

Chile Looks To LNG As Coal Projects Come Under Fire

By **Liz Hoffman**

Law360, New York (September 04, 2012, 8:21 PM ET) -- Chilean power producers Colbun SA and AES Gener SA on Monday selected a bidder to supply and operate a liquefied natural gas import terminal, part of a shift in the South American country toward cleaner-burning fuels after two big coal plants saw their environmental permits rejected.

Colbun and AES chose Norway's Hoegh LNG Holdings Ltd. to deliver a 500-million-cubic-foot-per-day floating LNG regasification vessel by 2014, a contract worth up to \$615 million over 15 years.

The announcement comes a week after Chile's highest court denied environmental permits to MPX Energia SA's \$4.5 billion Castilla coal-fired power plant. It was the latest legal setback for coal plants in Chile, which are coming under increasing judicial and regulatory scrutiny, and stoked concerns of an energy shortage in the country, where a boom in copper and other mining projects is taxing the power supply.

Experts say that tension — coupled with the promise of plentiful, cheap North American shale gas — could spur a return to gas-fired plants, which have dwindled in Chile since 2007, when a trade spat with neighboring Argentina cut off gas supplies.

“Given its power demands, Chile still needs new fossil-fuel generation, and nobody likes coal right now,” said Andres Mena, a Latin America-focused finance partner at Kirkland & Ellis LLP. “That opens doors for [LNG].”

Chile has huge power needs, especially as energy-intensive copper mines expand in the northern Atacama region. Over the next decade, Chile will need to nearly double its current power capacity to 30,000 megawatts to keep up with projected demand, according to the country's National Energy Strategy.

Much of that supply had been expected to come from coal plants. After Argentina defaulted on gas supply contracts in 2005 and 2006, Chile swung hard toward coal, launching plans for a dozen thermal plants around the country. Just last year, the government approved a massive coal mine in the country's south to power these new plants.

But the past 12 months have been a gut check for the industry. Groups like Greenpeace and Oceana have filed lawsuits and lobbied environmental regulators to deny permits, and indigenous communities have protested siting of new plants, claiming their rights are being infringed and their native lands polluted.

Germany's E.ON, Canadian miner Goldcorp Inc. and Chilean utilities like MPX and Endesa SA have had to defend coal projects in front of localities, national regulators and courts. At least four major projects have had to redo environmental assessments or now find themselves in legal limbo, awaiting an appeal of a regulatory or lower court ruling.

Just last week, the Chilean Supreme Court rejected permits for MPX's 2,100-megawatt Castilla plant, citing still-unresolved environmental concerns. In June, Chile's energy regulator rejected environmental permits for Endesa's \$1.4 billion Punta Alcalde coal project, which aims to fuel copper mines in the north.

"It used to be that administrative agencies rarely, if ever, second-guessed projects, and that courts rarely, if ever, second-guessed administrative agencies," Mena said. "That paradigm has shifted, and the last 12 to 18 months has clearly shown that. The level of scrutiny has been heightened at every step of the process."

Dino Barajas, an Akin Gump Strauss Hauer & Feld LLP partner, said he advises Chilean clients pursuing coal projects to "go above and beyond" the normal environmental impact statement process.

"Environmental considerations are probably going to end up becoming paramount, along with protection of indigenous rights," he said. "Those issues have drawn a lot of attention here, and [opponents] have shown that they really can hold up a project."

The two most recent rulings against MPX and Endesa, following legal challenges and regulatory delays at other planned coal generators, have contributed to a growing sense that coal is likely to be an uphill battle and stoked fears that the country could face a power shortage in the next few years.

But it has also opened the door to more LNG imports, and a spate of new deals show a possible shift in Chile's long-term energy mix.

Quintero LNG SA, which operates one of Chile's two existing LNG terminals, last week announced a \$30 million expansion to grow its regasification capacity by 50 percent.

In July, power producer GasAtacama SA awarded Golar LNG Ltd. a contract for the construction and operation of an offshore LNG import and regasification terminal and began negotiating long-term supply contracts with three U.S. shale gas producers.

In April, Spanish gas grid operator Enagas SA bought a 40 percent interest in Quintero in a deal worth \$352 million.

"We're seeing a lot of interest in the sector," Mena said. "It's less polluting, and new suppliers are emerging. If you manage to find the right site in Chile and avoid the [environmental] problems, you might accomplish a lot."

Barajas said the LNG flurry likely isn't directly tied to coal's recent struggles, simply because LNG plants take at least a year to plan. But the dual trends do illustrate the evolution of Chile's energy policy, which is trying to protect itself against a repeat of the Argentine gas shortage and keep the lights on at northern copper mines.

In addition to LNG imports, Chile is also pursuing gas deals with Brazil's Petrobras SA, approving new domestic coal mining, and recently adopted its first renewable energy requirement for utilities.

"We're starting to see the country try to have a longer-term energy policy that doesn't rely on Argentina," he said. "Chile is pursuing multiple fuel options, and making sure it has multiple sources for each of those fuels."

Colbun is represented by Mayer Brown LLP. Counsel information for AES was not immediately available.

--Additional reporting by Karlee Weinmann. Editing by Elizabeth Bowen and Lindsay Naylor.

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