



Global Markets & Investment Banking Group

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Sonia Brown
Director, Markets
Office of Gas and Electricity Markets
9 Millbank
London
SW1P 3GE

Consultation on the proposed treatment under section 19A of the Gas Act 1986 of gas storage facilities with split ownership

Dear Sonia,

Thank you for your letter of 22 September 2005 to the industry regarding the possibility of considering separate third party access (TPA) exemption requests from Statoil UK (STUK) and Scottish and Southern Energy (SSE).

Merrill Lynch Commodities (Europe) Trading Ltd (MLCE) considers that efficient and effective regulatory rules for TPA are an important part of the continued development of infrastructure and markets in the UK, and that the exemption regime can be a useful tool to encourage efficient investment when applied correctly.

In the current UK market there is a heavy reliance on market participants responding to price and supply/demand scenarios for the provision of infrastructure to delivery gas to consumers. The existence of TPA rules will help to ensure that assets can be used efficiently and effectively when the absence of those rules may have allowed restrictive or discriminatory access.

The circumstances leading to restrictive and/or discriminatory access to storage are most prevalent in markets with low levels of competition amongst system users, or from other sources of gas flexibility. This is a common problem in Continental gas markets where a lack of a traded market limits the value of using storage for trading purposes (even so, many of these markets have not applied TPA). Instead TPA rules in these markets, where they apply, tend to focus on access for the purposes of end user supply.

Issues may also arise where new facilities represent a significant part of total market share such that restrictive practices may unduly influence prices in the entire market. The current TPA exemption rules correctly focus on the main issue of market power in this respect.

We consider that the UK market exhibits an approach to storage where services are typically sold in competition with other providers of flexibility, and developers seek to invest based on a view that they will be able to achieve market based prices for their product. The TPA exemption regime is valued by storage developers because the commercial merchant risk of storage development is matched by a relatively unfettered ability to seek appropriate commercial returns. We believe that this model encourages the best investment decisions at a lower risk.

In terms of the STUK and SSE assets, we understand that the investment decision to develop commercial storage services was taken entirely separately by each company. The later decision

Merrill Lynch Commodities (Europe)
Trading Limited

Merrill Lynch Financial Centre
2 King Edward Street
London EC1A 1HQ

Tel 020 7628 1000



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to jointly develop and operate the facilities (which does not impinge on the individual parties commercial rights) appears to be based on the grounds of efficiency which should be welcomed.

While we understand concerns on whether separate consideration may encourage the development of particular business structures, we do not see this as a real problem with respect to UK storage assets given the current level of competition. In addition a decision to consider separate applications would not preclude Ofgem from making a different decision in different circumstances. In short, there appears little risk of setting a precedent that would fetter Ofgem's future decisions or signal any shift in the general policy on TPA exemptions.

In conclusion, we consider that separate consideration of applications for TPA exemptions would be appropriate in this case based on the commercial arrangements for this facility.

I hope that you will find these views useful. If you have any questions I can be contacted on 02079959021 or by e-mail at adam_cooper@ml.com.

Yours sincerely,

Adam Cooper
Vice President, Regulatory Affairs
Merrill Lynch Commodities (Europe) Trading Ltd