

Agrium, Unocal settle litigation over gas supplies to Nikiski fertilizer plant

New gas contract runs through end of October, after which plant will close if no new supplies found

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The Agrium-Unocal dispute over gas supplies to the Nikiski fertilizer plant has been settled.

Under a new gas sales agreement, Unocal will provide a total of 34 billion cubic feet to the plant through the end of October.

At that time, Agrium said in a Dec. 14 statement, the facility will close unless it can find alternate economic gas supplies.

Governor offers help to keep plant open

Petroleum News

Alaska Gov. Frank Murkowski said Dec. 14 that he is concerned about potential closure of the Agrium fertilizer plant and has offered state help in assessing natural gas supply options.

“We can’t afford to have that plant shut down,” the governor said in a statement. “It is a tough time of year for Agrium’s employees to learn this news. We’re committed to doing what we can to keep the plant operating — and we need the support of the community in those efforts.”

The governor initiated a teleconference with Kenai Peninsula community leaders after he learned from Agrium officials that an agreement reached between Unocal and Agrium in a long-standing dispute will provide a gas supply to the plant only through October 2005. The governor said Agrium indicated the

Unocal said in its Dec. 14 statement that it has reached a final settlement with Agrium of all claims arising from litigation regarding natural gas sales to Agrium's Nikiski fertilizer plant and the original sale of that plant to Agrium by Unocal, and under the settlement, all litigation between the companies will be dismissed with prejudice.

As part of the settlement, Unocal and Agrium have entered into a new gas sales agreement, effective Dec. 1, with defined monthly gas delivery obligations that terminate Oct. 31, 2005.

Under the settlement agreement, Unocal said it will pay Agrium \$25 million for early termination of the existing gas sales agreement, which originally ran until June 2009, full release of Unocal from all environmental claims, and resolution of all other issues, including certain contingent payment due Unocal under the 2000 purchase and sales agreement for the fertilizer plant. The settlement payment is in addition to remaining liquidated damages due under the existing sales agreement, and Unocal said it expects to take a \$15 million after-tax special-item charge to earnings in the fourth quarter 2004 as a result of the settlement.

Unocal: settlement provides clarity

"This settlement provides clarity and certainty to the two parties," Kevin Tabler, land and government relations manager for Unocal Alaska, told Petroleum News. "We are glad to see these issues resolved so that we can get back to the business of exploring for and producing oil and gas," Tabler said.

Agrium said the settlement "establishes a definitive gas supply obligation from Unocal to the Kenai facility" until Oct. 31, 2005, and said Unocal is obligated to

plant could be in jeopardy of closing in November 2005 if the company cannot secure future gas supplies.

The governor has proposed forming a working group of state officials, Agrium representatives and community representatives to assess alternatives and try to find ways to keep the plant open. The group is expected to begin work in early January. Staff from the governor's office, the Alaska Department of Natural Resources, the Alaska Department of Community and Economic Development and the Alaska Industrial Development and Export Authority will participate from the state.

Alternatives the governor expects the group to address include additional natural gas exploration including on the Kenai National Wildlife Refuge and the possibility of replacing natural gas generation with coal generation from the Healy Clean Coal facility.

The governor said he is concerned about the impact the closure of the Agrium plant would have on the Kenai Peninsula, especially Kenai and Soldotna. Agrium has 230 direct employees and 50 contractors working at the Kenai Peninsula facility.

supply a total of 34 billion cubic feet through Oct. 31, "on the same price basis as the current gas supply agreement."

Agrium said the new gas supply agreement will allow it to operate "at an average rate of 66 percent" through the end of October. "This rate could be further augmented with third party gas purchases during 2005," Agrium said.

Mike Wilson, president and CEO of Agrium, said in the company's statement: "The new gas supply agreement will enable us to continue to meet our ongoing customer requirements for nitrogen from Kenai for 2005, while we explore alternative gas supply agreements" beyond the end of October.

"While Agrium remains committed to working with local gas suppliers to develop alternatives, the facility will close in November of 2005 unless alternate economic gas supplies are obtained," he said.

Wilson told a Dec. 15 analysts' call that "it became clear to us that getting long-term gas from Unocal either through litigation or negotiation was not possible." The plant will be shut down Nov. 1, he said, if additional gas supplies cannot be found.

Agrium: not enough drilling

Richard Downey, investor/media relations with Agrium in Calgary, told Petroleum News Dec. 14 that Agrium believes "there's still a lot of gas in the region," but that "there just hasn't been enough drilling and enough finds" to replace the gas that has been produced. It "will take time and money to develop" additional Cook Inlet gas, he said.

Downey said Agrium hasn't totally given up hope, "but it does look likely the plant

will have to be closed” due to the “very tight gas supply” in the Cook Inlet basin. He noted that the new gas supply contract doesn’t specify a source for the gas Unocal will supply to the plant, just the volume, so the gas can come from whatever reserves Unocal has. This settles the litigation case in California, he said. Even if Agrium had gone ahead with that case, he said, “We wouldn’t have necessarily gotten any more gas.”

Ron Wilkinson, senior vice president, North America wholesale for Agrium, said on the conference call that Agrium has looked at moving the plant, but the company’s “analysis shows that given the age of the plant and cost of dismantling and shipping to another location,” the cost is very close to that of building a new plant, so it is unlikely that Agrium would move the plant.

Wilson said on the analysts’ call that Agrium would decide closer to October how to close the plant, “take it down hard or take it down in a mothball state.”

“Given what we know today, on the gas (supply), we would be closing that plant,” Wilson said. “As you get closer to the October timeframe, if we have new information we will consider mothballing it.”

Operation will mirror last winter

Lisa Parker, Agrium’s Nikiski spokeswoman, told Petroleum News: “This wasn’t an easy decision for Agrium. The employees here are top notch.” Parker said the Nikiski fertilizer plant has two ammonia trains and two urea trains, and when operating at capacity, she said, the plant uses 53 billion cubic feet a year.

The plan at this point is similar to the way we operated last year, Parker said: through

the winter months one ammonia train and one urea train will be operated. Then in the April-May timeframe the plant will ramp up, and run both sets of trains through September, “and then scale back down to one again.”

Cook Inlet gas supplies are very tight, and with the winter need for heat and light, that’s when the utility demand is highest, she said.

Gas options that Agrium sees

Chris Tworek, Agrium’s vice president supply management, said on the Dec. 15 analysts’ call that between now and the end of October, the period of the new gas supply contract with Unocal, Agrium thinks there is “a very good probability that, much like over the last couple of years ... we’ll be able to attract additional spot gas and run the plant at higher rates than the 66 percent that we’re going to get from the Unocal gas.”

But after Oct. 31, he said, “we do not believe there is any one supplier in the Cook Inlet that can supply us the gas that we need and so we are going to have to talk to several suppliers.” He said Agrium thinks that clearing up the situation with Unocal will make talking to other suppliers “a lot easier. And we think there’s still some probability that we could get enough gas after the 31st at least to run one train, or the overall operation at like 50 percent.”

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