ally, are repatriated at over 90 cents on the dollar in purchases of U.S. consumer and capital goods.

Together, the U.S. and Canada are producing nearly 11 million barrels of oil each day and these trends are likely to continue if we can efficiently move these new supplies to coastal refining centers. This dramatic rise in U.S. and Canadian production presents a range of logistical challenges. Historically, large volumes of domestic oil production were sourced from onshore and offshore petroleum provinces in the Gulf of Mexico region (Texas and Louisiana). Since the 1950s, the U.S. petroleum complex has been constructed around a network in which most, but not all, major refining centers were located on the coasts. The petroleum transportation network evolved into an integrated

system which moved large volumes of crude oil and petroleum product into the mid-continent and northern tier from the Gulf States. Refineries on the east and west coasts relied heavily on foreign crude oil imports (additionally supplemented by imports of refined products and Alaskan crude shipments to California). As U.S. field production declined, the states along the Gulf of Mexico became a major hub for moving larger volumes of waterborne petroleum imports (crude oil as well as petroleum products) into the mid-continent and northern tier of North America. The transportation network for crude oil (as well as petroleum products) was largely a system which moved supplies from the south to the north.

The recent surge in crude oil production from Canada and North Dakota combined with rapidly rising output from the Eagle Ford and Permian Basin plays in Texas (and now southeast New Mexico) are placing considerable stress on the North American crude oil transportation network (Figure 4). An expansion of our crude transportation network is required to move crude oil from Canada and North Dakota to processing centers not just on the Gulf Coast, but also to the East and West Coasts. The turnaround in North American crude oil production has been so extensive that all refineries in the mid-continent (central U.S. and Canada) have backed out nearly all non-Canadian imports and are processing only U.S. and Canadian crude (Figure 4).

The crude oil transportation network is responding to the emergence of new oil production primarily through expanded rail connections, pipeline construction and reversals (when approvals can be obtained), and extensive barge traffic. Trucking is also playing an important role in moving crude to rail and pipeline terminals from the wellhead. Rail has emerged as an important near and potentially long-term transportation solution (for certain crude oils to certain markets, namely Bakken crude to the East and West Coasts).

So how should we view the economic damage from the endless delays in getting the \$5.3 billion northern leg of the Keystone XL pipeline approved (Figure 5). For starters, delays on moving forward with the project now mean that future U.S.-Canada cross border pipeline projects will take much longer to complete. The owner of the Keystone XL pipeline, TransCanada, purchased \$2 billion worth of steel pipe two years before the anticipated regulatory approval, never expecting the United States would turn

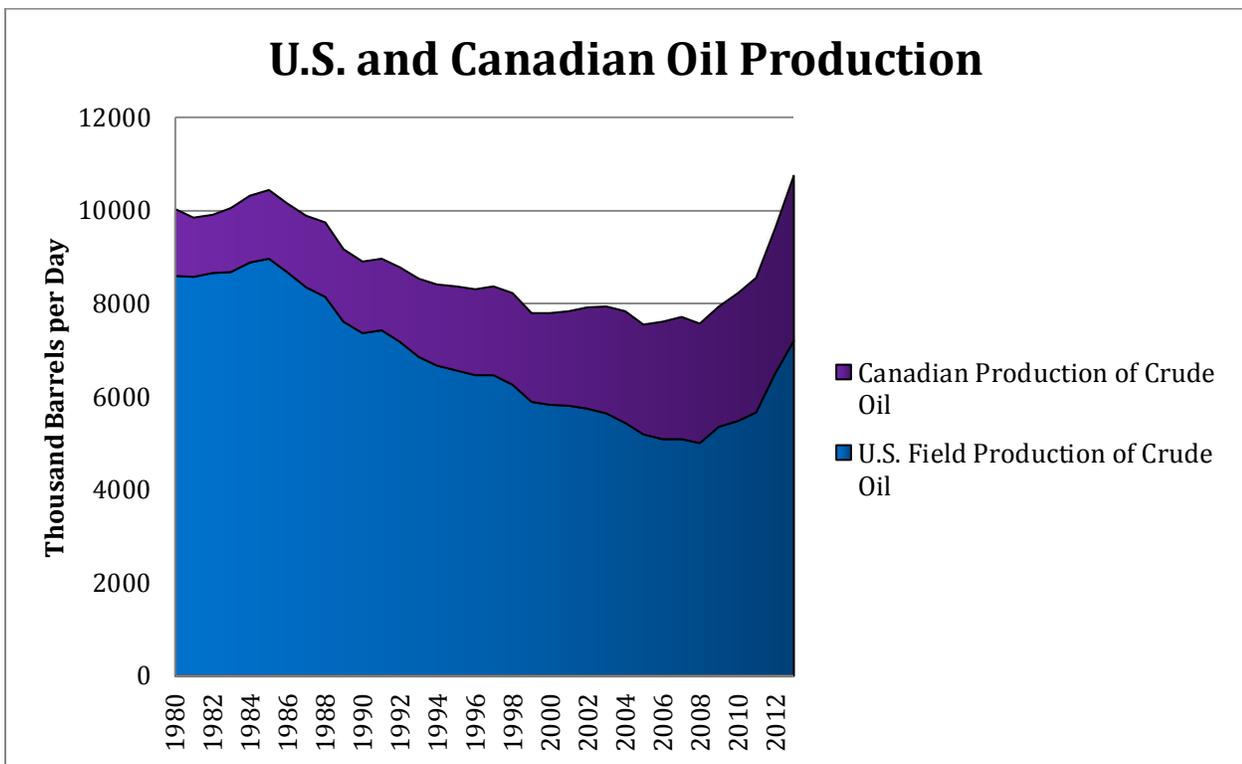
down a pipeline project when unrestricted volumes of Canadian oil sands are already permitted to cross the border when moved by either rail or truck. The President has also stated that the project would not be approved unless it could demonstrate that it would not result in any net additions to greenhouse-gas emissions (GHGs). Putting aside that the State Department's analysis of the project already concluded it would not add to GHG emissions, this requirement raises some obvious questions: Is the Administration planning to ban further shipments by rail and truck? Does the Administration have a plan to prevent the Canadian producers from selling oil in other markets around the world?

There are other economic consequences to the Administration's endless delays on Keystone XL. Few, if any, Canadian companies will propose new cross-border pipelines. No sane company will ever again preorder steel pipe with the expectation that the U.S. regulatory approval process will be both timely and reasonable. Even if other cross-border pipelines are proposed, future projects will await full regulatory approval before any pipeline company will order pipe or equipment, adding at least two years to construction time. While difficult to calculate, the consequences of such regulatory uncertainty are long-term and costly. If the Administration was really interested in job growth, they would put more effort in trying to contain the regulatory and political risks associated with their energy policies. In addition, the endless delays have also undermined the stability of U.S.-Canadian relations, a close ally and our largest trading partner.

We are now in the fifth year waiting for approval of this important infrastructure project. These delays come with significant costs to the national economy and our energy security. One of the hallmarks of an effective energy security strategy is proliferation of new crude oil supplies from secure and reliable producers, of which the U.S. and Canada should be placed on the top of the list. A decision to proceed with the pipeline would have sent a strong signal to investors in domestic crude oil projects and the world petroleum market (including OPEC) that North America is putting into place a long-term and sustained strategy for expanding domestic oil supplies. Approval would also have affirmed the close strategic and economic relationship the U.S. has with Canada. The advances in oil production in both the U.S. and Canada are of enormous economic and strategic value to both countries. We should embrace this petroleum renaissance with an approval process that is quick and attentive, not burdened by endless delays.

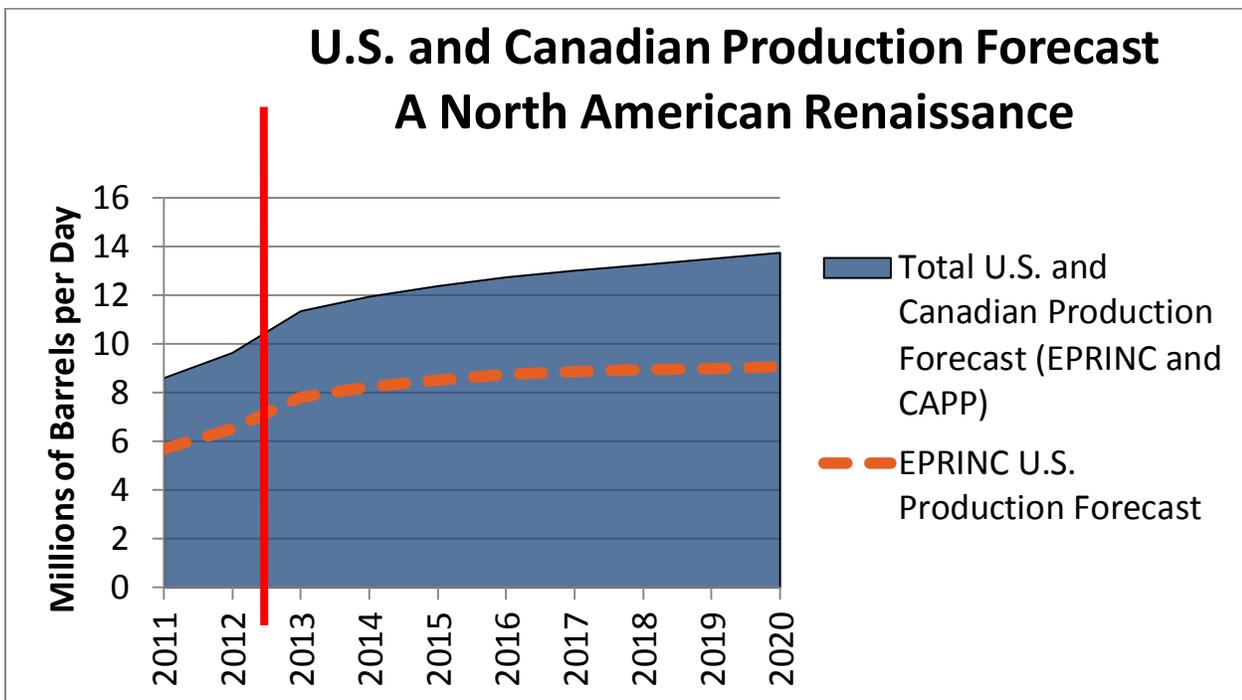
Appendix

Figure 1



Source: EIA

Figure 2



Source: EPRINC, CAPP

Note: Does not include NGLs

Figure 3

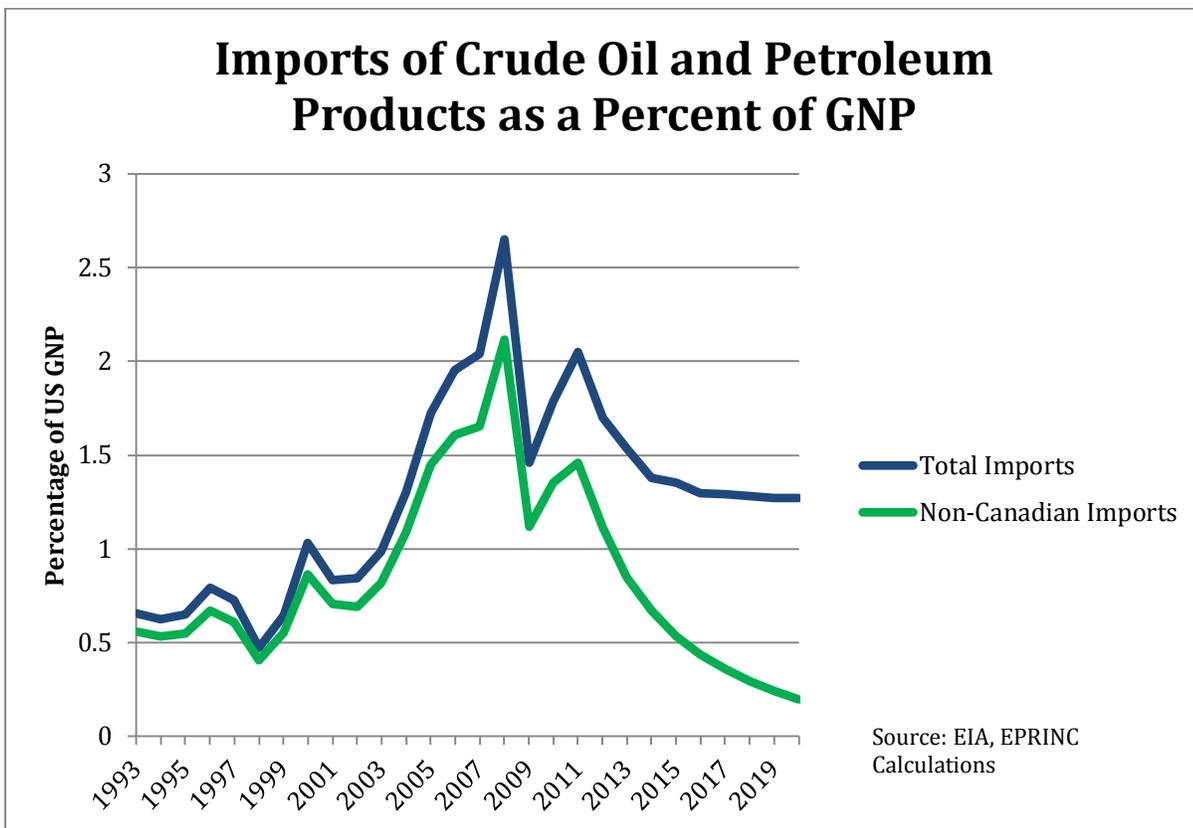
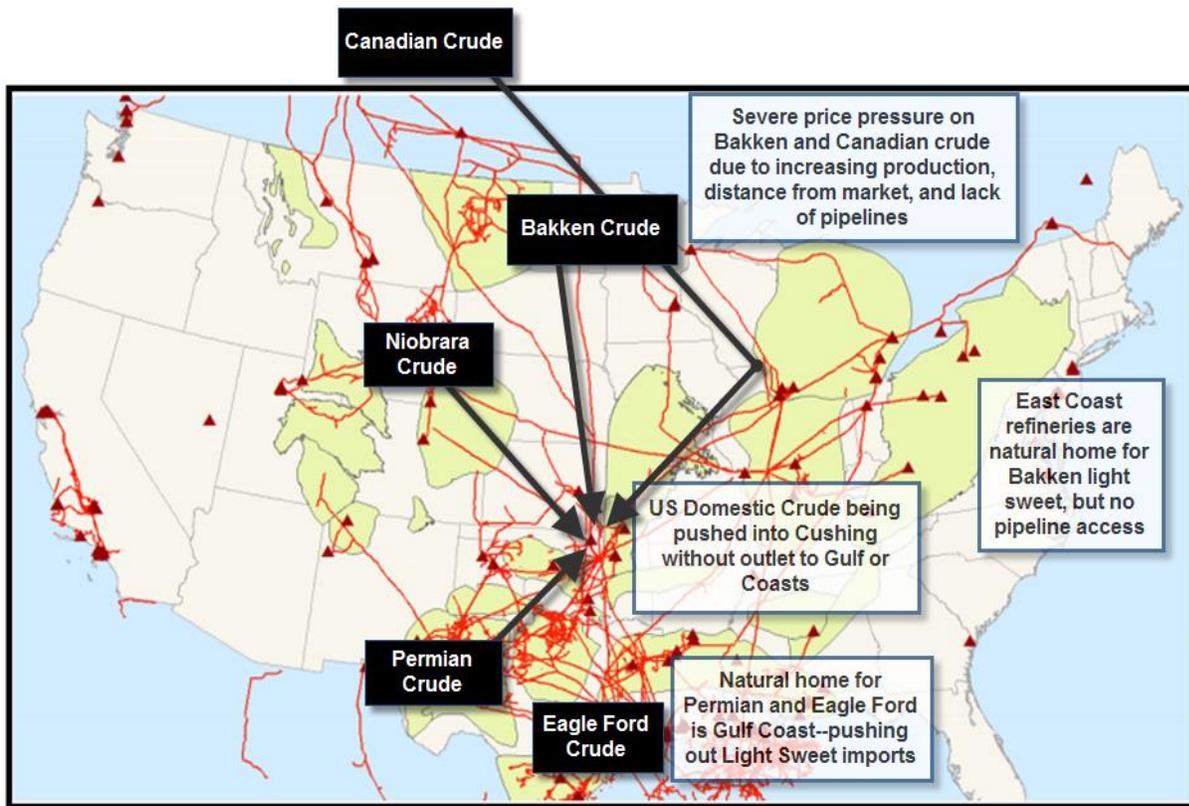


Figure 4

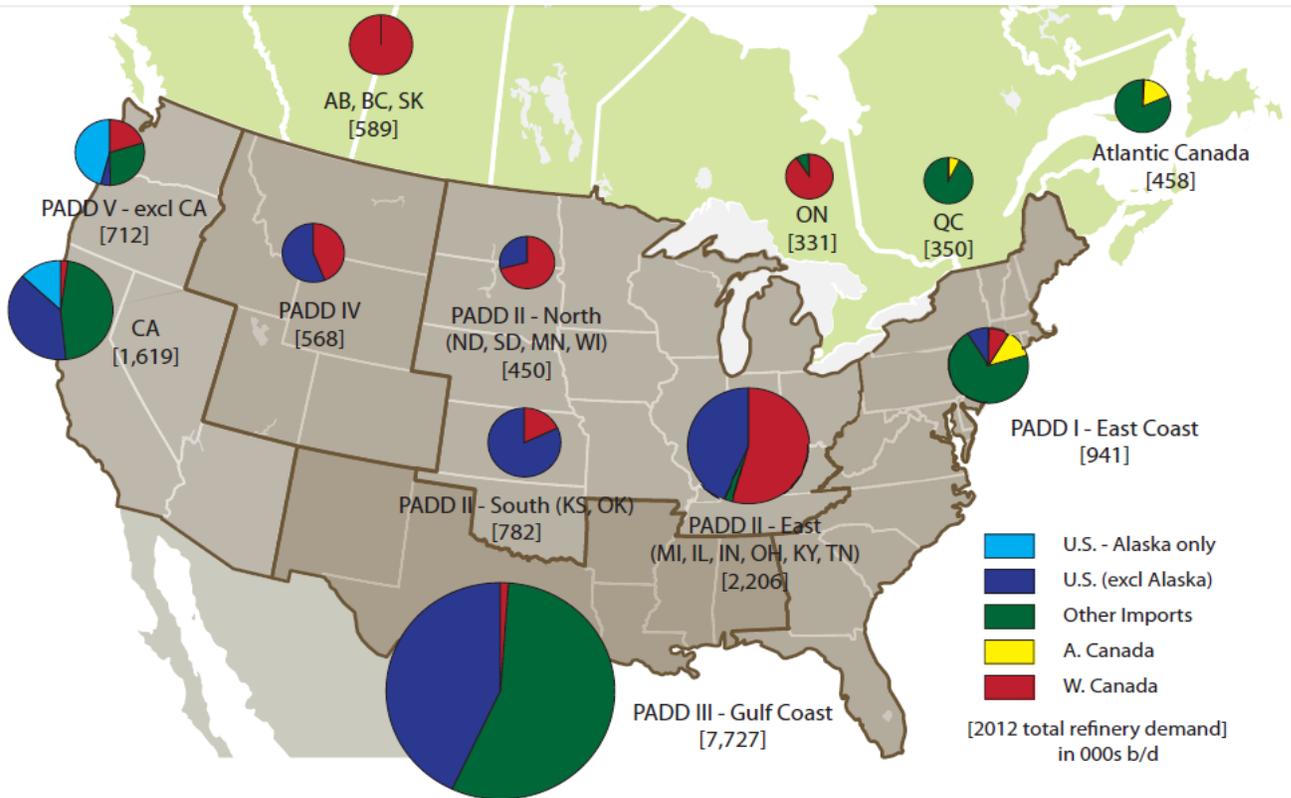
Choke Points in Moving Crude from the Northern Tier



Source: EPRINC

Figure 5

Rising Crude Supplies Must Move Long Distances



Sources: CAPP, CA Energy Commission, EIA, Statistics Canada

Figure 6

Keystone XL Northern Leg



Source: TransCanada