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To all interested Parties

24 March 2005

## **Consultation on an application by Scottish Power Energy Management Limited on behalf of Holford Gas Storage Limited for an exemption under section 19A(6)(a) of the Gas Act 1986 from section 19B of the Gas Act 1986**

### **Introduction**

This document provides details of an application made by Scottish Power Energy Management Limited (SPEML) on behalf of Holford Gas Storage Limited (HGSL) for an exemption under section 19A(6)(a) of the Gas Act 1986 (the Gas Act). This exemption is sought in respect of the negotiated third party access (TPA) requirements contained in section 19B of the Gas Act. The application relates to the proposed gas storage facility to be located in Byley, Cheshire. This document also provides Ofgem's initial views on the application and invites responses on these views.

### **Background**

As a result of the entry into force of the Second EU Gas Directive<sup>1</sup> there have been a number of important changes made to the legal and regulatory framework applying to gas storage facilities in Great Britain (GB). These changes were made through the Gas (Third Party Access) Regulations 2004 (the 2004 Regulations), which transposed, in part, the Second Gas Directive into GB law. The 2004 Regulations came into force on 26 August 2004. On 25 November 2004, Ofgem published a document<sup>2</sup> setting out a summary of the changes made to the Gas Act as a result of the 2004 Regulations and set out Ofgem's view of their impact on new and proposed gas storage facilities.

In summary, although the 2004 Regulations did not result in any material changes to the nature of the negotiated TPA requirements for gas storage, which are set out in section 19B of the Gas Act, a number of significant changes were made to section 19A of Gas Act, which allows for owners of storage facilities to be granted exemptions from these TPA requirements. In particular, for new storage facilities or for existing facilities which are, or are to be, modified to provide for a significant increase in capacity, section 19A of the Gas Act now provides two routes for exemption: the facility may be granted an exemption if either: use of the facility by

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<sup>1</sup> Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC.

<sup>2</sup> Ofgem, *The Second EU Gas Directive and storage regulation Great Britain*, November 2004. This document can be found under the 'Europe' area of work on Ofgem's website.

other persons is not necessary for the operation of an economically efficient gas market; or, if the six exemption requirements contained in section 19A(8) of the Gas Act are met<sup>3</sup>.

#### *The Byley gas storage facility*

The Byley storage facility will be owned and operated by HGSL, a wholly owned subsidiary of SPEML. The storage facility at Byley will be developed in two phases. The initial phase will consist of four caverns comprising 879GWh of useable space which will be commissioned by the end of 2007. The second phase will consist of a further four caverns and will add a further 879 GWh of useable space, which will be operational by the end of 2008. The total planned capacity is 1758GWh of useable space with 175GWh/day of deliverability and 88 GWh/day of injectability.

It should be noted that a TPA exemption has already been granted to SPEML in respect of the existing storage facility at Hatfield Moor, which has a capacity of 1260GWh (see the summary of existing and publicly known proposed storage facilities listed in Appendix 1).

On 4 March 2005, SPEML wrote to Ofgem under section 19A(2), on behalf of HGSL, applying for an exemption under section 19A(6)(a) of the Gas Act from the application of section 19B of the Gas Act for the planned Byley gas storage facility on the basis that the use of the facility by other persons is not necessary for the operation of an economically efficient gas market. SPEML's application can be found on Ofgem's website.

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

Based on the information available to Ofgem, the Byley gas storage facility with 1758 GWh space would constitute around four per cent of the overall market for existing (maximum) gas and LNG storage space in GB. If a different approach was taken to the definition of the storage space market – to the space provided by existing and likely future medium duration storage facilities<sup>4</sup> – the facility's estimated available storage space would represent around nine per cent of this market.

Based on the market definition provided by the Competition Commission<sup>5</sup> in relation to maximum daily flexibility (as distinct from storage space), the facility's estimated deliverability of

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<sup>3</sup> The six exemption requirements are contained in section 19A(8) of the Gas Act 1986 and are set out below:

- (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 be) 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.

<sup>4</sup> For the purpose of this calculation Hatfield Moor, Hornsea and Hole House are classified as existing medium duration storage facilities, and the Humbly Grove, Welton, Aldbrough and Byley storage facilities are classed as the likely future medium duration storage facilities (see Appendix 1). Ofgem considers that this interpretation is consistent with Table 4.5B of Transco's Transportation Ten Year Statement 2004 on the basis that 'likely future' storage facilities are those that have progressed beyond the 'conceptual' stage.

<sup>5</sup> Competition Commission, *Centrica plc and Dynegy Storage Ltd and Dynegy Onshore Processing UK Ltd*, August 2003, Table 5.9.

175GWh/day would constitute around four per cent of the overall existing market for flexibility in GB. If, again, a different approach was adopted to the definition of the flexibility market – to the flexibility provided by existing and likely future medium duration storage facilities – the facility’s estimated deliverability would represent around 17 per cent of this market.

It is Ofgem’s initial view that, on the basis of the size of the market share that the Byley gas storage facility would represent in the market for storage space and for flexibility (under both market definitions), and taking into account the fact that the facility would have a duration<sup>6</sup> of only ten days, the use of the facility by other persons is not necessary for the operation of an economically efficient gas market. Ofgem’s initial view is, therefore, that an exemption should be given to HGSL under section 19A(6)(a) of the Gas Act from the TPA requirements in section 19B of the Gas Act in respect of the whole of the capacity of the Byley gas storage facility.

It is Ofgem’s view that the test for the grant of an exemption under section 19A(6)(a) of the Gas Act is based on the “use of the facility” and, therefore, Ofgem considers that it is appropriate to consider Byley as a stand-alone facility in relation to the exemption test. That said, Ofgem considers that it is appropriate that the exemption test be carried out against the wider background of any other gas interests held or controlled by the person, or any related person, applying for an exemption in respect of a facility, particularly where the ownership or control of the facility for which the exemption is being sought may, in light of such other interests, give rise to concerns about actual or potential market foreclosure.

In arriving at its initial view, Ofgem has had regard to SPEML’s existing ownership of the storage facility at Hatfield Moor. Ofgem does not consider that, in the case of the Byley storage facility, Scottish Power’s interest in the Hatfield Moor storage facility would be likely to give rise to concerns about actual or potential market foreclosure.

For the avoidance of doubt, any views expressed, or decisions made, in respect of the giving of exemptions from section 19B are expressed or made solely in relation to the relevant criteria for the giving of exemptions set out in section 19A. Any decision that Ofgem may make, or view that Ofgem may express, in relation to this application for an exemption does not preclude or impact in any way 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.

### **Draft exemption order**

A draft exemption order for the Byley gas storage facility is set out in Appendix 2. The drafting of this exemption order is, where relevant, consistent with exemptions granted to other gas storage and LNG import terminal facilities since the 2004 regulations came into force.

### **Views invited**

This document presents Ofgem’s initial views on SPEML’s formal exemption application, lodged on behalf of HGSL. Ofgem would welcome views on the initial views contained in this

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<sup>6</sup> The ‘duration’ of a storage facility is the amount of time that the facility can deliver gas at maximum delivery until the level of gas in store equals zero.

document and the draft exemption order contained in Appendix 2 to be received by close of business 6 May 2005. All responses will normally be published on Ofgem's website and held in the Research and Information Centre. However, if respondents do not wish their response to be made public then they should clearly mark their response as not for publication. Ofgem prefers to receive responses in an electronic form so they can be placed easily on the Ofgem website.

Responses should be addressed to:  
Steve Smith  
Managing Director, Markets  
Office of Gas and Electricity Markets  
9 Millbank  
London  
SW1P 3GE

Electronic responses should be sent to [matthew.buffey@ofgem.gov.uk](mailto:matthew.buffey@ofgem.gov.uk) If you wish to discuss any aspect of this paper, Matthew Buffey (telephone 020 7901 7088) would be pleased to help.

### **Way forward**

Ofgem will consider responses received to this consultation in making its decision on whether to grant an exemption to HGSL under section 19A(6)(a) of the Gas Act from the TPA requirements in section 19B of the Gas Act to cover the whole of the capacity of the Byley gas storage facility. Ofgem will publish its decision in a final views document.

Yours sincerely

A handwritten signature in black ink, appearing to be 'Steve Smith', written in a cursive style.

Steve Smith  
**Managing Director, Markets**

## Appendix 1: Table 1 - Summary of existing and publicly known proposed storage facilities<sup>7</sup>

| Projected Start date                          | Storage facility                | Owner                                     | TPA status  | Space (GWh) | Deliverability (GWh/d) | Injectability (GWh/d)     |
|---|---------------------------------|---|---|-------------|------------------------|---------------------------|
| <i>Existing gas storage facilities</i>        |                                 |   |   |             |                        |                           |
| N/A   | Rough                           | Centrica Storage Limited                  | Required to provide Gas Act TPA. Also provided undertakings | 30300       | 455                    | 160                       |
| N/A   | Hatfield Moor                   | Scottish Power                            | Exempt  | 1260        | 25                     | 25                        |
| N/A   | Hornsea                         | Scottish and Southern Energy (SSE)        | Required to provide Gas Act TPA                             | 3495        | 195                    | 21.6                      |
| N/A   | Hole House                      | Energy Merchants Gas Storage (UK) Limited | Exempt  | 300         | 30                     | 60                        |
| <i>Existing LNG storage facilities</i>        |                                 |   |   |             |                        |                           |
| N/A   | Avonmouth                       | Transco LNG                               | Exempt  | 876         | 156                    | 2.3                       |
| N/A   | Partington                      | Transco LNG                               | Exempt  | 1121        | 219                    | 2.4                       |
| N/A   | Dynevor Arms                    | Transco LNG                               | Exempt  | 304         | 49                     | 2.6                       |
| N/A   | Glenmavis                       | Transco LNG                               | Exempt  | 505         | 101                    | 1.6                       |
| <i>Planned storage facilities</i>             |                                 |   |   |             |                        |                           |
| Q4 2005                                       | Humbly Grove                    | Star Energy                               | Exempt  | 3146        | 79                     | 90                        |
| First cavity Q3 2006<br>Second cavity Q3 2008 | Hole House (increased capacity) | Energy Merchants Gas Storage (UK) Limited | Exempt  | 300         | 60                     | 60                        |
| Mid 2007                                      | Caythorpe                       | Warwick Energy                            | Applied for exemption                                       | 3000        | 120                    | 90                        |
| 2007  | Welton and Scampton North       | Star Energy                               | Not applied   | 4720        | 89                     | Information not available |
| 2007/08                                       | Aldbrough                       | SSE/Statoil                               | Not applied   | 4427        | 421                    | 211                       |
| 2007/08                                       | Byley                           | Scottish Power                            | Applied for exemption                                       | 1758        | 175                    | 88                        |
| 2007/08                                       | Fleetwood                       | Cantaxx                                   | Not applied   | 18000       | 1200                   | 1200                      |

<sup>7</sup> The data in this appendix has been provided to Ofgem directly by the relevant storage facility owners.

## **Appendix 2: Draft exemption order**

# **GAS ACT 1986 SECTION 19A EXEMPTION**

Pursuant to sub-section 19A(6)(a) of the Gas Act 1986 (the Act), the Gas and Electricity Markets Authority hereby gives to Holford Gas Storage Limited<sup>8</sup>, as a person who expects to be an owner of a storage facility, an exemption from the application of section 19B of the Act in respect of the storage facility to be located in Byley, Cheshire, subject to the attached Schedule.

**Steve Smith**

Authorised in that behalf by the  
Gas and Electricity Markets Authority  
Dated xxxxxx

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<sup>8</sup> Registered in Scotland No. SC254265. Registered Office: 1 Atlantic Quay, Glasgow, G2 8SP.

**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 the Byley storage facility  |
| “facility owner”    | means Holford Gas Storage Limited in its capacity as owner of the storage facility                    |
| “facility operator” | means Holford Gas Storage Limited in its capacity as operator of the storage facility                 |

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

The capacity of the facility, being 1758GWh.

**C. Period**

Subject to section E below, and pursuant to section 19A(3)(a) of the Act, this exemption shall come into effect on the date that it is issued and will continue until it is revoked in accordance with Section E.

**D. Conditions**

Pursuant to sub-section 19A(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 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, each as amended from time to time; or
  - (b) monitoring the operation of this exemption.
- 3. 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 | means any holder of a gas transporter licence under   |



|              |   |
|--------------|---|
| transporter” | 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 |
|--------------|---|

4. 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.
5. The Authority may, with the consent of the facility owner, amend this exemption.
6. 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 19A(4) of the Act, this exemption may be revoked in the following circumstances:

1. 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) the Authority considers that the use of the facility is necessary for the operation of an economically efficient gas market;
    - (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, as amended from time to time) 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, as amended from time to time, made in relation to it;
  - (iv) the facility owner is found to be in breach of any national or European competition laws, such breach relating to the facility;,
- (b) the facility owner has failed to comply with a request for information issued by the Authority under paragraph D2 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 D3 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.
2. This exemption may be revoked by the Authority with the consent of the facility owner.