

ANNEX

Storengy UK Limited Application for Exemption from 19B of the Gas Act 13 July 2009

1 Introduction

- 1.1 Storengy UK Limited (“SL”) is a wholly owned subsidiary of the GDF Suez Group (“GDFS”). SL is responsible for the design, construction, ownership, operation and maintenance of the Stublach Gas Storage facility over the next 30 years after which it will be transferred back to landowners, INEOS Enterprises Limited (“INEOS”). This development represents GDFS’s first Gas Storage Facility in the UK; the implementation of the Stublach Gas Storage Project (“SGSP”) by SL, a new entrant, will enhance competition in the UK flexibility market.
- 1.2 The Gas (Third Party Access) Regulation 2004 came into force on 26th August 2004. Section 19A of the Gas Act sets out the process via which owners of storage facilities can apply for an exemption from the requirements to provide negotiated third party provided for in Section 19B.
- 1.3 SL is making an application under section 19A(6)(a) of the Gas Act requesting an exemption from the application of section 19B in relation to its ownership of the salt cavity gas storage facility being constructed at Stublach. In making this application SL is of the view that the use of Phase 1 of the facility by third parties is not necessary for the operation of an economically efficient gas market.
- 1.4 The Energy White Paper set out Government’s strategy to managing security of supply risks. Integral to that strategy is the need for increased gas storage infrastructure which Government recognized should be provided by commercial ventures. In order to encourage private investment in new storage infrastructure, Government has introduced the Planning Bill which aims to streamline the approval process for the construction of major infrastructure of national importance, including Gas Storage facilities. Consistent with Government policy aims the development of the Stublach facility will contribute to the management of UK security of supply risks.
- 1.5 When assessed against the definition of the appropriate market for flexibility as set out in the Competition Commission’s report on Centrica’s acquisition of Rough Storage, the proportion of flexibility that will be provided by the Stublach facility is not significant and therefore the use of this facility by other persons is not necessary for the operation of an economically efficient gas market. It is clear that the market for flexibility is already highly competitive and would therefore not be impacted by an exemption being granted to SL.
- 1.6 Furthermore, the size of Phase 1 of the Stublach facility is similar to that of the storage facility at Byley in respect of which Ofgem granted an exemption in July 2005¹. Even if it

¹ Decision on an application by Scottish Power Energy Management Limited on behalf of Holford Gas Storage Limited for an exemption under section 19A(6)(a) of the Gas Act 1986 from section 19B of the Gas Act 1986: Ofgem, 06 July 2005



is on a limited scale Phase 1 of the Stublach project will increase the level of storage capacity and flexibility in the UK and therefore will reinforce the level of economic efficiency of the UK gas market.

2 Project detail

- 2.1 SL acquired the Stublach development from INEOS in December 2007. The agreement with INEOS permits SL to construct a Gas Storage Facility on land owned by INEOS. SL will maintain ownership and operational control for 30 years, transferring the facility to INEOS in 2037. Phase 1 of the development, providing 10 salt caverns, will be constructed between 2010 and 2012 allowing for gas filling to occur during summer 2013. The first 4 cavities of Phase 1 will be ready to commence storage services during autumn 2013. The remaining 6 cavities of Phase 1 will be operational from autumn 2014. A decision to expand the facility further will be taken at a later date.
- 2.2 On completion of Phase 1, the facility will provide 1500GWh of space, 175GWh/day of injectability and 175GWh/day of deliverability. The deliverability rate is the maximum rate which can be achieved when the facility is full; as the level of inventory declines so does the available rate of deliverability. The facility is classified as mid-range due to its ability to cycle on a seasonal and non-seasonal basis.

3 Competition Analysis

- 3.1 As part of its letter on storage regulation, Ofgem suggested that a competition analysis should accompany any application for exemption².
- 3.2 Based on the Competition Commission report into the acquisition of Rough storage facility by Centrica PLC³, Ofgem define the relevant product market against which exemptions should be tested as the flexibility market within Great Britain. Ofgem states in its final decision relating to the application made by Statoil in relation to its share of the Aldbrough storage facility (the Statoil Decision), that the product definition of gas flexibility is not straightforward.⁴
- 3.3 SL has carried out its analysis based upon that presented by Ofgem in the Statoil Decision. The data presented incorporates all contracted sources of potential flexibility within the GB Gas Market available to companies within the GDF Suez Group ("GDFS").
- 3.4 GDFS's share of the flexibility market will increase with the construction of Stublach, however, as stated above this increase in market share is not significant. Table 1 identifies GDFS's contracted sources of potential flexibility which shows that GDFS flexibility peaks in 2014⁵. The competition analysis performed by SL has been conducted using this peak flexibility. All of the facilities assumed to be operational in 2014 are also

² The Second EU Gas Directive and storage regulation Great Britain: Ofgem, 25 November 2004

³ Centrica plc and Dynegy Storage Ltd and Dynegy Onshore Processing UK Ltd: A report on the merger situation; Competition Commission,

⁴ Final Decision: Statoil UK Ltd's application for an exemption from section 19B of the Gas Act 1986: Ofgem, 25 October 2007

⁵ All capacity holdings included in Table 1 and attached footnotes are provided to Ofgem on a confidential basis. Given their commercial sensitivity SL would kindly request that Ofgem does not publish these figures.



assumed to be operational in 2013, thus Gas Year 2014 provides currently the most severe case for competition analysis.

Table 1 – GDFS Contracted Sources of Flexibility in the GB Gas Market

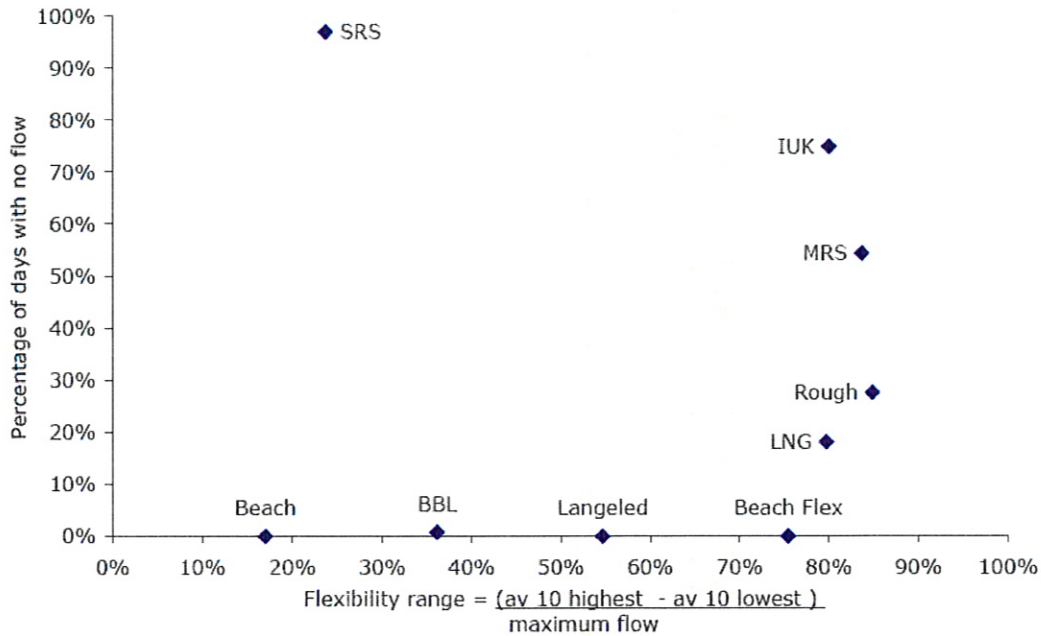
GWh/day	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Medium Range Storage ¹	CONFIDENTIAL										
Long Range Storage ²											
Short Range Storage											
BBL											
IUK reverse ³											
Langeled											
Vesterled ⁴											
Isle of Grain LNG ⁵											
Flexible Beach ^{6,7}											

- ¹ Confidential
- ² Confidential
- ³ Confidential
- ⁴ Confidential
- ⁵ Confidential
- ⁶ Confidential
- ⁷ Confidential

3.5 As detailed in Table 1 there are numerous sources of flexibility in the gas market. In addition to medium range storage these can broadly be characterised as follows: short range storage, long range storage, beach flexibility, LNG imports, pipeline imports and demand interruption. While theoretically all of the above sources of flexibility could be substituted for medium range storage, in the Statoil Decision Ofgem analyzed historic substitutability between MRS and the above sources and concluded that there were three separate potential market definitions:

- a. Medium range storage (MRS) + Long range storage (LRS) + Imports through Interconnector UK (IUK) + Flexible beach + LNG imports,
- b. MRS + LRS + IUK imports + Flexible beach + LNG imports + Flexible element of supplies from the Langeled pipeline (200GWh/day),
- c. MRS + LRS + IUK imports + Flexible beach + LNG imports + Flexible element of supplies from the Langeled pipeline (600GWh/day).

Figure 1: The flexibility of gas supply (25 November 2006 to 31 March 2007)



- 3.6 In the Statoil Decision Ofgem analysed the impact of discounting the applicant's holdings in other TPA facilities. While it is sensible to suppose that use it or lose it rules (uioli) in both LNG import facilities and IUK will prevent both capacity hoarding and the exercise of market power, like Ofgem, SL has elected to consider the impacts of including and excluding flexibility available in these facilities.
- 3.7 The results of the analysis carried out by SL are shown in Table 2⁶. The table represents the reproduction of the analysis carried out by Ofgem in its decision to provide Statoil with a TPA exemption in relation to its share of the Aldbrough facility.

⁶ All capacity holdings included in Table 2 and attached footnotes are provided to Ofgem on a confidential basis. Given their commercial sensitivity SL would kindly request that Ofgem does not publish these figures. However, SL would not be adverse to Ofgem presenting GDFS's share of flexibility markets in the form of data ranges.

Table 2 – GDFS Market Share of Flexibility Products

Ofgem Market definitions	a		b		c	
	Total	GDFS (TPAin)	GDFS (TPAex)	Total	GDFS (TPAin)	GDFS (TPAex)
Flexible Beach ¹	441			441		
LRS	455			455		
MRS ²	1233			1233		
LNG import	1568	Confidential		1568	Confidential	
Iuk ³	433			433		
Langeled ⁴	0			200		
Total GWh/d	4130	Confidential		4330	Confidential	
GDFS market share		5-10%	0-5%		5-10%	0-5%

¹ Sean/Barrow as proxy for Flexible Beach, rather than a wider market analysis, or the figure of 1145Gwh/d used in the Competition Commission report on the merger of Centrica plc and Dynegy Storage Ltd

² Includes: Hornsea, Hatfield Moor, Hole House, Humbly Grove, Holford165, Byley, Hole House Phase 2, Aldbrough Phase 1 and Stublach Phase 1

³ Limited IUK flexibility (433 Gwh/d) rather than capacity of 755Gwh/d

⁴ Only Langeled considered as source of additional pipeline import flexibility

TPAin means that capacity held by GDFS in such infrastructures have been included in the analysis.

TPAex means that capacity held by GDFS in such infrastructures have been excluded from the analysis.

- 3.8 It can be seen in all six cases GDFS has a market share of less than 10%. This share is consistent with that established in the Statoil Decision. Even in the most extreme of cases, under Ofgem Market Definition, where Langeled is assumed to provide no flexibility and the import supplies through LNG Terminals and IUK are included in the determination of GDFS's total flexibility, the market share attributable to GDFS is only approximately 8%.
- 3.9 Furthermore, in applying the assumptions employed by Ofgem in the Statoil Decision, GDFS believes that the outputs are likely to underestimate the overall market for flexibility. For example: beach flexibility used in this analysis is far lower than that assumed by the Competition Commission in its report on the merger of Centrica plc and Dynegy Storage Ltd; IUK reverse flow capability is lower than its nominal capability of 755GWh/d; and Langeled is assumed to be the only source of pipeline import flexibility.
- 3.10 SL has performed some additional analysis to satisfy Ofgem that under even more extreme tests, the market share attributable to GDFS remains negligible. SL has created two additional Market Definitions to those generated by Ofgem in the Statoil Decision. Each definition, including the Ofgem Definition, is then assessed against high and low level flexibility scenarios. The market definitions are as follows:



Case 1 (Max flex) = Flexible Beach + LRS + MRS + LNG Import + IUK + Langeled + Vesterled/Tampen + BBL + SRS

Case 2 (Ofgem flex) = Flexible Beach + LRS + MRS + LNG Import + IUK + Langeled

Case 3 (Min flex) = Flexible Beach + LRS + MRS

3.11 The results of the analysis are presented in Table 3⁷, noting that the volumes attributed to the high and low levels of flexibility are contained in the relevant columns.

Table 3 – GDFS Market Share under alternative Market Definitions

Case 1 Max Flex	Market (low)	GDFS (TPAin)	GDFS (TPAex)	Market (high)	GDFS (TPAin)	GDFS (TPAex)
Flexible Beach	441	Confidential	Confidential	1145	Confidential	Confidential
LRS	455			455		
MRS ¹	1233			1665		
LNG import	1568			1568		
IUK ²	433			755		
Langeled	200			600		
Vesterled/ Tampen ³	0			681		
BBL ⁴	0			473		
SRS	525			525		
	4855			7867		
GDFS market share				5-10%		

¹MRS for Market (high) includes Whitehill and assumes Aldbrough Phase 2 does not provide additional flexibility i.e. no increase in deliverability

²High case assumes max reverse flow; source National Grid 10 Year Statement 2007

³Vesterled/Tampen; source National Grid 10 Year Statement 2007

⁴BBL; source National Grid 10 Year Statement 2007

⁷ All capacity holdings included in Table 3 and attached footnotes are provided to Ofgem on a confidential basis. Given their commercial sensitivity SL would kindly request that Ofgem does not publish these figures. However, SL would not be adverse to Ofgem presenting GDFS's share of flexibility markets in the form of data ranges.

Case 2 Ofgem							
	Market (low)	GDFS (TPAin)	GDFS (TPAex)		Market (high)	GDFS (TPAin)	GDFS (TPAex)
Flexible Beach	441	Confidential			1145	Confidential	
LRS	455				455		
MRS	1233				1665		
LNG import	1568				1568		
IUK	433				755		
Langeded	200				600		
	4330				6188		
GDFS market share		5-10%	0-5%			5-10%	0-5%

Case 3 Min Flex							
	Market (low)	GDFS (TPAin)	GDFS (TPAex)		Market (high)	GDFS (TPAin)	GDFS (TPAex)
Flexible Beach	441	Confidential			1145	Confidential	
LRS	455				455		
MRS	1233				1665		
	2129				3265		
GDFS market share		5-10%	5-10%			5-10%	5-10%

3.12 Table 3 clearly shows that under alternative and more stringent Market Definitions to those proposed by Ofgem, GDFS's market share of flexibility remains below 10% of the total markets identified.

3.13 On its own, Phase 1 of Stublach accounts for less than 5% of the existing storage space.

4 Conclusions

4.1 The analysis performed by SL supports the application for an exemption from Section 19B of the Gas Act. The size of the storage facility is such that it is not necessary for the operation of an economically efficient gas market to necessitate third party access. Using the Ofgem Market Definitions for Flexibility, the Stublach facility Phase 1 on its own will hold less than 5% of market share. In addition, the market share of the GDFS Group within the flexibility market is, independent of the market definition selected, below 10% when tested against the Ofgem Market Definitions.