CHENIERE ENERGY INC
Form 10-Q
November 06, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2006

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from ______ to ______

Commission File No. 001-16383

CHENIERE ENERGY, INC.

(Exact name as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

95-4352386

(I.R.S. Employer Identification No.)

717 Texas Avenue, Suite 3100

Houston, Texas

(Address of principal executive offices)

77002

(Zip Code)

(713) 659-1361

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.   Yes x   No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer x   Accelerated filer ¨   Non-accelerated filer ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).   Yes ¨   No x

As of October 31, 2006, there were 55,143,564 shares of Cheniere Energy, Inc. Common Stock, $.003 par value, issued and outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements

CHENIERE ENERGY, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

(in thousands, except share data)

	September 30, 2006 (unaudited)	December 31, 2005 (as adjusted)
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 586,787	$ 692,592
Restricted cash and cash equivalents	139,623	160,885
Restricted certificate of deposit	694	676
Advances to EPC contractor	2,730	8,087
Accounts receivable	4,654	2,912
Derivative assets	9,194	5,468
Prepaid expenses	2,005	843
Total current assets	745,687	871,463
NON-CURRENT RESTRICTED CASH AND CASH EQUIVALENTS	100,098	16,500
PROPERTY, PLANT AND EQUIPMENT, NET	624,026	280,106
DEBT ISSUANCE COSTS, NET	47,401	43,008
INVESTMENT IN LIMITED PARTNERSHIP		
GOODWILL	76,844	76,844
LONG-TERM DERIVATIVE ASSETS		1,837
INTANGIBLE ASSETS	1,283	93
ADVANCES UNDER LONG-TERM CONTRACTS	11,762	
OTHER	5,001	296
Total assets	$ 1,612,102	$ 1,290,147
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 13,792	$ 778
Accrued liabilities	44,304	54,544
Current portion of long-term debt	6,000	6,000
Total current liabilities	64,096	61,322
LONG-TERM DEBT	1,264,500	917,500
DEFERRED REVENUE	41,000	41,000
LONG-TERM DERIVATIVE LIABILITIES	23,978	1,682
OTHER NON-CURRENT LIABILITIES	703	102
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS EQUITY		
Preferred stock, $.0001 par value, 5,000,000 shares authorized, none issued		
Common stock, $.003 par value		
Authorized: 120,000,000 shares at both September 30, 2006 and December 31, 2005		

Issued and outstanding: 55,109,038 shares at September 30, 2006 and 54,521,131 shares at December 31, 2005	166	164
Additional paid-in-capital	383,736	375,551
Deferred compensation		(9,684)
Accumulated deficit	(153,824)	(101,288)
Accumulated other comprehensive (loss) income	(12,253)	3,798
Total stockholders equity	217,825	268,541
Total liabilities and stockholders equity	$ 1,612,102	$ 1,290,147

The accompanying notes are an integral part of these financial statements.

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CHENIERE ENERGY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF OPERATIONS

(in thousands, except per share data)

(unaudited)

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005 (as adjusted)	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005 (as adjusted)
Revenues				
Oil and gas sales	$ 737	$ 729	$ 1,572	$ 2,154
Total revenues	737	729	1,572	2,154
Operating costs and expenses				
LNG receiving terminal and pipeline development expenses	2,923	4,127	6,730	14,902
Exploration costs	661	246	2,089	1,347
Oil and gas production costs	61	78	166	166
Impairment of fixed assets	1,628		1,628	
Depreciation, depletion and amortization	896	362	2,080	816
General and administrative expenses	12,044	6,523	37,669	17,114
Total operating costs and expenses	18,213	11,336	50,362	34,345
Loss from operations	(17,476)	(10,607)	(48,790)	(32,191)
Gain on sale of investment in unconsolidated affiliate		20,206		20,206
Equity in net loss of limited partnership		(2,261)		(3,232)
Derivative gain (loss)	(966)	931	(44)	264
Interest expense	(10,886)	(5,058)	(33,120)	(5,058)
Interest income	11,100	4,541	30,978	8,114
Other income	201	295	485	722
Income (loss) before income taxes and minority interest	(18,027)	8,047	(50,491)	(11,175)
Income tax provision	(15,079)		(2,045)	
Income (loss) before minority interest	(33,106)	8,047	(52,536)	(11,175)
Minority interest				97
Net income (loss)	$ (33,106)	$ 8,047	$ (52,536)	$ (11,078)
Net income (loss) per common share basic	$ (0.61)	$ 0.15	$ (0.97)	$ (0.21)
Net income (loss) per common share diluted	$ (0.61)	$ 0.14	$ (0.97)	$ (0.21)
Weighted average number of common shares outstanding				
Basic	54,496	53,938	54,361	53,358
Diluted	54,496	55,749	54,361	53,358

The accompanying notes are an integral part of these financial statements.

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CHENIERE ENERGY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY

(in thousands)

(unaudited)

	Common Stock		Treasury Stock						
	Shares	**Amount**	**Shares**	**Amount**	**Additional Paid-In Capital**	**Deferred Compen-sation**	**Accumulated Deficit**	**Accumulated Other Compre-hensive Income (loss)**	**Total Stockholders Equity**
Balance December 31, 2005 (as adjusted)	54,521	$ 164		$	$ 375,551	$ (9,684)	$ (101,288)	$ 3,798	$ 268,541
Issuances of stock	360	1			1,727				1,728
Issuances of restricted stock	252	1			(1)				
Reversal of deferred compensation					(9,684)	9,684			
Stock-based compensation					17,075				17,075
Purchase of treasury stock			(24)	(932)					(932)
Retirement of treasury stock	(24)		24	932	(932)				
Comprehensive loss:									
Interest rate swaps								(16,004)	(16,004)
Foreign currency translation								(47)	(47)
Net loss							(52,536)		(52,536)
Balance September 30, 2006	55,109	$ 166		$	$ 383,736	$	$ (153,824)	$ (12,253)	$ 217,825

The accompanying notes are an integral part of these financial statements.

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CHENIERE ENERGY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS

(in thousands)

(unaudited)

	Nine Months Ended September 30, 2006	2005 (as adjusted)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (52,536)	$ (11,078)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation, depletion and amortization	2,080	816
Impairment of unproved properties	416	583
Dry hole expense	894	
Impairment of fixed assets	1,628	
Amortization of debt issuance cost	2,752	
Non-cash compensation	15,975	2,487
Deferred tax provision	2,045	
Equity in net loss of limited partnership		3,232
Gain on sale of investment in unconsolidated affiliate		(20,206)
Non-cash derivative gain	(213)	(282)
Other	(257)	795
Changes in operating assets and liabilities		
Accounts receivable	831	(604)
Prepaid expenses	(380)	(473)
Deferred revenue		15,000
Regulatory assets	(12,343)	
Accounts payable and accrued liabilities	(1,673)	589
NET CASH USED IN OPERATING ACTIVITIES	(40,781)	(9,141)
CASH FLOWS FROM INVESTING ACTIVITIES:		
LNG terminal and pipeline construction-in-progress	(307,559)	(164,541)
Investment in restricted cash and cash equivalents	(62,336)	(203,452)
Advances under long-term contracts	(11,762)	
Purchases of fixed assets	(7,799)	(2,806)
Other	(6,652)	(713)
Oil and gas property additions, net of sales	(2,568)	(705)
Advance to EPC contractor	(2,729)	(16,173)
Investment in limited partnership		(1,592)
Proceeds from sale of investment in unconsolidated affiliate		20,206
NET CASH USED IN INVESTING ACTIVITIES	(401,405)	(369,776)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Debt issuance costs	(11,416)	(42,019)
Repayment of Term Loan	(4,500)	
Purchase of treasury shares	(931)	
Issuance of convertible senior unsecured notes		325,000

Proceeds from Term Loan		600,000
Purchase of issuer call spread		(75,703)
Other		47
Sale of common stock	1,728	2,095
Borrowing under Sabine Pass Credit Facility	351,500	
NET CASH PROVIDED BY FINANCING ACTIVITIES	336,381	809,420
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(105,805)	430,503
CASH AND CASH EQUIVALENTS BEGINNING OF PERIOD	692,592	308,443
CASH AND CASH EQUIVALENTS END OF PERIOD	$ 586,787	$ 738,946
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest (net of amounts capitalized)	$ 37,931	$ 3,238

The accompanying notes are an integral part of these financial statements.

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CHENIERE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 Basis of Presentation

The accompanying unaudited consolidated financial statements of Cheniere Energy, Inc. have been prepared in accordance with generally accepted accounting principles in the United States (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In our opinion, all adjustments, consisting only of normal recurring adjustments necessary for a fair presentation, have been included. As used herein, the terms Cheniere, we, our and us refer to Cheniere Energy, Inc. and its subsidiaries.

Certain reclassifications have been made to conform prior period amounts to the current period presentation. These reclassifications had no effect on net income (loss) or stockholders equity. As discussed below, we changed our method of accounting for investments in oil and gas properties from the full cost method to the successful efforts method of accounting, and as a result, the change in accounting method requires that all prior period financial statements be adjusted to reflect the results and balances that would have been reported had we been following the successful efforts method of accounting from inception.

Interim results are not necessarily indicative of results to be expected for the full fiscal year ending December 31, 2006. All references to issued and outstanding shares, weighted average shares, and per share amounts in the accompanying unaudited consolidated financial statements have been retroactively adjusted to reflect our two-for-one stock split that occurred on April 22, 2005.

For further information, refer to the consolidated financial statements and footnotes included in our annual report on Form 10-K for the year ended December 31, 2005.

New Accounting Pronouncements

In February 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 155, *Accounting for Certain Hybrid Financial Instruments An Amendment of FASB Statements No. 133 and 140.* SFAS No. 155 provides entities with relief from having to separately determine the fair value of an embedded derivative that would otherwise be required to be bifurcated from its host contract in accordance with SFAS No. 133. SFAS No. 155 allows an entity to make an irrevocable election to measure such a hybrid financial instrument at fair value in its entirety, with changes in fair value recognized in earnings. SFAS No. 155 is effective for all financial instruments acquired, issued or subject to a remeasurement event occurring after the beginning of an entity s first fiscal year that begins after September 15, 2006. We believe that the adoption of SFAS No. 155 will not have a material impact on our financial position, results of operations or cash flows.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets An Amendment to FASB Statement No. 140*. Once effective, SFAS No. 156 will require entities to recognize a servicing asset or liability each time they undertake an obligation to service a financial asset by entering into a servicing contract in certain situations. This statement also requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value and permits a choice of either the amortization or fair value measurement method for subsequent measurement. The effective date of this statement is for annual periods beginning after September 15, 2006, with earlier adoption permitted as of the beginning of an entity s fiscal year provided the entity has not issued any financial statements for that year. We do not plan to adopt SFAS No. 156 early, and we do not believe that it will have a material impact on our financial position, results of operations or cash flows.

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CHENIERE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

(Unaudited)

In July 2006, the FASB issued FASB Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109*. FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes.* It prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This new standard also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The provisions of FIN No. 48 are to be applied to all tax positions upon initial adoption of this standard. Only tax positions that meet the more-likely-than-not recognition threshold at the effective date may be recognized or continue to be recognized upon adoption of FIN No. 48. The cumulative effect of applying the provisions of FIN No. 48 should be reported as an adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) for that fiscal year. The provisions of FIN No. 48 are effective for fiscal years beginning after December 15, 2006. Earlier application is permitted as long as the enterprise has not yet issued financial statements, including interim financial statements, in the period of adoption. We believe that the adoption of FIN No. 48 will not have a material impact on our financial position, results of operations or cash flows.

In July 2006, the FASB issued FASB Staff Position (FSP) No. FAS 13-2, *Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction*. FSP No. FAS 13-2 requires that changes in the projected timing of income tax cash flows generated by a leveraged lease transaction be recognized as a gain or loss in the year in which change occurs. The pretax gain or loss is required to be included in the same line item in which the leveraged lease income is recognized, with the tax effect being included in the provision for income taxes. FSP No. FAS 13-2 is effective for fiscal years beginning after December 15, 2006. We believe that the adoption of FSP No. FAS 13-2 will not have a material impact on our financial position, results of operations or cash flows.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under the standard, fair value measurements would be separately disclosed by level within the fair value hierarchy. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years, with early adoption permitted. We are currently determining the effect, if any, the adoption of SFAS No. 157 will have on our financial statements.

In September 2006, the FASB issued SFAS No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plan an amendment of FASB Statement No. 87, 88, 106 and 132(R)*. SFAS No. 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and recognize changes in the funded status in the year in which the changes occur. SFAS No. 158 is effective for fiscal years ending after December 15, 2006. We believe that the adoption of SFAS No. 158 will not have a material impact on our financial position, results of operations or cash flows.

In September 2006, the FASB issued FSP No. AUG AIR-1, *Accounting for Planned Major Maintenance Activities*. FSP No. AUG AIR-1 prohibits the use of the accrue-in-advance method for accounting for major maintenance activities and confirms the acceptable methods of accounting for planned major maintenance activities. FSP No. AUG AIR-1 is effective the first fiscal year beginning after December 15, 2006. We believe that the adoption of FSP No. AUG AIR-1 will not have a material impact on our financial position, results of operations or cash flows.

CHENIERE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

(Unaudited)

Change in Method of Accounting for Investments in Oil and Gas Properties

Effective January 1, 2006, we converted from the full cost method to the successful efforts method of accounting for our investments in oil and gas properties. While our primary focus is the development of our liquefied natural gas (LNG) related businesses, we have continued to be involved, to a limited extent, in oil and gas exploration and development activities in the U.S. Gulf of Mexico. We believe that, in light of our current level of exploration and development activities, the successful efforts method of accounting provides a better matching of expenses to the period in which oil and gas production is realized. As a result, we believe that the change in accounting method at that time was appropriate. The change in accounting method constituted a Change in Accounting Principle, requiring that all prior period financial statements be adjusted to reflect the results and balances that would have been reported had we been following the successful efforts method of accounting from our inception. The cumulative effect of the change in accounting method as of December 31, 2004 and 2005 was to reduce the balance of our net investment in oil and gas properties and retained earnings at those dates by $18,237,000 and $17,977,000, respectively. The change in accounting method resulted in an increase in net income of $369,000 for the three months ended September 30, 2005 and a decrease in the net loss of $296,000 for the nine months ended September 30, 2005, and had no significant impact on earnings per share (basic and diluted) for these respective periods (see Note 15 Adjustment to Financial Statements Successful Efforts). The change in method of accounting had no impact on cash or working capital.

Successful Efforts Method of Accounting

We have elected to follow the successful efforts method of accounting for our oil and gas properties. Under this method, production costs, geological and geophysical costs (including the cost of seismic data), delay rentals, costs of unsuccessful exploratory wells, and internal costs directly related to our exploration and development activities are charged to expense as incurred. The costs of property acquisitions, successful exploratory wells, development costs, and support equipment and facilities are initially capitalized when incurred. In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, we review proved oil and gas properties and other long-lived assets for impairment when events and circumstances indicate a decline in the recoverability of the carrying value of such properties, such as a downward revision of the reserve estimates or commodity prices. We estimate the future cash flows expected in connection with the properties and compare such future cash flows to the carrying amount of the properties to determine if the carrying amount is recoverable. When the carrying amounts of the properties exceed their estimated undiscounted future cash flows, the carrying amount of the properties is written down to their estimated fair value. The factors used to determine fair value include, but are not limited to, estimates of proved reserves, future commodity prices, timing of future production, future capital expenditures and a risk-adjusted discount rate. Individually significant unproved properties are also periodically assessed for impairment of value, and a loss is recognized at the time of impairment by providing an impairment allowance. Depreciation, depletion and amortization of proved oil and gas properties is determined on a field-by-field basis using the unit-of-production method over the life of the remaining proved reserves.

Application of SFAS No. 71 to Regulated Operations

During the second quarter of 2006, we determined that certain of our natural gas pipelines to be constructed have met the criteria set forth in SFAS No. 71, *Accounting for the Effects of Certain Types of*

CHENIERE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

(Unaudited)

Regulation that would require us to capitalize certain costs that have previously been expensed. SFAS No. 71 requires rate-regulated subsidiaries to account for, and report, assets and liabilities consistent with the economic effect of the way in which regulators establish rates, if the rates established are designed to recover the costs of providing the regulated service and if the competitive environment makes it probable that such rates can be charged and collected.

Our application of SFAS No. 71 is based on the current regulatory environment, our current projected tariff rates, and our ability to collect those rates. Future regulatory developments and rate cases could impact this accounting. Although discounting of our maximum tariff rates may occur, we believe the criteria set forth in SFAS No. 71, for its application, are met and the use of regulatory accounting under SFAS No. 71 best reflects the results of future operations in the economic environment in which we will operate. Regulatory accounting requires us to record assets and liabilities that result from the rate-making process that would not be recorded under GAAP for non-regulated entities. We will continue to evaluate the application of regulatory accounting principles based on on-going changes in the regulatory and economic environment.

Capitalized Exploratory Well Costs

In April 2005, the FASB issued FSP No. FAS 19-1, *Accounting for Suspended Well Costs,* which amends FSP No. FAS 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies*. Under the provisions of FSP No. FAS 19-1, exploratory well costs continue to be capitalized after the completion of drilling when (i) the well has found a sufficient quantity of reserves to justify completion as a producing well and (ii) the enterprise is making sufficient progress assessing the reserves and the economic and operating viability of the project. If either condition is not met, or if an enterprise obtains information that raises substantial doubt about the economic or operational viability of the project, the exploratory well would be assumed to be impaired, and its costs, net of any salvage value, would be charged to expense. FSP No. FAS 19-1 provides several indicators that can assist an entity in demonstrating that sufficient progress is being made when assessing the reserves and economic viability of the project.

At September 30, 2006, our suspended well costs for wells on which drilling was completed more than one year ago were $164,000 relating to a single well. There were no suspended well costs charged to expense in the three and nine months ended September 30, 2006.

NOTE 2 Restricted Cash and Cash Equivalents

In August 2006, Cheniere Creole Trail Pipeline, L.P., our wholly-owned subsidiary (CCTP), entered into a purchase order with ILVA S.p.A (ILVA) for the purchase of pipe at an aggregate cost of approximately $175,700,000 (see Note 13 Commitments and Contingencies). Associated with this purchase order, CCTP delivered a standby letter of credit to ILVA in the amount of $87,852,000, to secure CCTP s obligations under the purchase order. This letter of credit required a deposit of $87,852,000 with the issuer of the letter of credit and has been recorded as non-current restricted cash and cash equivalents on our Consolidated Balance Sheet at September 30, 2006. Once the value of the goods and services paid by CCTP exceeds the value of the letter of credit, ILVA will submit a notice of reduction to the issuing bank to reduce the amount of the letter of credit by 100% of any subsequent payments by CCTP. The non-current restricted cash and cash equivalents cash collateral account on deposit with the issuing bank will be reduced by such amount.

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CHENIERE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

(Unaudited)

NOTE 3 Property, Plant and Equipment

Property, plant and equipment is comprised of LNG terminal and natural gas pipeline construction-in-progress expenditures, LNG site and related costs, investments in oil and gas properties, and fixed assets, as follows (in thousands):

	September 30, 2006	December 31, 2005 (as adjusted)
LNG TERMINAL COSTS		
LNG terminal construction-in-progress	$ 587,241	$ 271,142
LNG site and related costs, net	1,114	1,249
Total LNG terminal costs	588,355	272,391
NATURAL GAS PIPELINE COSTS		
Pipeline construction-in-progress	20,636	
Pipeline right-of-ways	1,623	
Total natural gas pipeline costs	22,259	
OIL AND GAS PROPERTIES, successful efforts method		
Proved	2,367	97
Unproved	777	1,600
Accumulated depreciation, depletion and amortization	(184)	(57)
Total oil and gas properties, net	2,960	1,640
FIXED ASSETS		
Computers and office equipment	4,863	3,611
Furniture and fixtures	1,310	1,145
Computer software	6,933	1,640
Leasehold improvements	2,278	1,757
Other	123	26
Accumulated depreciation	(5,055)	(2,104)
Total fixed assets, net	10,452	6,075
PROPERTY, PLANT AND EQUIPMENT, net	$ 624,026	$ 280,106

Our developing natural gas pipeline business is subject to the jurisdiction of the Federal Energy Regulatory Commission (FERC) in accordance with the Natural Gas Act of 1938 and the Natural Gas Policy Act of 1978, and we have determined that our pipelines to be constructed have met the criteria found in SFAS No. 71. Accordingly, we began applying the provisions of SFAS No. 71 to the affected pipeline subsidiaries in the second quarter of 2006.

Natural gas pipeline costs also include amounts capitalized as an Allowance for Funds Used During Construction (AFUDC). The rates used in the calculation of AFUDC are determined in accordance with guidelines established by the FERC. AFUDC represents the cost of debt and equity funds used to finance our natural gas pipeline additions during construction. AFUDC is capitalized as a part of the cost of our natural gas pipelines. Under regulatory rate practices, we generally are permitted to recover AFUDC, and a fair return thereon, through our rate base after our natural gas pipelines are placed in service.

In the third quarter of 2006, we impaired certain of our leasehold costs related to our current office space at 717 Texas Avenue in Houston, Texas. The impairment was the result of signing our new

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CHENIERE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS   Continued

(Unaudited)

office lease for space in the North Tower of Houston Pennzoil Place with Sunbelt Management Company (see Note 13   Commitments and Contingencies), and the belief that we would not recover or utilize our leasehold costs in the future. The impact of this impairment in property, plant and equipment was to increase accumulated depreciation by $1,628,000 and recognize an impairment of fixed assets by the same amount in our Consolidated Statement of Operations.

NOTE 4   Investment in Limited Partnership

We account for our 30% limited partnership investment in Freeport LNG Development, L.P. (Freeport LNG   ) using the equity method of accounting.

For the three and nine months ended September 30, 2005, our equity share of the net loss of the limited partnership was $2,261,000 and $3,232,000, respectively. Our recorded equity share of the Freeport LNG net loss for the three months ended September 30, 2005 includes $1,075,000 (2005 Suspended Loss   ) related to a portion of our 30% equity share of the second quarter 2005 net loss of the limited partnership. The 2005 Suspended Loss was not recognized as of June 2005 because our investment in Freeport LNG had been reduced to zero, and we did not intend to fund the 2005 Suspended Loss at that time; however, we received additional capital call notices during the third quarter of 2005, which we intended to fund in the fourth quarter of 2005. As a result, we recorded the 2005 Suspended Loss as part of our 30% equity share of the third quarter 2005 net loss of Freeport LNG.

For the three and nine months ended September 30, 2006, our equity share of the net losses of the limited partnership was $1,698,000 and $7,216,000, respectively. As of September 30, 2006, the basis of our investment in Freeport LNG was zero, and as a result, we did not record our share of the losses of the partnership for these periods because we did not guarantee any obligations and have not committed additional financial support to Freeport LNG at this time.

At September 30, 2006 and December 31, 2005, we had cumulative suspended losses of $11,184,000 and $3,968,000, respectively, related to our investment in Freeport LNG.

The financial position of Freeport LNG at September 30, 2006 and December 31, 2005, and the results of Freeport LNG   s operations for the three and nine months ended September 30, 2006 and 2005, are summarized as follows (in thousands):

	September 30, 2006	**December 31, 2005**
Current assets	$ 331,744	$ 380,615
Construction-in-progress	521,665	246,351
Fixed assets, net, and other assets	9,693	9,309
Total assets	$ 863,102	$ 636,275
Current liabilities	$ 60,252	$ 53,533
Notes payable	839,928	595,766
Deferred revenue and other deferred credits	5,748	5,748
Partners deficit	(42,826)	(18,772)
Total liabilities and partners deficit	$ 863,102	$ 636,275

CHENIERE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Continued

(Unaudited)

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Loss from continuing operations	$ (5,659)	$ (3,950)	$ (24,054)	$ (10,771)
Net loss	(5,659)	(3,950)	(24,054)	(10,771)
Cheniere s 30% equity in net loss from limited partnership (1)	$ (1,698)	$ (1,185)(2)	$ (7,216)	$ (3,232)

(1) As discussed above, we did not record the $1,698,000 and $7,216,000 losses in our Consolidated Statement of Operations for the three and nine months ended September 30, 2006 because our investment basis was zero.