



SOUTH HOOK
LNG TERMINAL COMPANY LTD

BY RECORDED DELIVERY & EMAIL

Economist, Markets
OFGEM
9 Millbank
London SW1P 3GE

ATTN: Francesca Caputo

Date: 25 November 2011

Our Ref: SHLNG/CM/C/112

Dear Ms Caputo,

Subject: Consultation on the regulated Third Party Access regime for Liquefied Natural Gas facilities in Great Britain

Please find attached a submission from South Hook LNG Terminal Company Ltd. ('South Hook LNG') on the above consultation.

As operator of the largest LNG receiving terminal in Europe, South Hook LNG welcomes the opportunity to contribute to this important debate though, as an exempt terminal, South Hook LNG is not directly impacted by the matters under discussion.

In summary, South Hook LNG welcomes Ofgem's acknowledgement that there are no plans to change the regulatory basis under which exempt terminals such as South Hook LNG operate as a consequence of this consultation on guidance for Third Party Access in regulated facilities.

South Hook LNG is also of the view that there are sound, fundamental reasons why Ofgem might expect secondary capacity trading and use it or lose it mechanisms to have been used so little to date.

In a European context, South Hook LNG notes and welcomes the findings from CEER's study on CAM, CMP & anti-hoarding mechanisms in European terminals. This study found no evidence of capacity hoarding in EU LNG terminals and that shippers responding to the CEER public consultation were generally satisfied with the existing CAM and CMP terms used.

However, compliance with existing TPA legislative provisions across Europe is relatively modest. An initial emphasis on securing such compliance before further changes are considered should be made a priority by Ofgem in its work through CEER.

If you have any questions or comments, please do not hesitate to contact me

Yours sincerely,

Imran Juma
Commercial and Regulatory Affairs Manager

**Consultation on the regulated Third Party Access Regime
for Liquefied Natural Gas facilities in Great Britain**

Response from South Hook LNG Terminal Company Ltd.

Introduction

South Hook LNG Terminal Company Ltd. ('South Hook LNG') is the largest LNG receiving terminal in Europe whose shareholders are subsidiaries of Qatar Petroleum (67.50%), Exxon Mobil Corporation (24.15%) and Total SA (8.35%). The terminal is part of the Qatargas 2 venture, the world's first fully integrated LNG value chain, which comprises production facilities in the North Field in the territorial waters of the State of Qatar, two on-shore liquefaction trains and a fleet of LNG ships in addition to the receiving terminal located in West Wales.

The terminal began full commercial operations in April 2010 and has a total processing capacity of 15.6 million tonnes per annum (mtpa) of LNG and is capable of delivering up to 21 billion cubic metres (bcm) per annum of gas into the UK National Transmission System (NTS). Currently, the maximum capacity of the terminal is constrained by limitations on the capacity of the NTS.

In calendar year 2010, South Hook LNG regasified 124,922 GWh of natural gas to its users for subsequent sale into the UK market. This represented 61.3% of the UK's total LNG imports, 21.5% of the UK's total natural gas imports, 30.2% of the UK's net natural gas imports and 11.4% of total UK natural gas demand.

In the gas year ended 30 September 2011, the terminal operated at a capacity utilisation of 91.3% (as measured against the constrained capacity of the NTS) – the highest utilisation of any on-shore terminal within the European Union.

South Hook LNG has been granted exemption from regulated Third Party Access for a period of 25 years from the start of commercial operations. This exemption enabled 100% of the terminal's primary capacity rights to be purchased by South Hook Gas Company Ltd ('South Hook Gas'), a UK joint venture of Qatar Petroleum Gas Trading (QGII) Limited (70%) and ExxonMobil Qatargas (II) Limited (30%). Third Parties ('Additional Users') can purchase secondary terminal capacity rights from South Hook Gas through a non-discriminatory and transparent process. South Hook LNG, through the terms of the Terminal Access Code, facilitates the trading of capacity rights with other Additional Users.

Where terminal capacity is likely to remain unused, an auction is held and administered by the terminal operator. Such capacity is advertised on the South Hook LNG website 14 days ahead of a berthing slot being available and is auctioned over 4 days ending 10 days before the date of the berthing slot. Gas is redelivered over a 7 day period. Potential users are free to apply via the terminal's Electronic Bulletin Board.

Overview of the South Hook LNG response to the consultation

As mentioned above, South Hook LNG was granted exemption from regulated Third Party Access (rTPA) for a period of 25 years. South Hook LNG notes with satisfaction that OFGEM confirms none of the matters raised in the current consultation will directly impact the terminal's rTPA exemption. Exemption from rTPA was a *sine qua non* for the shareholders to proceed with the significant investment needed to build the terminal and to secure the necessary finance. Any retrospective change to the regulatory consent regime would be a major concern for the terminal and its

shareholders and moreover would create uncertainty for potential future investors in significant UK gas infrastructure.

South Hook LNG notes that the consultation document is primarily aimed at investors that have yet to invest in Great Britain but who may be considering operating under the rTPA regime. Not all the questions posed, therefore, are directly relevant to South Hook LNG. However, Ofgem raises some questions in the consultation that have a relevance to exempt terminal operation and South Hook LNG provides some views below in that regard.

Responses to the Consultation Questions

Question 1: What level of consultation should an LNG system operator undertake when developing its main commercial conditions for the first time or when proposing amendments to its standard terms and conditions?

South Hook LNG has no views to offer on this matter.

Question 2: Should an LNG system operator be expected to formally consult or test the market before changing existing services or offering any new services to the market? If no, please state your reasons.

South Hook LNG has no views to offer on this matter

Question 3: Do market participants have any concerns with our preliminary views on capacity allocation?

South Hook LNG is a member of Gas LNG Europe ('GLE'), part of the wider Gas Infrastructure Europe ('GIE') trade association. As an active participant in the GLE's activities, South Hook LNG has followed the Capacity Allocation Mechanism ('CAM') and Congestion Management Principles ('CMP') debate closely. South Hook LNG has been working with the Council of European Energy Regulators ('CEER') since 2009.

South Hook LNG notes with satisfaction the responses to the recent European Regulators' Group for Electricity and Gas ('ERGEG') study on CMP and anti-hoarding mechanisms. We note that shippers surveyed mainly expressed satisfaction with the CAMs and CMPs applied. We also note that CEER acknowledged that the diversity of CMP's applied at terminals across Europe could be explained by particular characteristics and technical constraints, both in LNG facilities and downstream gas markets. South Hook LNG considers that the harmonisation of terms across Europe is not necessary or possible today, should certainly not be a priority for European regulators, but should be an evolution driven by sharing of best practice and the operation of competitive markets.

Question 4: Can the Use It or Lose It (UIOLI) arrangements implemented by the LNG system operators in GB be improved to ensure greater utilisation? What lessons can we learn from current models to encourage greater use under an rTPA regime?

South Hook LNG has published a guide on its website to assist those parties seeking access to secondary Terminal Capacity at the Terminal. This guide describes the facilities available at the Terminal, the nature of the secondary Terminal Capacity a party may access and the different methods of accessing such capacity. It also sets out the process by which a party may become an Additional User at the Terminal and a step-by-step guide of how to participate in a capacity auction, should an Additional User decide to access secondary Terminal Capacity in this way. The rules for access and use of the Terminal are contained in the Terminal Access Code (TAC).

Additional Users can purchase secondary Terminal Capacity from SHG as a Base User, and hold such capacity, in the form of a South Hook Bundle (or SHB). Once an SHB has been created and purchased by an Additional User, it can be sold to other Additional Users.

As outlined above, utilisation of the South Hook LNG terminal is at an effective rate of 91.3% when current NTS capacity constraints are taken into account. All of this capacity has been utilised by South Hook LNG Gas as the primary capacity holder. Measures to further improve capacity utilisation at the terminal are therefore simply not an issue.

More generally, it is a truism that demand for UIOLI capacity will be highest when demand for LNG import capacity is highest. So far in the UK, this has not been the case for anything other than very limited periods of peak demand. Though declining, UK Continental Shelf (UKCS) production still has the capacity to supply around 43% of current UK demand. Current import capacity of 156 bcm/year comfortably exceeds demand of 98 bcm/year. LNG represents some 56 bcm of the total import capacity. In this scenario, it is hardly surprising that demand for UIOLI capacity has been modest and that it may be premature to seek 'what lessons can we learn from current models to encourage greater use under an rTPA regime'.

Question 5: Do market participants have any views on why secondary capacity trading has been used so little? Is access to unused capacity happening through mechanisms other than secondary trading and/or UIOLI arrangements?

As outlined above in the response to Question 4, the circumstances currently prevailing in the UK natural gas market make it unlikely market participants would undertake high levels of secondary capacity trading.

In addition, it is important to remember that, almost uniquely in the EU, the UK market is highly liquid, with much trading around the National Balancing Point (NBP). Options other than secondary capacity trading or utilising UIOLI arrangements therefore exist for UK market participants to balance their portfolios.

Question 6: Are there any mechanisms that could be established to facilitate greater use of secondary trading arrangements?

There are a number of ways by which an Additional User can access secondary South Hook LNG Terminal Capacity:

- by agreeing to purchase an SHB with the Base User;
- by participation in an auction conducted by the Terminal Operator (as and when secondary Terminal Capacity is available in defined timescales); and
- by agreeing SHB transfers with other Additional Users.

The Base User can also offer LNG processing services to others for periods when it is not using all the Terminal Capacity for its own business needs. This is an alternative arrangement for third party access that would not require the interested LNG supplier to hold terminal capacity.

From the responses to Questions 4 and 5, it is apparent that South Hook LNG is of the view that current market conditions provide no evidence that current secondary trading arrangements are not working satisfactorily. South Hook LNG is of the view that with significant spare import and storage withdrawal capacity the market is providing little incentive to secondary capacity trading and in any event our experience is that potential users may prefer to gain access through alternative

mechanisms as described. Our role as LNG facility operator is to facilitate arrangements to assist users and we will remain responsive to such requests where they are made directly to us.

Question 7: In addition to the information detailed [in Chapter 3], is there any further information that LNG system operators should make publicly available?

There is always the possibility that providing public information to answer every conceivable request risks 'information overload' for many potential users. South Hook LNG is convinced that a more pragmatic approach is more appropriate with Electronic Bulletin Boards etc. identifying clear points of contact from which further information on specific matters can be sought. This approach has worked well for South Hook LNG in the past.

In addition, South Hook LNG is actively involved in, and fully supports, an initiative by GLE which will facilitate access to the necessary information for accessing LNG terminals. This will take the form of a common template installed on a relevant page of each system operator's website.

Question 8: To what extent do you consider that market participants will be able to observe non-compliance with the legislative requirements by an LNG system operator?

South Hook LNG has no experience that non-compliance is an issue for Additional Users of capacity. We believe the information provided on our Website, Bulletin Board and in supporting documentation is accurate, comprehensive and fully meets the requirements of our TPA exemption. Where there have been questions or comments, these have been swiftly and effectively handled.

The key to meeting the legislative requirements is good governance. South Hook LNG is confident of the effectiveness of its procedures and systems in ensuring that its Users' confidential information is kept confidential.

Question 9: Taking into account your answer to Question 8, what (if any) additional information to that set out in [Chapter 3] should LNG system operators provide to the Authority?

Given the response to Question 8, it follows that South Hook LNG see no need for further information disclosures to the Authority.

The new common Transparency template will make it easier for new users and regulators to gain a better understanding about the access arrangements at each terminal.