PETGAS

PETGAS TRADING (UK) LTD

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PETGAS Response to Consultation on Proposed Incentive Arrangements for the Provision of NTS Entry Capacity at Milford Haven

PETGAS welcomes the opportunity to respond to the above mentioned consultation. PETGAS participation in the UK gas market stems from its role as the primary capacity holder at the Dragon LNG terminal, currently under construction in Milford Haven, Wales.

Background

Ahead of the Entry Capacity Auction held in September 2004, Dragon LNG entered into a Preliminary Works Agreement with National Grid in 2003 and early 2004. The execution of the PWA provided National Grid with advance notice on the requirement for additional NTS capacity, allowing National Grid to plan for its activities in relation to the timely delivery of the required NTS capacity. It should be recognised that the parties at Dragon entered into the PWA with National Grid at a very uncertain time, accepting the risk of not having Third Party Access exemption granted to Dragon LNG. Should the exemption not been granted, the project may have ceased to be viable and the several million pounds paid to National Grid would have been forfeited.

The parties at Dragon have been in close communication with National Grid from as early as 2002 onwards on the plan of constructing an LNG terminal at Milford Haven and consequently the requirement for NTS capacity. Therefore, the difference between the results of the first and second entry capacity auction held respectively in September and December 2004 should not be construed as a surprise to National Grid.

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In view of the above, PETGAS would like to share the following comments on the consultation.

Should new incentive arrangements be developed for National Grid NTS be developed in relation to the delivery of gas transmission capacity for Milford Haven?

PETGAS is of the opinion that given the magnitude of the potential buyback costs and the fact that these buybacks are required as a result of a once-off and specific event, a new incentive arrangement is required for Milford Haven. PETGAS acknowledge that the existing regime is designed to allow and incentivise National Grid in managing day-to-day operational constraints within the system.

Additionally, PETGAS believes that any new arrangement should provide the right incentive to National Grid for timely completion of the pipeline connection and NTS reinforcement related to Milford Haven. As such, the caps on the exposure to National Grid should be higher than the costs involved in ensuring timely completion of the pipeline project.

Are the principles identified in paragraph 4.3 an appropriate basis for new incentive arrangements?

Considering the chain of relevant events, and acknowledging that it is in the industry interest that National Grid remains financially viable, PETGAS believes that National Grid should not be protected from the risks which arise as a result of its operations. Recognising that parties at Dragon LNG and specifically shippers at Milford Haven have gone beyond the requirements of the regime in providing relevant investment signals to National Grid for the provision of NTS capacity, PETGAS is of the opinion that the idea of localising the issue and exposure at Milford Haven to the shippers at Milford Haven is unreasonable.

For National Grid to remain competitive as a regulated business within a liberalised market, PETGAS would suggest that an incentive be put in place such that it reflects the true performance of National Grid as a business entity.

What are the advantages and disadvantages of the new incentive arrangements described in this chapter?

PETGAS believes none of the options proposed provide the necessary incentive on National Grid to ensure timely delivery of the required NTS capacity. Furthermore, given the circumstances that have led to the issue we face today at Milford Haven, PETGAS propose that National Grid bear a greater proportion of the buyback costs, possibly more than the 35% suggested.

Should National Grid Gas NTS be shielded from buyback costs if there are undue delays in the DTI giving consent for the construction of the reinforcement pipelines, adverse weather conditions or other exceptional factors

PETGAS is of the opinion that given National Grid's experience in constructing gas pipelines in the UK, National Grid should be very familiar in managing aspects relating to the construction of gas pipeline in the UK e.g. planning permission, weather etc. Therefore, it is reasonable to expect National Grid to factor appropriate allowances into its construction schedule to manage gas pipeline construction projects. DTI consent, planning permission and adverse weather conditions are typical operational risks that an entity like National Grid faces and it is not unreasonable for National Grid to put in place the necessary risk management procedures to manage such risk. Nevertheless, PETGAS acknowledge that there are circumstances which are beyond National Grid's control that may warrant National Grid's exposure to buyback costs being deferred, however having examined the relevant chain of events PETGAS does not believe the circumstances at Milford Haven falls under this category.

Should this deferral skip the period November-February during which construction is not practical?

Once again, we believe National Grid being an experienced gas pipeline developer would have taken the period between November-February in scheduling pipeline construction projects. Therefore, PETGAS considers this proposition as another attempt to weaken the incentives on National Grid in fulfilling its obligation.

Are there further steps which should be taken to encourage National Grid Gas NTS and the relevant shippers to enter into arrangements that would minimise the economic costs of any delay in the provision of transmission capacity at Milford Haven?

As one of the shipper at Milford Haven, PETGAS has been in close discussion with National Grid and will continue to do so to help tackle the issue. Perhaps it is worthwhile at some point for the shippers at Milford Haven to discuss this matter jointly with Ofgem and National Grid.

We hope you find the above comments useful. I look forward to discussing these points with you further, if required.

Yours sincerely

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Commercial Executive

Additional Note:

1. PETGAS is a wholly-owned subsidiary of Petronas
2. PETGAS owns a 3 billion cubic metre capacity per annum at the Dragon LNG terminal
3. PETGAS is a registered gas shipper in the UK, under the name Petgas Trading (UK) Limited
4. PETGAS holds long term entry capacity at the Milford Haven ASEP
5. Petronas is a 30% shareholder in Dragon LNG