



**Industry & Regulation**

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25 January 2007

Carlos Martínez-Rico  
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Ofgem  
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Dear Mr Martínez-Rico,

**Re: National Grid Grain LNG Ltd application for exemption from Section 19D of the Gas Act 1986.**

Thank you for the opportunity to comment in respect of the above response. These comments are on behalf of the Centrica Group apart from Centrica Storage Ltd.

Centrica is supportive of Ofgem's initial view that the exemption for Grain Phase 3 should be granted. We believe that the National Grid Grain LNG Ltd (GLNG) application meets the exemption criteria, and as a Shipper, we need the certainty that the exemption will be granted in order to make a commitment to capacity in Grain 3.

Furthermore it is important that Ofgem should be consistent in its regulatory decisions, so that shippers operating in Phase 3 at the Isle of Grain are not disadvantaged compared to shippers operating at other terminals in GB. We do consider that Ofgem's initial view is essentially consistent, subject to our comments on specific points set out below.

***Question 1: Do you agree with our overall assessment that the proposed exemption should be granted, based on the examination of whether each of the exemption criteria have been met?***

We agree with the assessment that the exemption should be granted based on the fact that GLNG's paper demonstrates that it meets all of the exemption criteria. In addition, we welcome those elements of the application which clearly move towards the preferred approach under the European Directive, including an open season which makes capacity available to the market.

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**Question 2:** *Do you agree with the proposed duration of the exemption?*

We are able to support the proposed 20 year exemption as it would cover a shipper's long term contract in the Terminal. This would mean that those shippers who have been successful in the open season process would have certainty with regards to access to the importation and regasification facilities for the full duration of their contract.

Matching the term of the exemption to the term of the contract enables capacity holders to confidently seek long term supplies without concerns over possible non-extension or non-renewal of the exemption at the end of its term. We do, of course, note the provisions around revocation in the draft Order, but this would normally be a much more limited risk.

However, our support for the 20 year exemption period is contingent upon robust anti-hoarding measures being in place. We note the proposals in respect of anti-hoarding in the application and are satisfied that these should be sufficient, subject to adherence by all parties involved and careful monitoring of their effectiveness by the terminal operator.

**Question 3:** *Do you agree that the proposed exemption should be subject to re-examination by the Authority, and if necessary to amendment or revocation, once the actual allocation of capacity through the open season process is known (particularly in the event that the outcome of the open season differs from that as represented by GLNG in its additional information and undertakings)?*

Ofgem's own analysis shows that there are no competition concerns attached to the exemption, recognising that 'even in the worst case scenario where the maximum volume of capacity goes to the bidder with the largest market share, we would not expect the market to become concentrated to an extent that would be detrimental to competition'. Additionally, the Frontier Economics analysis submitted by GLNG also found this to be the case. Centrica does not therefore believe that the proposed exemption should be re-opened after the allocation in the open season process is known on the basis that the existing exemption criteria have been met by Grain's application irrespective of the identity of the successful bidders.

We also wish to highlight that we do not support any limitation being placed on amounts of capacity acquired by individual market participants in the Grain Phase 3 open season process. In the absence of competition concerns, the open season process should not be restricted in this way and should provide all bidders, whether new or existing, with the same opportunities to acquire capacity. Principles of economic efficiency and fairness require capacity to be allocated to those market participants who place the highest value on it. Further review after the event would thus breach the fundamental principles of the open season process.

**Question 4:** *Do you consider the competition assessment to be complete, and that it provides you with sufficient information on which to comment?*

We agree that the competition assessment is complete and provides sufficient information (in the document and appendix) on which to comment.

**Question 5:** *Do you agree with the assumptions underlying our competition assessment, as outlined in Appendix 4?*

The assumptions referenced in appendix 4 seem reasonable.

**Question 6:** *Do you agree with our views on the definition of the relevant market? In particular, do you consider the flexible gas market remains the appropriate market definition for considering the effect on competition for the development of a new LNG importation facility?*

Centrica believes that Ofgem has covered all scenarios by analysing not only LNG, but also the broader market for flexible gas supplies – including storage and gas pipelines. It is helpful that Ofgem concluded that LNG alone was too narrow a position to consider. We also believe that it is relevant to consider flexible beach gas supplies and demand side interruption as part of the overall flexibility market, but their exclusion has not materially affected the result in this case.

**Question 7:** *Do you agree with our views that granting an exemption for Grain 3 would not have a detrimental impact on competition in any European gas market?*

Centrica fully supports Ofgem's view that granting an exemption would not have a detrimental impact on the European gas markets considered (which we believe to be those which are most relevant). This support is dependent on the implementation of robust anti-hoarding measures.

**Question 8:** *Do you consider that there should be any additional conditions attached to the proposed exemption?*

Centrica believes that there should not be any additional conditions attached to the exemption as Ofgem should avoid regulatory uncertainty and be consistent with other GB importation terminals in form of the exemption to be granted.

However, we do consider that the anti-hoarding measures will need to be given full effect. On the basis that Ofgem has not included the requirement in the draft Order, we assume that condition 1 under Section D, in combination with the information given in the Application and Undertakings is deemed sufficient to impose this requirement. We would welcome confirmation of this point.

**Question 9:** *Do you think that we should develop a guidance note on anti-hoarding arrangements to apply at LNG importation terminals?*

Centrica is supportive of Ofgem developing a guidance note on anti-hoarding arrangements to apply at LNG importation terminals, so long as this matches any similar/related guidance papers that may be drafted at a European level by for example ERGEG. We believe that it is important that the industry has clarity on this issue, especially since there is no specific provision in the draft Order.

In addition, we understand that ERGEG has issued guidelines in the areas of the Secondary Market, New Gas Infrastructure and Exemption from Article 22 and LNG TPA. With this in mind we believe that any guidelines drawn up on anti-hoarding arrangements at a UK level should support and complement any that may be drawn on a wider European scale. We do consider it important that equally effective anti-hoarding measures be applied across the EU and we would, therefore, see advantages in such guidelines being developed at the ERGEG

level. We note that the recent decision on anti-hoarding measures in respect of new LNG terminals in The Netherlands is somewhat different from the UK approach, which in turn is somewhat different to that adopted for the Zeebrugge terminal in Belgium. This further reinforces the case for EU-wide guidelines, to help ensure a greater consistency of application across the market as a whole.

In addition to the above points, we have noted with interest the helpful report prepared for ERGEG by NERA on TPA at LNG regasification terminals. The section on the need for harmonisation is particularly useful in the context of the guidelines under discussion.

## **Additional Comments**

One further point we would like to make concerns the Investment Risk criteria applied to the application.

We have reviewed the DG Tren Note on Exemption from TPA Regulation, in particular with respect to the definition of major investment.

The Note states that "an example of a suitable rule of thumb might be that to be defined as a 'major investment', the project would have a capital cost of more than €10 per connected customer". In a footnote it refers to the number of households benefiting from the investment, although the number of customers will exceed the number of households in a market by also including non-residential customers.

The Note then goes on to state that a risky investment should concern firstly a sunk cost, and secondly be risky in terms that the market which it aims to supply is open to potential large changes; changes in projected consumption, other competing investments being made, changes in world market for primary fuel, or an above average amortisation period for such type of investment.

In our opinion, Grain Phase 3 would be expected to fall within the definition of the second paragraph above, without the requirement to rely on the "rule of thumb" guidance of 10 euros per connected customer.

However, we have received indications that GLNG believed it necessary to apply the "rule of thumb" guidance strictly, such that Grain Phase 3 required investment in excess of €210m, to qualify for an exemption. Centrica is concerned that such an interpretation might operate in a way which would be unnecessarily restrictive in defining the project scope. We believe that GLNG should be able to find the most economically attractive solution to increase the importation capacity without having to ensure that the capital requirement in their project exceeds an arbitrary threshold.

We understand that there were potential options for Grain which required a lower investment, but they were not pursued with as much vigour by GLNG due to this strict interpretation. For example, we understand that GLNG could build a jetty only and increase the efficiency of the existing storage tanks, or they could build a new jetty and a new storage tank (which represents the major component in cost terms of building a regas terminal. Opting to pursue the second course took the project above the deemed EC major investment indicative threshold but was not necessarily the most economic option.

If GLNG had chosen to pursue the first option of building a jetty only, the efficiency of the Terminal could have been increased by maximising the existing throughput for all shippers.

This would have been expected to lower the tariff rate for shippers since prospective shippers would only have to underwrite the costs of the new jetty and associated equipment, rather than the costs of a new jetty plus a new storage tank and associated infrastructure.

We are concerned that such an apparently overly restrictive interpretation might lead to relatively inefficient outcomes, and we would welcome clarification of Ofgem's view in this area.

We hope that these comments have been helpful, and if you would like to discuss any points in more detail, I should be happy to help.

Yours sincerely,

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Upstream Energy