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Dear Bogdan,

Proposed disposal of part of NTS for Carbon Capture and Storage Consultation

Thank you for providing Scottish and Southern Energy (SSE) with the opportunity to comment on the above consultation. We have detailed our responses to the consultation questions in an attached annex; however we would take the opportunity to reiterate our high level views.

SSE are the UK's largest non-nuclear generator and have a wide-ranging commitment to addressing the long-term energy challenges facing the UK: to encourage lower carbon; and more secure supplies of electricity. We operate the largest renewable energy fleet in the UK and have recently increased our target to reduce the carbon intensity of our fleet from 20% by 2016, to 50% by 2020.

We fully support the objective of the UK Government for CCS to be developed and demonstrated to be a viable low carbon option for deployment post 2020, and recognise the potential of CCS as a tool in the battle against climate change. We also have a long standing and active interests in developments in CCS technologies, evidenced by the Peterhead DF1 project and our role as prime sponsor in the BERR supported Oxycoal 2 Project.

Moreover, we support the concept of disposing of redundant assets for alternative uses. We would highlight that little mention is made in the consultation of the impact the disposal will have on offtake supplies to the Scottish DN and directly connected customers, nor has there been an assessment of the potential impact on flexibility availability.

On the understanding that there will be no impact on offtakes, we believe that Ofgem, by allowing NGG to appropriately dispose of redundant pipeline for alternative usage, will open a much needed 'fast track' enabling the UK to tackle climate change by allowing faster testing of the feasibility of CCS.

I hope that you find our comments helpful. If you would like to discuss any of the points raised in more detail, please do not hesitate to get in contact.

Yours sincerely,

Claire Riach
Regulation Analyst

Annex 1: Consultation Questions

Chapter 2: Proposal to dispose of assets for CO₂ transportation

Q1: Do you think this proposal is a good idea in principle?

SSE fully supports the proposal to dispose of redundant assets for alternative use. We believe doing so could result in: benefit to customers by finding an alternative (or more valuable) use for network assets leading to lower transportation bills; fast track CCS testing; and ultimately avoid unnecessary pipelines and environmental impacts.

Q2. In the event that a feeder section is removed, existing compressors may be required to work harder to transport the same volumes of gas through fewer pipes. It is proposed to capture these additional compressor fuel costs and to introduce a capped volume for these additional fuel costs, based on pre-disposal levels, over which the new CO₂ transportation business would bear the costs and make payment to NGG. What is your view of this proposed treatment of these additional compressor fuel costs?

Please refer to Chapter 3 Q.6

Chapter 3: Regulatory issues

Q1. Do you agree with our view of the regulatory issues of the proposed asset disposal?

Yes.

Q2. Do you agree with the projected forecast flows at St. Fergus?

We believe that in order to provide a truly accurate assessment of the asset value of the pipeline to used for CO₂ transportation, the forecast flows should be modelled in more detail.

NG's 10 yr Statement gives the following sensitivities at St.Fergus:

- UKCS +/- 20 bcm by 2014 down to West of Shetland & general decline uncertainty.
- Norwegian imports +/- 20 bcm by 2014 down to Vesterled, Tampen (St Fergus Entry) & Langeled (Easington) uncertainty.

This large level of uncertainty relative to demand, (100 bcm/year) gives considerable uncertainty as to how much capacity might be required at St Fergus. We are concerned that NGG's forecasts underestimate the projected forecast flows at St. Fergus. We believe NGG must undertake more detailed forecast flow analysis to look in more detail at the low base and high base flow scenarios.

Q3. Are there other flow forecasts or scenarios which should be taken into account?

Please refer to Chapter 3 Q.2

We note the absence of analysis on the impact the disposal would have on offtakes to the Scottish DNs and NTS directly connected sites. Similarly no information has been provided on the impact the disposal of 130km of NTS pipeline might have on flexibility availability. It would be helpful if this information could be provided.

We would also like to better understand how the benefits are to be transferred back to customers i.e. from sale of asset and sale of linepack in pipeline. For example, we assume that the revenue from the asset sale will come off the NTS RAV, but are unsure when this will happen i.e. immediately or after a number of years (presumably it is after 5 years in common with the policy applied to other network businesses). However, we are unsure how the sale of linepack will revert to shippers.

Q4. What is your view of the indicated capability at St. Fergus with the feeder removed, with and without additional compression?

We are unable to provide a view in regards to the indicated capability as we do not have access to either: NGG's forecasting models; and the information inputted.

Q5. What is your view of the projected buyback costs which have been identified?

We believe the assumed buyback price in NGG's forecasting to be too low (1p/kWh). Based on our experience, we believe the assumed buyback cost should be at least three times NGG's assumption i.e. 3p/kWh.

Q6. Are there any other issues that you believe are relevant?

Regardless of which commercial arrangement is decided upon, we believe the following points should be taken into consideration:

- If NGG opt to buy a new compressor rather than compensate via buyback (at least until 2020 when NGG propose the original feeder would have been removed), the value of the additional compressor fuel costs should be paid by the new NG CO₂ transportation subsidiary, rather than by customers via the regulated NGG business.
- If NGG opt to use the buyback method, there should be no cap on the additional buyback spend required to balance the system by the NG CO₂ transportation subsidiary. NGG have proposed there should a cap on the amount paid by the up to the value of an additional compressor. If NG's CO₂ transportation subsidiary choose to opt with the buyback option rather than buy a compressor option; they are responsible for the risks associated with it. Customers should not be expected to effectively neutralise NG's CO₂ transportation subsidiary risk by being forced to pay for the costs associated i.e. buyback costs over and above cap.
- The consultation states that by removing the feeder, the existing compressors will need £5m more fuel per annum. If NG's CO₂ transportation subsidiary decides to use the buy back option, they should be required to pay the full value of the buyback costs plus the cost of the additional compressor fuel required. This will prevent customers paying for costs associated with CO₂ transportation.

Q7. What is your view of the proposed disposal of these assets?

Please refer to Chapter 2: Q1.

Chapter 4: Valuation of assets**Q1. Do you agree with the possible ranges of valuations for the assets which have been identified?**

We agree with the possible ranges for valuation, but note that there are alternatives, that could be assessed that may or may not lie in this range, for example:

As a matter of principle, we believe the valuation should reflect the relevant risks that the two entities are taking in the transaction. Accordingly, in our view a residual value based on the existing use of the asset, reflecting the remaining life would seem more appropriate.

Ofgem has put forward a number of non-market based alternative methodologies to derive an appropriate asset value that are based on a residual value of the assets. The depreciation can either be in line with NTS depreciation policy or the Regulated Assets Value (RAV) depreciation policy if different. At this stage, we believe that to the extent that these policies do indeed differ, it would be most appropriate to use the RAV depreciation such that the valuation is based on the residual value of the assets in terms of the RAV.

Other options may also have merit for example, the value could be based on the purchase price of book value assets, depreciated in line with the NTS depreciation policy to reflect the age of the assets. We note that this principle would be consistent with the valuation of metering assets being transferred out of the electricity distribution networks during DPCR4.

Finally, it would be helpful if Ofgem could confirm when and how the final valuation figure would be realised for customers. It is our understanding that the prescribed sum and associated operating costs would be taken off NGG's RAV and allowed operating costs. This would result in correspondingly reduced allowed revenue for NGG and therefore, all other things being equal, reduced transportation charges. However, we are unsure whether this would take effect immediately, or whether there is a "capex roller" mechanism that allows NGG to reap the benefit of the sale for 5 years before the RAV is reduced. To retain incentives for efficient asset disposal, we could support the application of such a 5-

year rolling mechanism.

Q2. Do you agree with the assumptions which underpin the asset valuations?

Based on the information provided in the consultation, we believe the assumptions to be reasonable. As above we seek clarification on how the value would be released to customers.

Q3. Is there an alternative method of asset valuation which should be considered?

Please refer to Chapter 4: Q1.

Q4. Do you agree with the assessment of benefits associated with asset disposal and alternative use?

Yes.

Q5. Are there any other considerations that should be taken into account?

In light of the requirement to progress CCS technology, we believe its proposed use to be the most effective.

Chapter 5: Commercial options

Q1. Do you consider that the opportunity to potentially share in the benefits of CCS using ex NTS assets represents an appropriate balance of risk and reward?

We believe that any commercial option that exposes the customer to an excessive and unnecessary level of risk is fundamentally wrong. We do not believe customers would wish to take on the risks associated with a non-regulated business.

Q2. What is your view of a lump sum payment, in the event that consent is granted for disposal?

We believe it is the correct method as it is a clear and simple process.

Q3. What is your view of a participatory royalty arrangement, in the event that consent is granted for disposal?

Please refer to Chapter 5: Q1

Q4. Are there other risks/benefits which should be taken into account?

No.