MIDSTREAM Monitor

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FEATURES

Sabine Bankruptcy Ruling Reveals Midstream Sector's Achilles' Heel

By **JOSEPH MARKMAN**, Hart Energy

A judge's ruling in the Sabine Oil and Gas Corp. bankruptcy case, while unlikely to devastate the midstream industry as feared, nevertheless exposes the sector's near-term vulnerability in its contracts with struggling producers.

On March 8, U.S. Bankruptcy Judge Shelley Chapman of the Southern District of New York authorized Sabine to reject certain gathering and processing agreements with Nordheim Eagle Ford Gathering LLC and HPIP Gonzales Holdings LLC. Sabine had argued that it was no longer able to deliver minimum amounts of natural gas and condensate and was subject to deficiency payments that would cost the company $35 million. Drilling an uneconomic well to avoid payments could cost it between $2.5 million and $80 million.

"If an energy company does not have a conservative capital structure and access to liquidity, which is very important, then not only will they not survive, potentially, but more importantly they are going to miss some very interesting opportunities," Samaha said. "Today is an incredible investing opportunity but if you don't have the liquidity or the capital structure, you're not going to be able to take advantage of that."

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(*Continued from page 1*)

Mark Sherrill,
Sutherland Asbill & Brennan

Mark Sherrill, a Houston-based partner specializing in energy bankruptcy issues for the Sutherland Asbill & Brennan law firm, anticipated the ruling given comments made by the judge a month ago. But the decision still stunned many in the midstream who believed the sector could ride out this downcycle because contracts locked in cash flow, hydrocarbons or no hydrocarbons.

"I think that we shouldn't necessarily interpret this as a wide-reaching, universal ruling, either," Sherrill told Hart Energy. "The decision reached in the Sabine case is to some extent just based on the exact language that was in the contract and the way that gets treated under Texas law, so there could be different results if the same issue got litigated in different cases."

A number of other cases are being closely watched by the industry, with Sherrill expecting the tactic introduced by Sabine's counsel, Kirkland & Ellis LLP, to be repeated.

"It's already pretty far underway in one bankruptcy case, the Quicksilver Resources case, and just in the last week or so it was commenced in another bankruptcy case, which is the Magnum Hunter case," he said. "It's clearly, to some extent, given a green light to other producers to drive this as a tactic and even if they don't bring it fully before the court, it gives them a strong negotiating chip with the midstream companies, unfortunately."

It remains to be seen how those cases will be determined, Sherrill said, and rulings could vary based on the individual contract language and the state law that governs the agreement. Until then, it's unclear what midstream operators need to do to improve contractual language to avoid unfavorable rulings in the future. "It looks like we will be able to make those fixes," he said. "There's reason for some optimism going forward but it might be a very messy situation with regard to existing contracts."

"This ruling should give E&Ps significantly more leverage in these discussions, as the threat of filing and canceling these contracts is now likely more legitimate," wrote Kristina Kazarian of Deutsche Bank. "While this is not necessarily the first step a producer would want to take, it may appear to be a more viable option for those with significant midstream commitments that they see as onerous."

Tudor, Pickering, Holt & Co. noted that there were other midstream contracts held by Sabine that they did not attempt to reject. "These appear to be written with language that elevates them to a claim that 'runs with the land' status," the analysts wrote, adding a warning: "In the current environment, a midstream investment decision should assume some E&P counterparty risk, particularly as it relates to above-market fees and/or minimum volume commitments above current production levels."

What could be especially unsettling to many is the aggressive stance taken by an upstream producer against a midstream partner.

"Their statements in court suggest that they believe they have some alternatives, but certainly midstream companies will have some cause for concern," Sherrill said.

"I think under more normal market conditions you might not see quite as aggressive a move from the producers," he said, "but with the commodity markets as they are, I suspect that forced their hand a bit."

By **Frank Nieto,** Hart Energy
Interactive elements by **Joseph Markman**, Hart Energy

Editor's Note: The following is an excerpt of Midstream Business' latest Midstream Interactive article. The entire text, including interactive features such as video, audio and photo galleries can be found at MidstreamBusiness.com.

The Road South

It will take until the end of this decade for the Southeast market to begin to further grow. While it is switching to natural gas-fired power generation, the bulk of this capacity is contracted by Gulf Coast producers.
While pipeline capacity into the West and South is being built, both markets are already fully supplied and the production into those regions isn't going away anytime soon.

"Marcellus gas moving to the South could extend the geographic area of depressed gas prices because the existing producers from Texas, Oklahoma and Louisiana won't give up their gas markets," Dan Lippe, managing partner, Petral Consulting Co., told *Midstream Business*. This production has the advantage of flowing through older pipeline systems at lower tariffs compared to gas from the Appalachian Basin. Dominion's 564-mile Atlantic Coast Pipeline has allowed Marcellus supplies to make inroads into the Southeast market. Atlantic Coast, which is 96% contracted for its 1.5 billion cubic feet per day, passes through West Virginia, Virginia and North Carolina.

One of the unique aspects of this pipeline is that it was developed as a result of a request for proposal from end users rather than from producers. It is these end users, including Duke Energy, Dominion Virginia Power,

Piedmont Natural Gas, Public Service of North Carolina and Virginia Natural Gas that have contracted the system's capacity.

Market-Driven Pipeline

"What separates this project is that this is a market-driven project, as opposed to a producer-push project. The primary use for the supplies will be for power generation to meet growing market and environmental targets. The strategic location of this project also provides for future growth to these dynamic markets," said Don Raickes, senior vice president, Dominion Energy.

The Mariner East system is an important facet of Sunoco Logistics' plan to create a Northeast hub that will move up to 600,000 barrels per day of Marcellus and Utica NGL volumes to domestic and foreign markets. This schematic shows the layout of the system's key Marcus Hook Terminal. The project can be further expanded up to 800,000 bbl/d of shipping capability. Source: Sunoco Logistics Partners LP

The markets that the Atlantic Coast Pipeline will serve remain one of the largest demand growth centers in the U.S. On a long-term basis, the U.S. Census Bureau predicts a population increase of 2.1 million in North Carolina and 1.8 million in Virginia by 2025.

The Mariner East system is an important facet of Sunoco Logistics' plan to create a Northeast hub that will move up to 600,000 barrels per day of Marcellus and Utica NGL volumes to domestic and foreign markets. This schematic shows the layout of the system.

The U.S. Energy Information Administration reported that in the six-year period from 2008 to 2013, natural gas-fired power generation demand greatly increased in both states with North Carolina increasing by 459% and Virginia by 123%.

When you think of the Marcellus and Utica, one midstream player that is relatively quiet in the play is Enterprise Products Partners LP, but the company plays a very important role in the region nonetheless through its 1,230-mile Appalachia to Texas (ATEX) Pipeline.

This system went into service in 2014 and has been helping to solve the Appalachian Basin's ethane "problem" by providing transportation capacity for up to 190,000 barrels per day (bbl/d) of ethane out of the Marcellus and Utica from Washington County, Pa., to Mont Belvieu, Texas.

The benefit of moving this production to the Gulf Coast is because of the unsurpassed fractionation and cracking capacity at the Mont Belvieu, Texas, complex as well as the increasing export capacity offered from the Gulf Coast.

"We focus as much on the demand side of the equation as we do on the supply side," Bill Ordemann, executive vice president–commercial, Enterprise Products Partners, said at Hart Energy's Midstream Texas conference last October.

"We essentially became a problem solver ..."
John Hotz, Vice President, Corporate Strategy, NOVA Chemicals Corp.,
on markets for ethane and Canada, in particular, as an outlet.

To view this video and to read the entire article "Opening The Bottleneck," visit MidstreamBusiness.com

Viewpoints: Midstream Market In 2016

By **STRATAS ADVISORS**

Stratas Advisors midstream analyst Greg Haas says that crude oil supplies are expected to continue to grow in 2016. (*Source: Hart Energy*)

After adding roughly 100 million barrels of crude stocks in 2015, the high level of supply in the US continues to bubble over into 2016, according to Greg Haas, director of integrated oil and gas at Stratas Advisors.

The vast crude supply "has helped drive prices down because you've certainly have a lot more carrying cost for that inventory today than you did a year or two ago," Haas said recently at Hart Energy's breakfast series, Viewpoints.

"We import roughly 650,000 barrels a day of light crude. That light crude is the kind we have sitting in our storage tanks," Haas said. Compared to five-year averages, the US had roughly 130 million more barrels in commercial storage at year-end 2015, he added. "That's over 200 days' worth of imports sitting in storage. So that's an epic overhang."

With refineries at peak — 91-plus percent for the year — exports are the only other option aside from cutting drilling, which has already happened, according to Haas.

"We've come off of zero [exports] in the last couple of years. We're certainly exporting some light crude oil to Canada, which was always allowed. "We began exporting some processed condensate and crude to some new nations once that became possible through Enterprise Products, Pioneer and others," he said. "At year-end last year, we were given the gift of a new regulatory allowance for crude exports without even having to process it. So that will possibly help some going forward as long as it makes economic sense."

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Getting On Board For Exports

Crude oil and LNG exports are finally a reality for the domestic oil and gas industry, while product exports continue to grow. How will upstream producers and midstream operators need to change to serve these new markets?

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FRAC SPREAD

Frac Spread: What's Causing All This?

By **FRANK NIETO**, Hart Energy

A surprise comeback by crude oil also spurred gains for NGL prices and left questions over whether it was a signal of a recovery with a floor being set or another false dawn in this down market. In just over a week, West Texas Intermediate (WTI) crude gained nearly $10 per barrel (/bbl) in value to reach its highest level of 2016.

This caught many observers by surprise because it came after the U.S. Energy Information Administration (EIA) reported that crude stock levels had increased, including reaching 92% of capacity at the Cushing, Okla., hub.

NGL PRICES

Mont Belvieu	Eth	Pro	Norm	Iso	Pen+	NGL Bbl
March 2 - 8, '16	15.95	44.76	52.98	54.48	80.86	**$17.51**
Feb. 24 - March 1, '16	14.10	41.30	53.24	53.52	75.40	**$16.43**
Feb. 17 - 23, '16	14.51	38.08	54.48	54.20	69.24	**$15.77**
Feb. 10 - 16, '16	15.13	36.13	51.73	51.65	64.58	**$15.11**
February '16	14.83	37.42	53.83	53.80	69.04	**$15.68**
January '16	14.99	33.52	49.29	49.26	73.66	**$15.20**
4th Qtr '15	17.50	42.15	60.09	60.57	97.59	**$19.11**
3rd Qtr '15	18.26	40.99	54.16	55.19	100.10	**$18.80**
2nd Qtr '15	17.93	46.30	58.11	59.66	126.14	**$21.48**
1st Qtr '15	18.38	53.01	66.35	67.81	110.53	**$21.94**
March 4 - 10, '15	18.43	58.38	68.66	70.00	118.16	**$23.28**
Conway, Group 140	**Eth**	**Pro**	**Norm**	**Iso**	**Pen+**	**NGL Bbl**
March 2 - 8, '16	12.18	40.58	49.92	57.16	80.80	**$16.46**
Feb. 24 - March 1, '16	11.10	37.10	47.78	58.16	74.76	**$15.37**
Feb. 17 - 23, '16	12.90	33.88	48.36	59.80	70.10	**$15.04**
Feb. 10 - 16, '16	13.78	32.90	46.65	60.83	66.08	**$14.73**
February '16	13.09	33.72	48.44	60.06	69.16	**$15.00**
January '16	14.14	30.31	46.42	53.17	72.76	**$14.72**
4th Qtr '15	14.90	38.06	57.31	64.04	95.84	**$18.20**
3rd Qtr '15	15.47	36.28	48.59	54.34	99.10	**$17.59**
2nd Qtr '15	15.50	40.55	52.40	56.80	121.50	**$19.89**
1st Qtr '15	17.81	49.00	66.13	76.84	106.32	**$21.49**
March 4 - 10, '15	18.03	53.56	65.16	83.46	110.96	**$22.52**

"Just one month ago, analysts were claiming that if Cushing's working storage capacity reached 90%, WTI prices would have a good chance of breaking the $20 level. Instead the momentum for WTI is upward with no signs that a logistical bottleneck will occur at Cushing just yet. The market is looking way past record crude inventories and perceives that both domestic and international supply/demand fundamentals will improve," En*Vantage said in its March 10 *Weekly Energy Report*.

These positive fundamentals include increased gasoline demand, which has seen gasoline inventory decline by more than 8 million bbl. in the past month even as refinery run rates increased, which is supporting the theory that low crude prices are increasing gasoline demand. Additionally, OPEC production appears to be peaking with additional optimism over a production freeze agreement between some producers. Despite the positives, prices may not experience much more uplift.

"Weighing the pros and cons of the fundamentals, it does appear that crude oil prices are a bit overextended and that a

CURRENT FRAC SPREAD (CENTS/GAL)				
MARCH 11, 2016	**Conway**	**Change from Start of Week**	**Mont Belvieu**	**Last Week**
Ethane	12.18		15.95	
Shrink	9.88		10.81	
Margin	2.30	69.98%	5.14	25.79%
Propane	40.58		44.76	
Shrink	13.65		14.93	
Margin	26.93	13.95%	29.83	8.59%
Normal Butane	49.92		52.98	
Shrink	15.45		16.90	
Margin	34.47	5.94%	36.08	-4.00%
Isobutane	57.16		54.48	
Shrink	14.84		16.23	
Margin	42.32	-2.76%	38.25	-0.61%
Pentane+	80.80		80.86	
Shrink	16.52		18.08	
Margin	64.28	9.95%	62.78	7.04%
NGL $/Bbl	16.46	7.07%	17.51	6.58%
Shrink	5.44		5.95	
Margin	11.02	10.13%	11.55	5.88%
Gas ($/mmBtu)	1.49	1.36%	1.63	7.95%
Gross Bbl Margin (in cents/gal)	25.08	10.43%	26.75	6.12%
NGL Value in $/mmBtu (Basket Value)				
Ethane	0.67	9.73%	0.88	13.12%
Propane	1.41	9.38%	1.55	8.38%
Normal Butane	0.54	4.48%	0.57	-0.49%
Isobutane	0.36	-1.72%	0.34	1.79%
Pentane+	1.04	8.08%	1.04	7.24%
Total Barrel Value in $/mmbtu	4.02	7.35%	4.39	7.23%
Margin	2.53	11.23%	2.76	6.80%

Price, Shrink of 42-gal NGL barrel based on following: Ethane, 36.5%; Propane, 31.8%; Normal Butane, 11.2%; Isobutane, 6.2%; Pentane+, 14.3%, Fuel, frac, transport costs not included. Conway gas based on NGPL Midcontinent zone, Mont Belvieu based on Houston Ship Channel.

RESIN PRICES – MARKET UPDATE – MARCH 11, 2016					
TOTAL OFFERS: 19,618,268 lbs		SPOT		CONTRACT	
Resin	Total lbs	Low	High	Bid	Offer
PP Homopolymer - Inj	4,482,900	0.555	0.65	0.58	0.62
HDPE - Blow Mold	3,056,140	0.48	0.56	0.465	0.505
PP Copolymer - Inj	2,951,680	0.57	0.71	0.6	0.64
LDPE - Film	2,654,416	0.49	0.68	0.52	0.56
LLDPE - Film	2,466,508	0.49	0.6	0.49	0.53
LLDPE - Inj	1,731,128	0.48	0.61	0.52	0.56
LDPE - Inj	875,564	0.495	0.6	0.53	0.57
HDPE - Inj	662,920	0.52	0.62	0.48	0.52
HMWPE - Film	485,012	0.48	0.535	0.48	0.52
Scrap/Regrind/Repro	252,000	0.5	0.53		

Source: Plastics Exchange – www.theplasticsexchange.com

significant amount of short covering has been taking place. It is highly possible a $20 handle will not be seen again this year unless a distressed situation occurs at Cushing, but it is hard to see the upward momentum continuing past $40 until we see signs that U.S. crude inventories are declining and that will take another six weeks for that to occur," En*Vantage said.

Gains in the crude market helped C5+ prices reached their highest levels for the year as the Conway price rose 8% to 81 cents per gallon (/gal) and the Mont Belvieu price increased 7% to 81 cents/gal. Butane and isobutane prices were more muted due to refiners switching from winter-grade gasoline to summer-grade gasoline.

Light NGL prices continued to make solid gains at both hubs as propane inventories continue to decline and ethane prices are slightly decoupling from natural gas prices. This resulted in propane reaching its highest level for 2016 at both hubs while Mont Belvieu ethane did the same. Conway ethane remains challenged at its second lowest price of the year at 12 cents/gal even after a 10% from the previous week.

Overall the theoretical NGL bbl. price improved 7% at both hubs with the Mont Belvieu price reaching $17.51/bbl. with a 6% gain in margin to $11.55/bbl., and the Conway price improving to $16.46/bbl. with a 10% gain in margin to $11.02/bbl.
The most profitable NGL to make at both hubs was C5+ at 63 cents/gal at Mont Belvieu and 64 cents/gal at Conway. This was followed, in order, by isobutane at 38 cents/gal at Mont Belvieu and 42 cents/gal at Conway; butane at 36 cents/gal at Mont Belvieu and 35 cents/gal at Conway; propane at 30 cents/gal at Mont Belvieu and 27 cents/gal at Conway; and ethane at 5 cents/gal at Mont Belvieu and 2 cents/gal at Conway.

Natural gas storage levels fell by 57 billion cubic feet the week of March 4, the most recent EIA data available. This left inventory at 2.479 trillion cubic feet (Tcf) from 2.536 Tcf the previous week, which was 58% greater than the 1.568 Tcf level posted last year at the same time and 42% greater than the five-year average of 1.752 Tcf. While the heating demand season ends, cooling demand may start earlier than expected as the warm temperatures being experienced along the East Coast are expected to continue into next week according to the forecast from the National Weather Service.
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MORE TOP STORIES

Report: Oil May Have Bottomed As Non-OPEC Producers Cut Output

Brent crude was on track for its third weekly gain on March 11, supported by an optimistic report from the International Energy Agency (IEA) that said the market may have reached its bottom.

Still, analysts cautioned that a large glut of oil remained, with Goldman Sachs warning that U.S. crude could saturate storage in the coming months.

U.S. crude futures were trading at $38.64 a barrel at 7:08 a.m. CT (13:08 GMT), up 80 cents from their last close, having hit a 2016 high of $38.96 earlier in the day.

Brent crude futures were at $40.65 a barrel, up 60 cents, and on track for their third weekly gain in a row. Both contracts were trading more than 45% higher than the lows plumbed earlier this year.

The IEA said in a monthly report that oil might have bottomed and that low prices were beginning to impact crude output outside producer organisation OPEC.

"There are clear signs that market forces ... are working their magic and higher-cost producers are cutting output," the Paris-based IEA said.

The group, which coordinates energy policies of industrialised nations, said it believed non-OPEC output would fall by 750,000 barrels per day (bbl/d) in 2016 up from its previous estimate of 600,000 bbl/d.

It also said Iran's post-sanctions return to exporting was happening more gradually than expected, keeping its barrels from putting significant pressure on the market.

Still, Iran said this week it would not participate in any output freeze until it had regained market share. Industry sources also told Reuters on Friday that oil resumed pumping from Iraq's Kurdistan to the Turkish port of Ceyhan. The pipeline's closure in mid-February had taken some 600,000 bbl/d out of the market.

Earlier in the day, support also came from a global weakening of the U.S. dollar.

The greenback fell after easing measures announced by the European Central Bank. A weaker dollar supports oil prices as it makes dollar-traded oil cheaper for countries such as China, potentially spurring fuel demand. The IEA said it nevertheless saw global oil and product stocks rising heavily in the first half of 2016, in the range of 1.5-1.9 MMbbl/d, but that would slow to 0.2 MMbbl/d in the second half. The excess itself led some to warn that a premature price recovery could hamper market rebalancing.

"We reiterate our view that oil prices need to remain low for longer, as the oil and capital market rebalancing are only beginning," Goldman said in its report.

-REUTERS

Report: TransCanada Discusses Buying Columbia Pipeline Group

TransCanada Corp. is in talks to buy U.S. natural gas pipeline operator Columbia Pipeline Group Inc., the *Wall Street Journal* reported, citing people familiar with the matter.

The deal could be announced in coming weeks and could be valued at well over US$10 billion, the *Journal* reported.

Columbia Pipeline had a market value of about $8 billion as of March 9's close and long-term debt of $2.75 billion as of Dec. 31.

"TransCanada remains focused on opportunities that would be in line with our strategy and grow shareholder value," said spokesman James Millar, while declining to comment directly on the *Wall Street Journal* report. Columbia Pipeline declined to comment.

ETE Makes Private Share Offering To Fund Williams Deal

Energy Transfer Equity (ETE), which is in the process of buying rival pipeline company Williams Cos. Inc., said it carried out a private offering of convertible shares to some of its investors in order to help pay for the deal.

ETE said shareholders - including CEO Kelcy Warren - holding more than 329 million of the company's units elected to receive convertible units in exchange for agreeing to forgo some of their distributions for up to nine quarters.

The company said that it had originally intended to allow all of its unitholders to participate in the offering, but Williams wouldn't allow its accounting firm to consent to a public offering.

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