July 31, 2014

The Honorable John Kerry
Secretary of State
U.S. State Department
2201 C Street NW
Washington, DC 20520

Dear Secretary Kerry:

We welcome the State Department's openness to revising its analysis of the Keystone XL tar sands pipeline. However, we find it troubling that the Department chose to focus on a narrow and dubious correction to the risk estimate for crude by rail, while disregarding crucial and highly publicized developments with significant implications for the National Interest Determination Process. The evidence clearly shows that the pipeline fails President Obama's climate test and should not be built. Nevertheless, as the State Department considers corrections to analysis in the environmental review for Keystone XL, we request that you likewise assess new details that further confirm that the tar sands industry's expansion plan is contingent on pipeline construction, particularly Keystone XL.

The State Department's environmental review relied on several flawed assumptions that led it to underestimate Keystone XL's importance in enabling new tar sands expansion projects. That is why recent evidence showing that approval of Keystone XL *will* in fact drive tar sands development should be considered in the National Interest Determination process. Much of this information comes from the tar sands industry itself and demonstrates that rejecting Keystone XL will reduce the tar sands expansion and its associated carbon emissions.

- In June, the Canadian Association of Petroleum Producers (CAPP) lowered their projection of tar sands production in 2030 by 400,000 barrels per day, citing factors "including cost competitiveness and delays in project schedules."[1] CAPP recognized that the largest factor in the tar sands industry's ability to reach even this reduced production forecast is whether proposed pipelines come on in a rapid manner.[2]

- After the State Department released its environmental review in January, two major proposed tar sands mines that would have started production of 360,000 bpd of tar sands later this decade were canceled due to financial pressures caused in large part by pipeline capacity constraints and the uncertainty of proposed pipeline project developments, including Keystone XL.[3]

[1] Canadian Association of Petroleum Producers, Crude Oil: Forecast, Markets & Transportation (2014), available at http://www.capp.ca/getdoc.aspx?DocId=247759&DT=NTV.

[2] "The biggest uncertainty in this forecast is the timing associated with this [pipeline] capacity and whether or not they can deliver the capacity on the timelines they now propose," Greg Stringham, Vice President of Canadian Association of Petroleum Producers, June 9, 2014

[3] These projects include Shell's 200,000 bpd Jackine mine and Suncor and Total's 160,000 bpd Josyln mine. Jeff Lewis, Total SA suspends $11B Joslyn oil sands mine in Alberta, lays off up to 150 staff, Financial Post, May 29, 2014, at http://business.financialpost.com/2014/05/29/total-sa-suspends-11b-joslyn-oil-sands-mine-in-alberta-lays-off-up-to-150-staff/?__lsa=2f42-46f0.

- André Goffart, chief executive of Total E&P Canada Ltd – which has contracted for a portion of Keystone XL's capacity - said "Joslyn is facing the same challenge that most of the industry worldwide is in the sense that the costs are continuing to inflate when the oil price and specifically the netbacks from the oil sands are remaining stable at best."[4]

- CAPP's forecast also shows that rising capital costs and increasing natural gas prices are rendering in situ tar sands projects economically infeasible.[5] Due to these factors, CAPP lowered its 2030 forecast of in situ production by over 300,000 bpd.[6] This reflects a flaw the Keystone XL environmental impact statement's assumption that *in situ* tar sands production projects would be economically viable at oil prices above $65 per barrel.[7]

- Moving tar sands by rail is proving to be more expensive than the State Department's environmental review anticipated.[8] According to recent analysis by RBN Energy, shipping tar sands by rail from Alberta to the Gulf of Mexico "costs a minimum of $15/Bbl more than pipeline –resulting in lower netbacks for the producer versus pipelines."[9]

- The State Department's environmental review used terminal capacity as a proxy for actual crude by rail volumes.[10] However, a recent analysis of North American crude by rail market shows that actual volumes are less than a third of maximum rail terminal capacity, making it a poor indicator of crude by rail growth.[11]

- When discussing the tar sands industry's pared down 2014 expansion forecast, CAPP's Vice President Greg Stringham concluded, "The biggest uncertainty in this forecast is the timing associated with this [pipeline] capacity and whether or not they can deliver the capacity on the timelines they now propose."[12]

- Recent developments show that tar sands expansion projects are vulnerable at oil prices far above the $75 per barrel threshold assumed by the State Department's environmental review of Keystone XL. As Chief Energy Economist at ARC Financial Corp Peter Tertzakian observed

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[4] *Id*.
[5] John Spears, The Star, Oil Industry sees continued production increase, June 9, 2014, http://www.thestar.com/business/economy/2014/06/09/oil_industry_scales_back_longterm_forecast.html.
[6] Canadian Association of Petroleum Producers, 2014 Crude Oil Forecast, Markets and Transportation, June 9, 2014, pg. 7, http://www.capp.ca/forecast/Pages/default.aspx.
[7] State, FSEIS, Jan. 31, 2014, 1.4.36.
[8] State assumed that crude by rail from Alberta to the Gulf would cost between $0 to $8 more per barrel than by pipelines. State Department, Finale Supplemental Environmental Impact Statement, January 31, 2014, 1.4.136 (footnote 167).
[9] Sandy Felden, Go Your Own Way – The Road to Market for Canadian Bitumen Crude, RBN Energy, June 22, 2014, https://rbnenergy.com/go-your-own-waythe-road-to-market-for-canadian-bitumen-crude.
[10] Elana Schor, Greens fume at State's bet on oil sands as the new Bakken, E&E, Feb. 11, 2014, http://www.eenews.net/special_reports/pipeline_politics/stories/1059994362.
[11] Oil Change International, Runaway Train: The Reckless Expansion of Crude-by-rail in North America, May 2014, pg. 4, 9, http://priceofoil.org/content/uploads/2014/05/OCI_Runaway_Train_Single_reduce.pdf.
[12] Shawn McCarthy, Rising costs, transport woes threaten to slow oil boom, Globe and Mail, June 9, 2014, http://www.theglobeandmail.com/report-on-business/industry-news/energy-and-resources/canadian-oil-sands-production-forecast-lowered-slightly-for-2030/article19075059/.

regarding the growth obstacles facing the tar sands industry, “A barrel of oil priced at $110 (U.S.) in world markets sounds high, but paperwork filed by chief financial officers is not convincing shareholders that investing ten-plus billion dollars into far-flung oil fields is worth the growing risks.”[13]

- The International Energy Agency’s 2014 World Energy Investment Outlook Special Report referenced Canadian oil sands as an illustration of how “attempts at rapid development in the past have led to sharp cost inflation, pricing the projects out of the market”(p.88).[14] This week, Canadian Finance Minister Joe Oliver said that the inability to move oil to the coast is costing Canada C$30 billion a year.[15]

The evidence is clear, pipelines are essential to the planned expansion of the Canadian tar sands and the construction of the Keystone XL pipeline will stimulate the expansion of tar sands development. The expansion of this industry is at odds with the global need to move away from climate-disrupting fossil fuels and President Obama’s climate commitment. Investors and analysts understand the importance that Keystone XL plays and it is critical that the State Department consider this evidence in determining whether Keystone XL is in the national Interest.

Sincerely,

[13] Peter Tertzakian, The Globe and Mail, The message of the Joslyn oil sands shelving: Higher prices needed, June 2, 2014, http://www.theglobeandmail.com/report-on-business/industry-news/energy-and-resources/the-message-of-the-joslyn-oil-sands-shelving-higher-prices-needed/article18954820/.
[14] International Energy Agency, World Energy Investment Outlook Special Report (2014), available at http://www.iea.org/publications/freepublications/publication/WEIO2014.pdf.
[15] Christopher Donville and Andrew Mayeda, Rickford says pipelines need aboriginal, province support, Bloomberg Businessweek, June 9, 2014, at http://www.businessweek.com/news/2014-06-09/rickford-says-pipelines-need-aboriginal-province-support.

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