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Dear Ian,

Guidance on the Third Party Access Regulatory Regime for Gas Storage Facilities

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

The GB gas storage market is currently exposed to an unprecedented high level of policy and regulatory uncertainty. We believe that the project risk created by the current level of uncertainty is creating a hiatus in much needed investment in new and existing storage facilities. SSE and Statoil (UK) Ltd have consent to increase the storage capacity at our Aldbrough site beyond that currently under development. If developed in full, this would approximately double the amount of gas that could be stored, to around 700mcm. However, due to the high level of policy and regulatory uncertainty, we publically announced on 10th November 2010 that any investment decision on the development will be deferred while the UK government develops its policy on gas security.

In the interests of reducing this uncertainty (to some extent), we welcome the publication of this consultation and the open communication Ofgem has maintained with industry throughout the process. However, some of the concerns we have highlighted throughout this process, still remain.

SSE fundamentally oppose the introduction of any unnecessary additional regulation in an already highly competitive market. We are concerned that some of the proposed requirements or expectations Ofgem have put forward in this consultation document go beyond the requirements laid out in the Third Package. The GB gas storage market has evolved over the last 15 years to become the most transparent and competitive market in Europe, therefore imposing requirements or expectations upon GB SSOs that go beyond those faced by other European SSOs, is wholly inappropriate. Our two key areas of concerns are reserve pricing and multi facility use.

Reserve Pricing

As the Third Package does not stipulate a requirement for a reserve pricing methodology to be established by market players, we do not believe it is appropriate for Ofgem to do so in an already highly competitive market. We were disappointed to find that there was no specific consultation question on the proposal considering this is such a key investment driver.

We strongly oppose Ofgem's proposal that SSOs should set the reserve price for short run services at the short run avoidable cost. As stated in section 5.18. "Currently, facilities that are subject to the nTPA requirements in the GB market offer the majority of capacity as standard bundled units on a year ahead basis". Forcing an SSO to set a reserve price for the majority of its capacity which takes account of only the short run (one year) avoidable cost level, and does not include long run marginal cost or the intrinsic value of the capacity, will certainly create a hiatus in investment and may result in moving investment in existing and new built storage facilities from marginal to uneconomic.

As stated above, we oppose the introduction of any reserve pricing methodology. However, if Ofgem believe one must be introduced, we believe that the reserve price for both short run service and long run services, should be set to reflect the long run marginal cost or intrinsic value.

Multi Facility Use

SSE do not support Ofgem's expectation that all of an SSOs storage facilities will to be subject to the same regulatory arrangements if the SSO offers services that utilise the storage capacity of those facilities. Doing so will stifle the development of innovative storage products.



Ofgem have indicated that the expectation has arisen as it is assumed that it would be difficult for an SSO to demonstrate that the maximum technical capacity has been offered to the market. We believe this assumption is incorrect as an SSO could readily demonstrate that the total capacity offered to the market is at least (in aggregate) equal to the maximum technical capacity of the nTPA facility. For example, if SSEHL were to offer services that utilise the storage capacity of both Hornsea and Aldbrough, SSEHL would be able to demonstrate that the capacities offered to market (deliverability, injectability and space) would be at least equal to the maximum technical capacity of Hornsea.

I hope that our comments are 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 Rattey
Regulation Analyst

Annex: Consultation Question Responses

Chapter 3

1. Should pivotal gas volume be used when assessing SMP? If no, please explain why.

SSE welcome Ofgem's preliminary view to assess SMP using a hybrid approach as we agree that due to the complexities of the gas market, no one measure in isolation is sufficient to accurately assess SMP. For example, solely relying on pivotal gas volume as an assessment criteria would not allow Ofgem to accurately assess an SSO who operates its facility/s as a purely trading vehicle, and consequently may have more of an incentive than a vertically integrated SSO to raise prices above a competitive level, as it has no onward supply chain which could be negatively impacted by such an increase.

However, the information provided within the consultation document is insufficient to allow SSE to provide detailed comment on whether the use of pivotal gas volume as one of the SMP assessment criteria is appropriate. For example, it is not clear whether the amount of supply is based on contractual or physical flows, or committed or uncommitted gas. We request that, in order to enable industry to provide informed comment, and consequently allow Ofgem to make an informed decision, Ofgem conduct a follow on consultation which includes the following key information: a detailed explanation as to how the analysis will be conducted; a clear market definition; the assumptions which will be used; and full details of the factors which will be taken into account. Such factors could include: upstream gas production on a UKCS, EU or global basis; gas trading position; hedging strategy; the level of inflexible and flexible gas supplies available in the UK, EU or global market; the period/s to which the analysis relates; whether different gas sources/demand are given different weightings; and customer demand and/or portfolio demand in the UK, European or global market. We would also request that to improve transparency, Ofgem include at least two fully worked examples of how the SMP assessment would be conducted by Ofgem in the consultation.

It should be noted that without this level of clarity, in addition to not being able to provide informed comment on the assessment methodology, operators will be unable to assess whether they are regarded by Ofgem as having SMP. Therefore, operators will be unable to assess which SMP good practice safeguards suggested in the guidance document, they are expected to have in place.

In addition to the above, we request that Ofgem provide clarity as to how the SMP assessment methodology will interact with the current nTPA exemption assessment methodology. It is vital that Ofgem clarify whether the SMP assessment methodology will replace the nTPA exemption assessment methodology or will remain as two separate methodologies, to avoid further investor confusion and uncertainty.

2. Is the proposed figure of ten per cent of pivotal gas volume an appropriate threshold for defining SMP? If no, what is an appropriate threshold?

Given the ten percent figure is a figure calculated by Ofgem, it would be helpful to have sight of the analysis to be able to provide comment. We note other values and methodologies are used by other regulatory authorities.

3. Is it appropriate to also consider market outcomes to assess whether a market player may have SMP at lower levels of pivotality?

In the interests of providing stability in the market and certainty to investors and SSOs, SSE believe that there should be no ambiguity about whether or not an SSO would be deemed to have SMP regardless of how the threshold is set or at what level. This will provide assurance to SSOs that the good practice safeguards that they have in place, are appropriate for their facility.

4. Are there any additional factors that should be used when considering if a market participant has SMP?

As noted above, until Ofgem have provided greater detail of their assessment, we are unable to provide comment on what additional factors should be included.

Chapter 4

1. What factors should be taken into consideration when defining the maximum capacity of a group of facilities?

SSE do not support Ofgem's expectation that all of an SSO's facilities will be subject to the same regulatory arrangements if the SSO offers services that utilise the storage capacity of multiple facilities, as doing so will stifle the development of innovative storage products.

Ofgem have indicated that the expectation has arisen as it is assumed that it would be difficult for an SSO to demonstrate that the maximum technical capacity has been offered to the market. We believe this assumption to be incorrect as an SSO could readily demonstrate that the total capacity offered to the market is at least (in aggregate) equal to the maximum technical capacity of the nTPA facility. For example, if SSEHL were to offer services that utilise the storage capacity of both Hornsea and Aldbrough, SSEHL would be able to demonstrate that the capacities offered to market (deliverability, injectability and space) would be at least equal to the maximum technical capacity of Hornsea.

2. What concerns, if any, do market participants have with Ofgem's preliminary views on capacity allocation?

Although auctions are used to allocate primary capacity at Hornsea, as the Third Package does not stipulate a requirement for a specific capacity allocation process, we do not believe it is appropriate for Ofgem to introduce unnecessary requirements in an already highly competitive market.

What concerns, if any, do storage users have with the use of allocation mechanisms other than auctions to allocate capacity, particularly standard services?

SSE believe that the existing processes which are used by all existing allocation mechanisms (such as auctions and bilateral agreements) are sufficiently objective, transparent and non discriminatory.

3. Does the use of auctions provide market participants with sufficient safeguards that any market player with SMP will provide standard services to the market on a non discriminatory basis? What other measures/safeguards in relation to how any market player with SMP allocates capacity could be considered?

The current safeguards in place are sufficient to ensure that all market players provide standard services to the market on a non discriminatory basis. We believe it would be inappropriate for Ofgem to introduce unnecessary requirements in an already highly competitive market.

4. Do market participants consider that the prevailing anti hoarding arrangements currently in place at GB storage facilities that are subject to the TPA regime are appropriate and compatible with the requirements of the Gas Regulation? If no, please explain why.

Yes.

5. Do market participants consider that the mix of interruptible and firm storage services is appropriate and compatible with the requirements of the Gas Regulation? If no, please explain why.

Yes.

6. Do market participants consider that the existing arrangements for the secondary trading of storage capacity are appropriate and compatible with the requirements of the Gas Regulation? If no, please explain why.

Yes.

Chapter 5

1. What levels of consultation should SSOs undertake when developing main commercial conditions for the first time and when proposing amendments to the standard terms and conditions?

SSE agree that the extent to which SSOs are required to consult when developing or making changes to their main commercial conditions should depend upon the extent of changes introduced. Minor changes should only require customer notification. However, the establishment of or fundamental alteration to main commercial conditions should require full industry consultation.

2. Are there aspects of an SSO's main commercial conditions where small changes are likely to have a significant impact on system users?

No.

- 3. Should SSOs be expected to formally consult or test the market before changing existing services or offering any new services to the market? If no, please explain why.**

No. As the Third Package does not stipulate a requirement for consultation before the introduction of new services or alteration to existing services, we do not believe it is appropriate for Ofgem to introduce unnecessary requirements in an already highly competitive market.

It should also be noted that such testing would be a highly unnecessary burden upon SSOs and customers, as the key driver behind the introduction of new services or alteration to existing services is in fact customer demand.

- 4. Should SSOs be expected to offer a minimum threshold of capacity on a short term basis? How should SSOs determine the minimum proportion of capacity that should be sold on a short term basis?**

As the Third Package does not stipulate a requirement to offer a minimum threshold of capacity on a short term basis, we do not believe it is appropriate for Ofgem to introduce unnecessary requirements in an already highly competitive market.

- 5. Should SSOs be expected to also offer unbundled capacity as part of their standard services? Please explain your views.**

No. We believe that an expectation to offer unbundled capacity would highly inappropriate as there is little customer demand for such a product, and it is likely to result in stranded capacity.

Chapter 6

- 1. What factors should Ofgem take into consideration when assessing a market player's flexible gas requirements and, in particular, need for storage services?**

When assessing a market player's requirement for flexible gas, Ofgem must take into account the player's supply and portfolio demand chain.

On the supply side, factors taken into consideration should include: upstream gas production which enters the UK or any interconnected markets such as Scandinavia or Europe; long term flexible gas contracts or contract which have an element of flexibility built into them; and LNG contracts in the UK, EU or global market.

On the demand side, factors taken into consideration should include: industrial and commercial fixed and interruptible customer demand; small to medium enterprise customer demand; domestic customer demand; and internal demand (generation portfolio demand, sites etc.).

Chapter 7

- 1. Do SSOs provide sufficient information on the services they offer and the terms and conditions of access? Is any further information required? Are there any improvements that could be made to how information is provided by SSOs?**

SSE believes that sufficient information is currently provided.

- 2. Do SSOs provide sufficient information on the maximum capacity and the level of utilisation? What further information is required? Are the current timeframes for providing this information appropriate?**

Yes.

- 3. Should SSOs publish the information required under section 19(4) on their websites or should NGG undertake this role for all SSOs?**

In the interests of efficiency and ease of access to the information, we believe NGG should undertake this role.