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Avonmouth Liquefied Natural Gas facility C3 price review

National Grid LNG (NG LNG) owns the Avonmouth liquefied natural gas (LNG) storage facility which provides a combination of commercial and regulated services.

The Avonmouth LNG storage facility supplies operating margins (OM) services to National Grid Gas (NGG). It also supplies LNG by tanker to Scotia Gas Networks to serve the needs of the Scottish Independent Undertakings¹ (SIUs) and has in the past provided Constrained LNG². All of these services are provided at prices regulated through Special Licence Condition C3 (these prices are referred to as the "C3 prices" in the remainder of this letter) of NGG's gas transporter's licence.

The C3 prices were last reviewed in 2011³; and were retained for Partington and Avonmouth. Glenmavis developed operational problems during the previous price review and subsequently a C3 price was not set⁴. In June 2012, NG LNG issued a statement confirming the closure of Partington and Glenmavis LNG storage facilities⁵. This followed on from its LNG Storage Strategic Review in 2010 where NG LNG decided not to offer commercial storage services beyond 2011 at Partington and Glenmavis⁶.

Both NGG⁷ and SGN⁸ have stated in their business plan submissions for the RIIO gas transmission and distribution price controls that they wish to continue to use Avonmouth for part of the RIIO period. In light of NGG's and SGN's statements in their RIIO business plan submissions it is necessary to review the C3 prices and this letter sets out our initial thoughts on the review. The current C3 prices are due to expire on 30 April 2013. In order to have determined the applicable C3 prices for the next OM tender exercise, we need to commence the review process now.

¹ These constitute four towns in Scotland which are not on the main grids. They are supplied with LNG which is delivered by road tanker.

² Constrained LNG is a geographic service to support the National Transmission System (NTS) in the resolution of local constraints. NGG provide discounts to shippers prepared to book such LNG storage capacity.

³ 'National Grid LNG facilities price control - Final Proposals': Ofgem ref 18/11, 21 February 2011.

⁴ In December 2010, the Glenmavis facility developed a suspected leak in the cold box and had to suspend its liquefaction process. Whilst Glenmavis was able to fulfil its supply requirements to the end of the 2010/11 storage year, its capability for the future was subject to a number of uncertainties which could not be assessed at the last review.

⁵ NG LNG Facility Closure Announcement: <http://www.nationalgrid.com/NR/rdonlyres/655FE1E5-873B-40EA-9490-C4C65F53E996/54422/LNGSSiteClosuresPublicAnnouncement27June2012.pdf>

⁶ NG LNG Strategic Review Announcement: <http://www.nationalgrid.com/NR/rdonlyres/7402D054-2A01-469F-BF3C-DE5B56556F5D/41412/LNGStorageStrategicReviewFurtherAnnouncement.pdf>

⁷ NGG RIIO-T1 Business Plan: <http://www.talkingnetworkstx.com/gastransmissionplan/our-business-plan.aspx>

⁸ SGN RIIO-GD1 Business Plan:

http://www.sgn.co.uk/ScotiaGas/uploadedFiles/About_us/Stakeholder_info/Business_plan/SC_BusPlan_HI.pdf

Scope, form, and duration of review

Scope of review

The RIIO business plan submissions from both NGG and SGN have highlighted an ongoing requirement to access the Avonmouth LNG facility from 1 May 2013. In its RIIO business plan submission, NGG put forward a pipeline solution that would remove the need for Avonmouth LNG facility from October 2018⁹. We have commented on this in our RIIO Initial Proposals¹⁰. SGN stated in its RIIO business plan submission that, from April 2013, LNG would be needed as a 'top up' gas in the medium term as the SIUs will be using up to 75% of Compressed Natural Gas (CNG) as their fuel source.

NGG's LNG business is not subject to price control regulation in the same way as its NTS business and we do not intend to bring Avonmouth under the remit of the main RIIO-T1 price review. We propose to conduct a separate review of the funding required to contribute to Avonmouth's continued provision of the regulated services, until the alternatives for NGG and SGN are in place, and to determine what this means for the C3 price.

Form of review

The existing C3 price cap which will end in April 2013 was operated by comparing the expected costs and revenues for all services, and then adjusting the scale of charges for the regulated services so that the total costs and revenues balance. The regulated prices, defined by the "price cap"¹¹ methodology, set an upper limit on the prices that can be charged by regulated facilities and has been used for this service since it became regulated.

The basis of this decision, as distinct from adopting other forms of control, is that it keeps the volume and decommissioning risks and benefits with NG LNG, which is best placed to manage the associated risks and benefits.

Duration of review

The most recent review by Ofgem of all NG LNG's remaining LNG storage facilities was concluded in 2011. This review was to set C3 prices to last until April 2013, to take into account the Transmission Price Control Review 4 (TPCR4) Rollover¹². The Rollover extended the previous control by one year to allow for implementation of the new RIIO model. We had signalled in the LNG final proposals issued in February 2011 that we expected that a new control should be developed concurrent with the transmission price control.

Our initial thoughts are that the C3 prices determined by this review should be for the period until April 2018. At this point we will be in a better position to understand whether there are any ongoing requirements for regulated services at Avonmouth LNG facility.

Next steps

We expect to publish for consultation an initial proposals document in November 2012. We will be reviewing the historical and projected costs and revenues in order to form a view on the appropriate funding arrangements ahead of initial proposals. We plan to issue our conclusions on the applicable C3 prices in time for the next OM tender exercise in February 2013.

⁹ This may be dependent on obtaining relevant planning consents.

¹⁰ RIIO-T1: Initial Proposals for National Grid Electricity Transmission and National Grid Gas

<http://www.ofgem.gov.uk/Networks/Trans/PriceControls/RIIO-T1/ConRes/Documents1/RIIO%20T1%20NGGT%20and%20NGET%20Outputs%20and%20incentives.pdf>

¹¹ Although denoted as a price cap, this represents a minimum price for the services, as the licence allows NG LNG to charge the greater of the regulated price or the price it has been able to secure for commercial services.

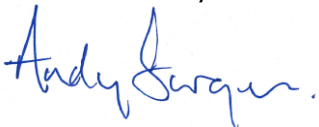
¹² http://www.ofgem.gov.uk/Networks/Trans/PriceControls/TPCR4Rollover/Documents1/TPCR4_Rollover_Final_Proposals.pdf

We would welcome any views on the approach we intend to adopt or issues we should address by **23 October 2012**.

Please submit responses by e-mail (to the email address below). Unless marked confidential, all responses will be published on Ofgem's website www.ofgem.gov.uk and placed in its library. Respondents who wish to have their responses remain confidential, should clearly mark the document/s to that effect and give the reasons for confidentiality.

If you have any comments or questions on this letter, please contact Natasha Ranatunga on +44 20 7901 7183 or Stathis Mokkalas on +44 20 7901 1876 or email: gas.transmissionresponse@ofgem.gov.uk in the first instance.

Yours faithfully

A handwritten signature in blue ink that reads "Andy Burgess".

Andy Burgess
Associate Partner, Transmission and Distribution Policy