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BY EMAIL

Ofgem
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Attention: Francesca Caputo, Economist, Markets

Consultation on National Grid Grain LNG's application for exemption from regulated third party access for Isle of Grain phase 4

Thank you for the opportunity to comment on the above consultation.

South Hook Gas (SHG), as part of the Qatargas 2 value chain, manages and owns the capacity at one of Europe's largest LNG terminals, the South Hook LNG terminal located at Milford Haven in South Wales. Commercial operations commenced in April 2010 and since then South Hook Gas has supplied natural gas into the UK National Transmission System (NTS) every day.

An exemption from regulated Third Party Access (rTPA) was awarded to South Hook LNG Terminal in November 2004 which allowed South Hook Gas to purchase all the primary capacity in order to process LNG from Qatargas 2. The award of this exemption was considered essential for the Qatargas 2 project, and a necessity in order to secure the finance needed to build the terminal.

Answers to specific questions:

Question 1: Do you agree that the requested exemption should be granted subject to the three conditions set out in this letter? Please explain your reasons.

In the absence of evidence to the contrary, SHG strongly believes that existing anti-hoarding measures at Grain and elsewhere in the UK are effective and we would caution against placing further regulatory burdens on the market. Ofgem should take care to ensure that the regulatory environment is balanced to meet the needs of both primary capacity holders and suppliers of LNG with long term contracts in place, and those wishing to participate in the spot market. For instance, increasing the time period within which spare capacity should be auctioned under the UIOLI process could cause uncertainty to the primary capacity holder who has invested in long term capacity precisely so that they can be certain capacity is available when they need it. Being forced to give up capacity too early means the long term suppliers may look to other markets and the impact could be a reduction in LNG supply.

Question 2: Do you consider that capacity that becomes un-contracted upon expiry of the initial contracts should be subject to rTPA arrangements? Please explain your reasons.

The UK is an efficient and liquid market and those who require access to capacity are easily able to do so. The current arrangements to prevent anti-hoarding are sufficient and we submit that Ofgem should allow market forces to regulate the sale of unused capacity rather than enforce unnecessary rTPA arrangements.

Question 3: What are your views on the competition analysis undertaken by Frontier? In particular, do you consider that they have sufficiently extended the analysis into the future to support the conclusion that no competition concerns from the Grain 4 exemption would arise?

No comment

Question 4: Do you consider the three levels of anti-hoarding arrangements which would apply to Grain 4 are sufficient to ensure that any unused capacity will be offered to third parties? What improvements (if any) would you like to see GLNG make?

The three levels of anti-hoarding arrangements cited by Grain are sufficient to ensure that interested parties are able to access terminal capacity at Grain if desired. These arrangements and similar are already in place at Grain and other UK terminals, and there is no evidence to suggest they are ineffective. SHG does believe however, that offering a variety of capacity products to the market will foster utilisation of unused capacity by third parties. As such, SHG offers a suite of contracts which facilitate flexible capacity trading and has already entered into a long term services agreement wherein access to a portion of its capacity rights has been contracted for a period of 25 years.

It is important to recognise that the LNG market is global and LNG will be attracted to the highest value markets. The low level of utilisation at some of the UK terminals is not a result of anti-hoarding arrangements being ineffective, but simply a function of supply and demand. Available import capacity in the UK outstrips requirements, and that, coupled with higher prices elsewhere, means that demand for capacity has been low. Having three levels of anti-hoarding arrangements (with UIOLI being the 'back stop' to ensure capacity is offered to the market), is more than sufficient, especially considering the present market environment. We do not believe therefore that any improvements need to be made to the current arrangements either at Grain, or in the UK more generally.

Question 5: Is there any information currently not provided by GLNG that would facilitate the trading of unused capacity through any of the three mechanisms available? Please provide details of the information that you would like GLNG to make available.

See answer to Question 6

Question 6: Do you consider that GLNG and primary capacity holders at Grain need to provide more information on secondary capacity products or do you consider that contact details of primary capacity holders are sufficient?

SHG supports information transparency and understands why Ofgem would believe that it would be beneficial if greater transparency on available secondary capacity was provided, that the terms and conditions for the products should be standardised, and that a simpler process for obtaining capacity introduced. It should be noted however, that releasing capacity is a complex process as there are many operational variables at play that need to be considered. Indeed, standardising products can actually limit the capacity that is made available. SHG has simplified the process for obtaining capacity at the SHLNG terminal by signing master agreements in advance with interested parties. Having terms and conditions agreed in advance should allow parties to swiftly contract for capacity when required. SHG routinely looks for spare capacity in their schedule and informs master agreement signatories concurrently of any availability. SHG endeavours to meet customer requirements with respect to operational parameters, rather than only releasing standard products.

We have found that this flexible approach benefits all parties and we strongly believe that flexibility, rather than standardisation, is the key to not only ensuring unused capacity is released to the market but also to increasing utilisation at the terminals. Furthermore, we strongly believe that additional information should only be provided if it is demonstrably beneficial to improving access and does not conflict with existing commercially sensitive and/or confidential arrangements and in the process impact the commercial positions of capacity holders thereby actually discouraging, rather than encouraging, utilisation of capacity.

Question 7: Do you consider that anti-hoarding arrangements at the Isle of Grain terminal might need to be improved to reflect the possible increasing importance of LNG as a route to market in the future? Should they be subject to regulatory approval and periodic review?

As previously stated, we do not believe there is any evidence to suggest that current anti-hoarding arrangements both at Grain and elsewhere in the UK are ineffective. LNG destinations will continue to be decided by price and LNG will be routed to more profitable regions. Any assessment of utilisation should be measured against global market conditions and until such time as demand for capacity in the UK increases there will be limited opportunity to test the anti-hoarding arrangements. It seems therefore premature, in the absence of any 'lessons learned', to reassess the arrangements. There also seems little point in a periodic review or a need for regulatory approval until such time as the market requires it.

We hope that you find these comments helpful.