

**Application by South Hook LNG Terminal  
Company Ltd (SHTCL) (owned by Qatar  
Petroleum and ExxonMobil) under section  
19C of the Gas Act 1986 for an exemption  
from section 19D of the Gas Act 1986**

**Ofgem final views**

November 2004

# Summary

The new Gas and Electricity Directives,<sup>1</sup> amongst other things, introduced a regulated third party access (RTPA) regime for interconnectors and Liquefied Natural Gas (LNG) import terminals. The Directives allow exemption from RTPA to be given by the relevant regulatory authorities, subject to veto by the European Commission. The Directives set down criteria that have to be met in order to justify such an exemption being granted.

On 22 September 2004, South Hook LNG Terminal Company Ltd (SHTCL), owned by Qatar Petroleum and ExxonMobil, wrote to Ofgem requesting an exemption under Section 19C(2) of the Gas Act 1986 from the application of Section 19D of the Gas Act 1986 to the entire proposed capacity of its LNG import facility at Milford Haven.

In its application, SHTCL argues that its application demonstrates that the South Hook LNG import facility satisfies the criteria set out in Section 19C of the Gas Act 1986 for an exemption from Section 19D.

On 13 October 2004, Ofgem issued a consultation<sup>2</sup> on SHTCL's formal application for an exemption under Section 19C(2) of the Gas Act 1986 from the application of Section 19D of the Gas Act 1986 in relation to all of the capacity of its proposed LNG import facility at Milford Haven. In summary, Ofgem's preliminary view was that at this stage the application had not materially changed from the draft application which Ofgem previously consulted upon.<sup>3</sup> Therefore, Ofgem maintained its previous view, outlined in the final views document<sup>4</sup> on Qatar Petroleum and ExxonMobil's draft application, that all the criteria for the granting of an exemption had been satisfied and that an exemption should be granted for the South Hook LNG import facility.

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<sup>1</sup> Directive 2003/55/EC of the European Parliament and of the Council concerning common rules for the internal market in electricity and repealing Directive 96/92/EC; and Directive 2003/54/EC of the European Parliament and of the Council concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC.

<sup>2</sup> *Consultation on an application by South Hook LNG Terminal Company Ltd (SHTCL) (owned by Qatar Petroleum and ExxonMobil) under section 19C of the Gas Act 1986 for an exemption from section 19D of the Gas Act 1986*, Ofgem, October 2004.

<sup>3</sup> *Qatar Petroleum and ExxonMobil Draft application for a Gas Directive exemption for a proposed LNG terminal at Milford Haven: Initial views*, Ofgem, December 2003.

<sup>4</sup> *'Qatar Petroleum and ExxonMobil, Draft Gas Directive Exemption Application for an LNG Terminal at Milford Haven, Final views'*, Ofgem, February 2004.

Ofgem has considered the responses received to the consultation on SHTCL's formal application in making a decision on whether to grant an exemption to SHTCL from the application of Section 19D of the Gas Act 1986 in respect of its proposed LNG import facility at Milford Haven. Ofgem remains of the view that all the exemption criteria are met and therefore the Authority has granted SHTCL an exemption in respect of the entire capacity of the proposed South Hook LNG import facility at Milford Haven under section 19C(5) of the Gas Act 1986 from the application of section 19D of the Gas Act 1986. This exemption order is set out in Appendix 1 of this document.

The European Commission has two months in which it can veto a decision by the relevant authority in a Member State to grant an exemption, or request that the regulatory authority amend its decision.<sup>5</sup>

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<sup>5</sup> This two month period may be extended by one additional month where additional information is sought by the Commission.

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# 1. Introduction

## Background

- 1.1. The new Gas and Electricity Directives, amongst other things, introduced an RTPA regime for interconnectors and LNG import terminals. The Directives allow exemption from RTPA by the relevant regulatory authorities, subject to veto by the European Commission. With respect to LNG import terminals, the new EU Gas Directive was transposed into GB law with the coming into force of the Gas (Third Party Access) Regulations 2004 on 26 August 2004. Ofgem therefore now has formal powers to grant exemption from the RTPA requirements for LNG import terminals, as set out in sections 19C and 19D of the Gas Act 1986.
- 1.2. The Directives set down criteria that have to be met in order to justify such an exemption being granted. The criteria contained in 19C(7) of the Gas Act 1986 relating to an exemption for an LNG import facility are:
  - (a) the facility or (as the case may be) the significant increase in its capacity will promote security of supply;
  - (b) the level of risk is such that the investment to construct the facility or (as the case may be) to modify the facility to provide for a significant increase in its capacity would not be or would not have been made without the exemption;
  - (c) the facility is or is to be owned by a person other than the gas transporter who operates or will operate the pipeline system connected or to be connected to the facility;
  - (d) charges will be levied on users of the facility or (as the case may) the increase in its capacity;

- (e) the exemption will not be detrimental to competition, the operation of an economically efficient gas market or the efficient functioning of the pipeline system connected or to be connected to the facility; and
- (f) the Commission of the European Communities is or will be content with the exemption.

1.3. It should be noted that it is against these exemption requirements that Ofgem will assess any application for exemption. Whilst there may appear to be some minor differences between the criteria in the Gas Act 1986 and those contained in the new Gas Directive, Ofgem does not consider that there are any material differences between the two sets of criteria.

### **DTI/Ofgem exemption policy**

1.4. In June 2003, the Department of Trade and Industry (DTI) and Ofgem issued a joint consultation document concerning new regulations to apply to LNG facilities and interconnectors.<sup>6</sup> This document set out the initial views of the DTI/Ofgem regarding the regulatory regime for interconnectors and LNG facilities. In addition to a quantitative competition analysis, DTI/Ofgem identified three areas that would be minimum requirements for an exempt regime:

- ◆ effective capacity allocation in terms of an initial offer of capacity to market (though under specific circumstances this condition might be loosened);
- ◆ effective mechanisms to ensure that capacity is not hoarded i.e. Use It or Lose It (UIOLI) arrangements; and
- ◆ information provision requirements relating both to the regulator and potentially also to market.

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<sup>6</sup> 'LNG facilities and interconnectors, EU legislation and regulatory regime, DTI/Ofgem initial views', DTI/Ofgem, June 2003.

1.5. In November 2003, the DTI and Ofgem issued final views in relation to the new Directives and the resulting regulatory regime.<sup>7</sup> By and large, the final views document confirmed, and clarified, the position set out in the initial views document. DTI and Ofgem expanded upon grounds for withdrawal of an exemption:

- ◆ breach of exemption criteria;
- ◆ breach of competition law;
- ◆ bankruptcy; or
- ◆ mergers / acquisition activity.

1.6. At the time, there were several potential projects that were moving to financial close prior to the Directives becoming transposed into GB law. Project developers requested early guidance as to whether they could expect their particular project to be exempt from RTPA. Ofgem said that while it would be prepared to give such guidance, any guidance would need to be informed by consultation on a case-by-case basis. Any such consultation would be on the basis of a draft application for exemption prepared by the relevant infrastructure developer. Ofgem indicated that while it would aim to ensure, as far as possible, that any potential guidance that was issued gave comfort as to the likely regulatory treatment of particular infrastructure, any such guidance issued would also be constrained to a significant extent by necessary legal caveats.

1.7. Ofgem received draft applications for exemption in respect of three projects. In each case, Ofgem consulted upon, and issued regulatory guidance to, each project. The first application was from Gastransport Services (GTS) for the proposed Balgzand Bacton pipeline project (BBL).<sup>8</sup> The second application

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<sup>7</sup> 'LNG facilities and interconnectors, EU legislation and regulatory regime, DTI/Ofgem final views,' DTI/Ofgem, November 2003.

<sup>8</sup> 'Gastransport Services, Draft application for an exemption for the Balgzand Bacton Pipeline project (BBL), Final views', Ofgem, December 2003.

was received from Qatar Petroleum and ExxonMobil for the proposed South Hook LNG import terminal at Milford Haven in Wales. The third application was received from Dragon LNG Ltd for the proposed LNG import terminal, also at Milford Haven.<sup>9</sup>

- 1.8. In each case, Ofgem expressed the view that the application for exemption would be likely to meet each of the exemption criteria set out in the relevant EU legislation. In these documents, Ofgem stated that once legislative authority was granted to Ofgem in respect of the ability to give exemptions to LNG facilities from the RTPA requirements, Ofgem would expect to undertake a formal consultation process in respect of formal applications it received for exemption.
- 1.9. In each case, Ofgem's views were submitted to the European Commission who indicated general support for Ofgem's position.

### **Formal application by South Hook LNG Terminal Company Ltd**

- 1.10. On 22 September 2004, SHTCL wrote to Ofgem formally requesting an exemption under Section 19C(2) of the Gas Act 1986 from the RTPA requirements set out in section 19D of the Gas Act 1986 to the entire proposed capacity of its LNG import facility at Milford Haven. The public version of SHTCL's application for exemption can be found on the Ofgem website.<sup>10</sup>

### **Ofgem's initial views**

- 1.11. On 13 October 2004, Ofgem issued a consultation paper on SHTCL's formal application for an exemption. Ofgem's initial view was that all the criteria for the granting of an exemption have been satisfied and that it would be appropriate to grant the exemption. Ofgem invited responses on Ofgem's

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<sup>9</sup> 'Dragon LNG Ltd, Draft application for an exemption for the Milford Haven LNG import terminal, Final views', Ofgem, June 2004.

<sup>10</sup> [www.ofgem.gov.uk](http://www.ofgem.gov.uk), under "Europe" area of work.



initial views and on the draft exemption order to be received by close of business 27 October 2004.

### **Respondents' views**

- 1.12. Ofgem received five responses to the consultation and these responses can be found in full on the Ofgem website. Of the respondents, four agreed with Ofgem's initial view that all the criteria for the granting of an exemption have been satisfied and that it would therefore be appropriate to grant the exemption. The remaining respondent did not comment on Ofgem's initial view. Respondents' views are discussed in Chapter 2.

### **Ofgem's final view**

- 1.13. Ofgem has considered respondents' views in making a decision on whether to grant an exemption to SHTCL from the application of Section 19D of the Gas Act 1986 for its proposed LNG import facility at Milford Haven. Ofgem considers that all the exemption criteria are met. Ofgem's final views are discussed in more detail in Chapter 2.
- 1.14. Ofgem has recently clarified the process by which an exemption decision should be notified to the European Commission. If Ofgem decides that the exemption criteria have been met then the Authority will grant the exemption. Ofgem will then submit the exemption decision to the European Commission for it to make its decision as to whether Ofgem's decision should be withdrawn or amended.
- 1.15. Since it is Ofgem's view that all the exemption criteria are met, the Authority has granted SHTCL an exemption under Section 19C(5) of the Gas Act 1986 from the application of Section 19D of the Gas Act 1986 to the entire proposed capacity of its LNG import facility at Milford Haven. This exemption order is set out in Appendix 1 of this document.

## **Way forward**

- 1.16. This final views document, together with the exemption order and all supporting documents will be submitted to the European Commission. The European Commission has two months in which it can veto a decision by the relevant authority in a Member State to grant an exemption, or request that the regulatory authority amend its decision.
- 1.17. If you wish to discuss any matters in this document, please contact Adam Higginson on 020 7901 7432.

## 2. Ofgem's decision

- 2.1. Ofgem's consultation on SHTCL's draft application set out the arguments presented by SHTCL as to why it considered that it met the various requirements of the Gas Directive. This document also set out why Ofgem was minded to exempt the South Hook LNG import facility from certain requirements of the Gas Directive.
- 2.2. In the consultation document on SHTCL's formal application, Ofgem's preliminary view was that the formal application has not materially changed from the draft application. Therefore, Ofgem maintained its previous view, outlined in the final views document on the draft application, that all the criteria for the granting of an exemption have been satisfied and that an exemption should be granted to the South Hook LNG import facility.
- 2.3. Ofgem received five responses to the consultation. This chapter provides a summary of respondents' views and provides Ofgem's final views on the formal application.

### ***Ofgem's analysis of whether the exemption conditions are met***

#### **(a) the facility or (as the case may be) the significant increase in its capacity will promote security of supply**

##### **Ofgem's view on draft application**

- 2.4. Ofgem considered that gas in a new location could be expected to enhance security of supply, as could the fact that this gas would be from a new source.

##### **Respondents' views**

- 2.5. No respondents commented on this condition.

### **Ofgem's final view on formal application**

2.6. Ofgem considers that this requirement has been met.

**(b) the level of risk is such that the investment to construct the facility or (as the case may be) to modify the facility to provide for a significant increase in its capacity would not be or would not have been made without the exemption**

### **Ofgem's view on draft application**

2.7. Ofgem considered that it was difficult to see how the risks associated with this project can be mitigated by anything other than some form of long-term contractual support. Ofgem concluded that the level of risk attached to the South Hook LNG import facility is likely to merit exemption and expected this requirement to be met.

### **Respondents' views**

2.8. No respondents commented on this condition.

### **Ofgem's final view on formal application**

2.9. Ofgem considers that this requirement has been met.

**(c) the facility is or is to be owned by a person other than the gas transporter who operates or will operate the pipeline system connected or to be connected to the facility**

### **Ofgem's view on draft application**

2.10. Ofgem explained that it was clear that the terminal would be fully separate from National Grid Transco. On that basis, Ofgem expected this criterion to be satisfied.

### **Respondents' views**

2.11. No respondents commented on this condition.

### **Ofgem's final view on formal application**

2.12. Ofgem considers that this requirement has been met.

### **(d) charges will be levied on users of the facility or (as the case may be) the increase in its capacity**

### **Ofgem's view on draft application**

2.13. Ofgem did not intend ex ante to set or approve the applicable tariff structure. However, Ofgem considered that tariffs for both third party and own use purposes should be published. Ofgem considered that this criterion is likely to be met.

### **Respondents' views**

2.14. One respondent welcomed the proposal for SHTCL to publish all charges.

### **Ofgem's final view on formal application**

2.15. Ofgem now considers that SHTCL should not be required to publish its tariffs. Public information disclosure requirements are discussed further below under the draft exemption order section. It should be noted that under the requirements of the exemption order SHTCL could be required to provide Ofgem with such information as tariffs. Therefore, Ofgem will have access to the necessary information to investigate any disputes raised by market participants over tariffs should such disputes arise.

2.16. As charges will be levied on all users of the facility, Ofgem considers that this criterion has been met.

**(e) the exemption will not be detrimental to competition, the operation of an economically efficient gas market or the efficient functioning of the pipeline system connected or to be connected to the facility**

**Ofgem's view on draft application**

- 2.17. Ofgem was of the view that in terms of upstream considerations, as a new entrant, the presence of Qatar Petroleum could be expected to enhance competition. This view also applied when considering the wholesale market as Qatar Petroleum would be a significant new entrant to the market when taking into account its 70 per cent ownership of the company selling gas out of the import terminal.
- 2.18. As for the downstream market, Ofgem noted that ExxonMobil is not at present a significant supplier of gas to customers in the downstream market and is not proposing to supply the Qatar Petroleum/ExxonMobil gas directly to customers. Ofgem considered that any effect on the downstream market, therefore, can be expected to be neutral.
- 2.19. Ofgem considered that an open season would have been a beneficial factor in support of this application. Ofgem committed to ensuring that effective anti-hoarding provisions are put in place.
- 2.20. Ofgem considered, on the basis of the competition analysis presented by Qatar Petroleum/ExxonMobil in its draft application and Ofgem's own competition assessment, that the project, when considered in isolation, is likely to meet this criterion. In particular, as the project would enhance the overall level of gas supply, this should increase competition to the benefit for customers, a benefit that would otherwise not have existed.
- 2.21. Ofgem considered that the connection of the South Hook terminal to the UK system would not be detrimental to the effective functioning of the internal gas market in the UK. Ofgem noted that NTS entry capacity will be booked consistent with entry capacity elsewhere on Transco's system and, to the extent that there are any technical implications arising from the connection,

for example, gas quality, Ofgem expected these to be resolved by Qatar Petroleum/ExxonMobil and Transco. As such, Ofgem considered that this exemption criterion is likely to be met.

### **Respondents' views**

- 2.22. One respondent was concerned that ExxonMobil would have 100 per cent of the supply capacity as well as 100 per cent of the physical supply contracts at the South Hook LNG import terminal and suggested that there may be competition issues that need addressing. Another respondent suggested that, in light of ExxonMobil's 25 per cent interest in Gasunie, ExxonMobil's position in the UK market would increase when it is receiving 100 per cent of the output from the South Hook LNG import terminal.
- 2.23. One respondent considered that it was unclear as to how SHTCL will create a secondary market for any unused capacity such that all capacity is made available to the market. This respondent suggested that since LNG shipments are dedicated supplies, as there is currently no liquid spot market for the product, it would seem reasonable to request a long-term secondary market for unused capacity and more detail on what type of contracts could be struck far in advance. This respondent considered that this would enable the market to respond to any extra unused capacity and contract the physical gas to supply through the LNG import facility.
- 2.24. One respondent noted that a third party is interested in participating in the Qatar Gas II project, a fact which was not brought to light in the draft application, and requested Ofgem's views on what material effect this might have on competition going forward.

### **Ofgem's final view on formal application**

- 2.25. Ofgem notes the concerns of a number of respondents as to the market share of ExxonMobil. As discussed previously in the preliminary views letter on SHTCL's informal application, if it is assumed that the wholesale market includes all sales and resales of gas, ExxonMobil's proportion of the

wholesale market is still not significant. Alternatively, taking a narrower assessment that the wholesale market is only physical, and treating ExxonMobil's purchase of the Qatar Gas II volumes as the relevant transaction, the addition of 100 per cent of the gas coming out of the South Hook terminal would result in an increase in ExxonMobil's share of the wholesale market but, in Ofgem's current view, not to a level that would be likely to be detrimental to competition. In any event, Ofgem's view is that the level of wholesale liquidity should lead towards the first scenario.

- 2.26. It has recently been announced that the activities of NV Nederlandse Gasunie ("Gasunie") are to be reorganised. As a result of the reorganisation, the transport company and the trading company of Gasunie will be legally fully dispersed. The State will takeover the interests of Shell and ExxonMobil (each currently has a 25 per cent interest) in the transport company of Gasunie and therefore will acquire the full interest in the transport company. The assets of the transport company will include Gasunie's shareholding in the new pipeline to be laid between the Netherlands and the United Kingdom, the Balgzand-Bacton pipeline. The ownership of the trading company, which includes Gasunie's interests in production, trade and supply, will remain the same i.e. the State, Shell and ExxonMobil. These changes are intended to take place as of 1 January 2005, with retrospective implementation completed by summer 2005.
- 2.27. As mentioned previously, it should be noted that Ofgem has not specifically approved the anti-hoarding measures that will be put in place by SHTCL. However, should the arrangements put in place by SHTCL result in primary capacity not being utilised, this could constitute grounds for reviewing the exemption, in particular on the grounds that the exemption from section 19D is operating in such a manner that is detrimental to competition or the operation of an economically efficient gas market. In Ofgem's view, at the very least SHTCL will need to demonstrate that there is a transparent mechanism that allows spare capacity to be made available to market. The ultimate objective is to ensure that capacity is not hoarded and that unused



capacity can be obtained in a transparent market-based manner by third parties so as to maximise the use of the LNG import terminal concerned.

- 2.28. Ofgem notes one respondent's request for Ofgem's views on how potential third party participation in the project might affect competition. As no such changes to participation have been finalised at this stage Ofgem does not consider it appropriate to discuss the potential impact of third party participation on competition. However, in the event that third party participation in the project is confirmed this could represent grounds for review of the exemption, in particular on the grounds that there is merger or acquisition activity in relation to, or by the facility owner.
- 2.29. Ofgem considers that the South Hook project should provide material benefits to upstream markets and that the project should have no material adverse effect on downstream competition. Ofgem considers that this project could be expected to have an overall positive impact on competition. Ofgem considers that this requirement has been met.

**(f) the Commission of the European Communities is or will be content with the exemption**

**Respondents' views**

- 2.30. No respondents commented on this condition.

**Ofgem's final view**

- 2.31. Ofgem notes that ExxonMobil is not at present a significant supplier of gas to customers in the downstream market. Ofgem considers that the South Hook project should provide material benefits to upstream markets and that the project should have no material adverse effect on downstream competition. Ofgem considers that this project could be expected to have an overall positive impact on competition. Ofgem therefore expects that the European Commission should be content with the exemption.

## ***The draft exemption order***

- 2.32. In Ofgem's consultation document a draft exemption order for the South Hook LNG import facility was included and Ofgem invited views from respondents on the draft exemption order.

### **Respondents' views**

- 2.33. In respect to the draft conditions for the provision of information, one respondent noted that the draft exemption order required the facility owner to make publicly available "such information as the Authority determines is reasonable". This respondent expressed concern that regulatory requirements should not prejudice individual companies' commercial positions through the public release of disaggregated or commercially confidential information. Another respondent considered that the principle of equivalence for making information publicly available should at least apply between facility operators (whether terminal processing, LNG, storage or interconnector) irrespective of whether regulatory powers are exercised by the DTI or the Authority.
- 2.34. One respondent suggested that the requirement in the draft exemption order to supply information to Transco might not automatically capture any change in ownership or operation of the relevant pipeline following the potential sale by National Grid Transco of gas distribution network businesses.
- 2.35. In respect of the drafting of the exemption order in relation to the grounds for revocation of an exemption, one respondent noted Ofgem's recognition that in the case where there was a material breach of the exemption criteria or a proven breach of competition law, revocation of an exemption would not be automatic and that it would be open to Ofgem to review the appropriateness of the exemption remaining in place. This respondent suggested, however, that this should be reflected in the wording of the exemption order. This respondent also suggested that the exemption order be amended to reflect that if Ofgem, prior to expiry of the minimum notice period for revocation

(four months), is content that action is being taken to remedy the breach, revocation would not occur.

- 2.36. One respondent was concerned that the grounds for revocation of an exemption order included the detrimental impact on competition caused by the direct behaviour of a throughputter. This respondent suggested that this may be appropriate for facilities developed by a vertically integrated organisation, which is able to exercise influence over the behaviour of the throughputter concerned, but that it is not appropriate for facilities developed by independent third parties that are unable to directly influence throughputter behaviour.
- 2.37. One respondent noted that the start date for 25 year exemptions for each phase is linked to the date of commercial operation. This respondent suggested that as there is no certainty on these dates, particularly for expansion capacity, the exemption order should include a "latest" date.

#### **Ofgem's view**

- 2.38. Having given respondents' views consideration in relation to information provision to the market, Ofgem considers that there should, where possible, be equivalence in the information required of LNG facility operators to that generally required of similar activities in relevant gas and electricity markets. Therefore, Ofgem has removed the condition from the draft exemption order which requires LNG import facility operators to make information publicly available. However, it should be noted that, in certain circumstances, Ofgem has statutory powers to publish or disclose information.
- 2.39. Ofgem notes that one respondent suggested that the requirement in the draft exemption order to supply information to Transco might not automatically capture any change in ownership or operation of the relevant pipeline following the potential sale of gas distribution network businesses. Ofgem agrees with this view and has updated the exemption order accordingly.

- 2.40. In respect of respondent's views on revocation, Ofgem considers that it is clear in the draft exemption order that, in the case that a material breach of the exemption criteria or a proven breach of competition law is established, revocation of an exemption would not follow automatically from such an event.
- 2.41. For the avoidance of doubt, in the event that any of the circumstances occur which may give rise to revocation of an exemption, Ofgem would not automatically commence the process to revoke the exemption by giving four month notice that the exemption order is to be revoked. First, Ofgem would likely enter into discussions with the party or parties involved to establish whether genuine grounds exist for the revocation of the exemption. Second, in the absence of a need to act urgently, should Ofgem determine that there are grounds for revocation, Ofgem would likely give the party or parties involved a reasonable opportunity to remedy the event or circumstances that have caused the grounds for revocation to arise. In the event that the party or parties involved have not remedied the event or circumstances which have caused the grounds for revocation to arise, Ofgem would consider whether formal action to revoke the exemption was required.
- 2.42. Ofgem notes one respondent's view that that it is not appropriate for the revocation of an exemption order as a result of a detrimental impact on competition caused by the direct behaviour of a throughputter. One of the criteria in considering an application by LNG import facility owners for exemption from RTPA is that the impact of the exemption will not be detrimental to competition. Ofgem considers that behaviour by throughputters at the LNG facility is a significant factor in terms of whether the LNG import facility meets these criteria. Therefore, Ofgem considers that it is appropriate that the exemption order may be revoked as a result of a detrimental impact on competition caused by the behaviour of a throughputter. The facility owner should be able to put in place contractual safeguards to minimise the risk that the operation of the exemption becomes prejudiced by the behaviour of throughputters of the facility.

2.43. Ofgem notes that one respondent considered that as there is no certainty in the start dates for the exemption, the exemption order should include a “latest” date. Ofgem considers that this is not necessary because a condition of the exemption is that the material provided by the facility owner to the Authority in respect of the exemption is accurate in all material respects. Therefore if the start date for the commercial operation of the first or second phase of the facility was significantly later than the start date suggested in the application this could constitute grounds for reviewing the exemption. Further, Ofgem would expect the facility owner to promptly inform it of any material change to its plans regarding the relevant start dates for the facility or indeed any other statement of intention (for instance, the commitment to put in place UIOLI arrangements).

#### **Withdrawal/amendment of an exemption by the European Commission**

2.44. As set out previously, Ofgem has recently clarified the process by which an exemption decision should be notified to the European Commission. To reflect this clarification, Ofgem has made amendments to the draft exemption order set out in Appendix 1 to this document as compared with the draft exemption orders that were initially consulted on as part of the formal application for exemption in respect of the South Hook LNG import facility and the Isle of Grain LNG import facility.<sup>11</sup>

2.45. To ensure consistency, Ofgem intends to reflect these amendments in any exemption orders that may be granted under section 19C, including the draft exemption order for the Isle of Grain LNG import facility.

#### **Transfer of an exemption**

2.46. Ofgem has made a further amendment to the draft exemption order set out in Appendix 1 to this document as compared with the draft exemption orders that were consulted on previously. This is to allow for the transfer of an

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<sup>11</sup> *Application by Grain LNG Ltd under section 19C of the Gas Act 1986 for an exemption from section 19D of the Gas Act 1986*, Ofgem, October 2004.

exemption to another facility owner and is dependent upon the written consent of the Authority. Again, Ofgem intends to reflect this amendment in any exemption orders that may be granted under section 19C.

## ***Conclusions***

- 2.47. Ofgem remains of the view that it would be appropriate to grant an exemption for the entire proposed capacity of the South Hook LNG import facility at Milford Haven (i.e. the initial capacity of 10.5bcm per year for a duration of 25 years and the expansion capacity of 10.5bcm per year for a duration of 25 years from when commercial operations commence) to SHTCL under Section 19C(5) of the Gas Act 1986 from the application of Section 19D of the Gas Act 1986.
- 2.48. For the avoidance of doubt, Ofgem's analysis has been carried out against the exemption criteria and is specific to the application for an exemption that Ofgem is considering. Any decision that Ofgem may make in relation to this application for an exemption does not preclude or impact in anyway on the operation of the Competition Act 1998 or the Enterprise Act 2002. Further, as the analysis contained in this document is in relation to a specific situation, the analysis may or may not necessarily be relevant to a consideration of any related issues that may arise, for example under the Gas Act 1986, the Competition Act 1998 or the Enterprise Act 2002.

### **3. Way forward**

- 3.1. This final views document, together with the exemption order and all supporting documents will be submitted to the European Commission.
- 3.2. As mentioned previously, the European Commission has two months in which it can veto a decision by the relevant authority in a Member State to grant an exemption, or request that the regulatory authority amend its decision.

# Appendix 1 Exemption order

## GAS ACT 1986

## SECTION 19C

## EXEMPTION

Pursuant to sub-section 19C(5) of the Gas Act 1986 (the Act), the Gas and Electricity Markets Authority hereby gives to South Hook LNG Terminal Company Ltd<sup>1</sup>, as the owner of an LNG import facility, an exemption from the application of section 19D of the Act in respect to the LNG import facility located at South Hook, Milford Haven Dale Road, Hubberston, Milford Haven, Pembrokeshire, SA73 1DR subject to the attached Schedule.



**Steve Smith**

Authorised in that behalf by the

Gas and Electricity Markets Authority

Dated 29 November 2004

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<sup>1</sup> Registered in England No. 4982132. Registered Office: 10 Upper Bank Street, London, E14 5JJ.



**SCHEDULE**

**PERIOD, CONDITIONS, AND REVOCATION OF EXEMPTION**

**A. Interpretation and Definitions**

In this exemption:

“the Authority”	means the Gas and Electricity Markets Authority established by section 1(1) of the Utilities Act 2000
“the Act”	means the Gas Act 1986 as amended from time to time
“the facility”	means LNG import facility
“facility owner”	means South Hook LNG Terminal Company Ltd in its capacity as owner of the facility
“facility operator”	means South Hook LNG Terminal Company Ltd in its capacity as operator of the facility
“throughputter”	means any user of the facility

**B. Full description of the LNG import facility to which this exemption relates**

The South Hook LNG import facility with:

- (a) an initial capacity of 10.5 billion cubic meters per year; and
- (b) an expanded capacity of 10.5 billion cubic meters per year.

### **C. Period**

Subject to section E below, and pursuant to section 19C(3)(a) of the Act, this exemption will cease to have effect:

- (a) in respect of the initial capacity of the facility, 25 years from the date that the facility commences commercial operation; and
- (b) in respect of the expansion capacity, 25 years from the date that the expansion capacity commences commercial operation.

### **D. Conditions**

Pursuant to sub-section 19C(3)(b) of the Act, this exemption is made subject to the following conditions:

1. That the material provided by the facility owner to the Authority in respect of this exemption is accurate in all material respects.
2. The facility owner notifies the Authority within ten days of:
  - (a) the initial capacity of the facility commencing commercial operation; and
  - (b) the expansion capacity commencing commercial operation.
3. The facility owner furnishes the Authority in such manner and at such times as the Authority may reasonably require, with such information as the Authority may reasonably require, or as may be necessary, for the purpose of:
  - (a) performing the functions assigned to it by or under the Act, the Utilities Act 2000, or the Energy Act 2004; or
  - (b) monitoring the operation of the exemption.
4. The facility owner complies with any direction given by the Authority (after the Authority has consulted the relevant gas transporter and, where relevant, the Health

and Safety Executive) to supply to the relevant gas transporter such information as may be specified or described in the direction -

- (a) at such times, in such form and such manner; and
- (b) in respect of such periods, as may be so specified or described.

Where the facility owner is prevented from complying with such a direction by a matter beyond its control, it shall not be treated as having contravened the condition specified in this paragraph.

In this condition:

“information”	means information relating to the operation of the pipe-line system which is operated by a relevant gas transporter
“relevant gas transporter”	means any holder of a gas transporter licence under section 7 of the Act owning a transportation system within Great Britain to which the facility is connected or with whom the facility operator interfaces with as a system operator

- 5. Should any of the grounds for revocation arise under section E of this exemption, the Authority may, with the consent of the facility owner, amend this exemption rather than revoke the exemption.
- 6. The Authority may, with the consent of the facility owner, amend this exemption where the Authority has been requested to amend the decision to grant this exemption by the European Commission (such request being made in accordance with Article 22(4) of Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003).
- 7. This exemption is transferable to another facility owner where the Authority has given its written consent to such a transfer. For the avoidance of doubt, all of the conditions contained in this exemption order continue unaffected in respect of any facility owner to whom this exemption order may be transferred.

## **E. Revocation**

Pursuant to sub-section 19C(4) of the Act, this exemption may be revoked in the following circumstances:

1. The Authority may revoke this exemption where the European Commission has requested (in accordance with Article 22(4) of Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003) that the Authority withdraw the decision to grant this exemption.
2. The Authority may revoke this exemption where the European Commission has requested (in accordance with Article 22(4) of Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003) the Authority amend the decision to grant this exemption and the facility owner does not agree (under paragraph D6 above) for this exemption to be amended in the manner so requested by the European Commission.
3. This exemption may be revoked by the Authority by giving a notice of revocation to the facility owner not less than four months before the coming into force of the revocation in any of the following circumstances:
  - (a) where:
    - i. in the Authority's reasonable opinion there is a material change in the degree to which the requirements of sub-sections 19C(7)(a), (c), (d) or (e) of the Act are met with respect to the facility as the result of an action or omission of the facility owner, facility operator, or throughputter;
    - ii. the facility owner has a receiver (which expression shall include an administrative receiver within the meaning of section 251 of the Insolvency Act 1986) of the whole or any material part of its assets or undertaking appointed;
    - iii. the facility owner has an administration order under section 8 of the Insolvency Act 1986 made in relation to it;

- iv. the facility owner is found to be in breach of the Competition Act 1998; or
  - v. there is merger or acquisition activity in relation to, or by the facility owner, that is detrimental to competition.
- (b) the facility owner has failed to comply with a request for information issued by the Authority under paragraph D3 above and the Authority has written to the facility owner stating that the request has not been complied with and giving the facility owner notice that if the request for information remains outstanding past the period specified in the notice, the exemption may be revoked; or
- (c) the facility owner has failed to comply with a direction issued by the Authority under paragraph D4 above and the Authority has written to the facility owner stating that the direction has not been complied with and giving the facility owner notice that if the direction remains outstanding past the period specified in the notice, the exemption may be revoked.