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Robert Hull
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By E-mail: robert.hull@ofgem.gov.uk

Dear Robert,

Re: LNG Storage Price Control – Initial Thoughts

Thank you for the opportunity to comment on the above document, this non confidential response is on behalf of Centrica plc excluding Centrica Storage Ltd. We are happy that Ofgem place this response on their website and in the Ofgem library.

In general we are broadly supportive of the document, and agree that if competition is to be introduced into the non competitive aspects of LNG storage (i.e. provision of Operating Margins and LNG tanker service support at Glenmavis), then it is necessary to continue a form of price regulation until competition is introduced. However, whilst we are not opposed to the introduction of competition in these areas, we believe that prior to implementation, Ofgem should demonstrate that there is a robust, quantitative case to show that there are likely to be significant financial benefits to customers as a result. Given the relatively small sums involved, we are not yet persuaded that the costs of introducing competition in these areas would be objectively justified.

If competition is to be introduced into the provision of operating margins, then it would seem appropriate that NGG should no longer be entitled to reserve existing LNG storage capacity for this purpose.

We would propose that the following steps would be required:

(a) Create a market/auction for Operating Margins gas
(b) Offer all the LNG storage capacity to third parties at auction; and
(c) NGG buy back what they need for Operating Margins, from that source or any other.

This should allow the LNG price regulation to be dropped after a transitional period which will be required to ensure that the new arrangements are fully functional.

In terms of the objectives for the price control which have not been listed in chapter 1, we believe it would also be appropriate to incentivise the efficient procurement by transporters of competitive services in future. Hence, Ofgem should consider in parallel whether a further incentive scheme may be required in this area under the SO control.

In addition, we note Ofgem's view in 1.13 that consumers should not underwrite the long term cost of facilities which might not be needed, and further that consumers should not bear decommissioning costs. Whilst we agree with the second part of this statement, as we consider such costs will have already been addressed in principle as part of the regulated asset base, we do not agree with the first part. Clearly, socialisation of costs is a very serious matter, and not a decision to be taken lightly, however, we do not agree that a blanket exclusion is appropriate. All such issues must be considered on a case by case basis, in the wider context, as we do believe that there are cases where such socialisation is appropriate and can be fully supported by reason of security of supply. Further, we would highlight that simply because a facility has not been used to date, it does not mean it is unnecessary.

We have considered the two options proposed for the form of control, namely, a price cap or a revenue allowance. On balance we believe that a third option would be beneficial and that Ofgem should introduce a revenue target with a cap, collar and sharing factors. This approach is flexible, has proven itself of value in terms of other incentive schemes and has the merit of sharing the costs and the risks between the transporter and customers. The flexibility inherent in a revenue target approach would be especially beneficial given that an implementation timetable of April 2009 seems challenging. We also believe that a revenue target approach would better support a transitional period as mentioned above.

In chapter 3 we noted the footnote reference to a document, "Review of the National Grid Storage Business" by TPA Solutions, 17th October 2006. Unfortunately, we understand this document is not presently in the public domain. We would welcome publication of this document as soon as possible, and may wish to comment further if the contents raise any particular issues.

Ofgem has flagged a potential issue of double counting in chapter 3, with an associated risk that NGG might be remunerated twice for investment for a limited period of time. Whilst the issue is time limited, we are still opposed to such double counting and consider that a revenue adjustment would be appropriate.

We agree with Ofgem that inclusion of the associated funds within the LNG storage price control would be more cost reflective. In our view, an amendment should be made to the NGG NTS RAB to bring the two into line.

Should you wish to discuss any of the points raised above in more detail, I should be happy to help.

Yours sincerely,

By e-mail

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