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Dear Paul

Gazprom Marketing & Trading Response to “User Commitment for National Transmission System Quarterly Entry Capacity – Initial Impact Assessment on modification proposals”

Gazprom Marketing and Trading Limited (“Gazprom”) welcomes the opportunity to comment upon Ofgem’s Impact Assessment (IA) for modification proposal UNC 246 (“Quarterly NTS Entry Capacity User Commitment”) and its alternatives (UNC 246A and UNC 246B). In particular, Gazprom appreciates the IA covering licence issues which were outside the remit of the UNC Review Group. Gazprom believes licence changes could provide a more effective and efficient means of ensuring that there are robust credit arrangements in place for the protection of customers.

Gazprom believes that it is inevitable that any additional securitisation costs incurred by shippers will eventually be paid by consumers, therefore, it is essential that the costs incurred are proportionate to the risks faced by the industry. The IA indicates a large decrease in risk of default would be required for a positive cost-benefit analysis to be derived. The range of percentages are high for UNC 246 (2.6-8.2%) and UNC 246A (1.5-5.5%), whilst UNC 246B (0.5-2.4%) seems attainable.

A major concern for Gazprom is the risk of over-securitisation being introduced through these proposals, leading to a whole new set of challenges for the UK gas industry. In particular, and as a consequence of the retrospective nature of UNC 246 and UNC 246A, shippers may discard their existing QSEC holding. The IA states “there is some £725m of capacity that could be considered to fall into this

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category”; a significant sum to be recovered by all shippers through the SO or TO commodity charges.

Gazprom would like the current defect of the long lead time between a user committing to buy long term NTS entry capacity and underpinning this commitment to be addressed through UNC 246B. This particular proposal introduces securitisation based on future QSEC bookings, avoiding the perverse effects of retrospective changes. The IA notes Ofgem’s particular concern of proposal UNC 246B potentially discriminating in favour of current market incumbents. Gazprom believes that the difference in treatment created by UNC 246B can be justified through the observations made in Review Group 221. The Group concluded that the risk of credit default is higher amongst those shippers entering the gas market at a single entry point when compared with the existing shippers that hold long term entry capacity at multiple ASEPs. The multiple ASEP users are currently deterred from defaulting through the prospect of losing their capacity holdings at the numerous ASEPs. This penalty is a proportionate deterrent against the likelihood of credit default. In the instance where a shipper is delivering against a single obligation from a single ASEP, the cessation of that obligation would allow the relevant shipper to default against the capacity obligation without fear of further penalty. Gazprom believes that the additional securitisation required under modification UNC 246B would reflect the additional risk imposed by a single site users, therefore, creating a level playing field amongst new and existing shippers. It is also arguable that shippers might have booked different levels of capacity had they known they would need to provide security for it, hence the retrospective nature of some of the proposals could be seen as unfair to them.

Gazprom believes licence changes would facilitate the same end goal of protecting consumers from the effects of credit default by a shipper. In the event of a shipper defaulting, Gazprom would like to suggest an automatic trigger of the reopening of the licence parameters. For example, where capacity has been allocated through the QSEC auction NGG’s allowed revenue has been increased i.e. by £100m over 5 years even though only £30m has been spent by NGG. Under the current rules £100m will be funded by the industry and customers. This key licence change permits NGG to recoup the £30m, whilst removing the industry’s 5 year liability for £100m. This automatic process removes the uncertainty associated with whether an Income Adjusting Event (IAE) will be raised by NGG, currently the only permitted party. The automatic trigger also avoids having to introduce conditions relating to when an IAE can be raised if the provision was extended to shippers. In the IA, the Authority has highlighted their concern regarding frequent adjustments to the allowed revenue, as a result of shippers being able to request an IAE.

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In addition to the introduction of the automatic trigger of the reopening of licence parameters, the current mechanistic triggering of the revenue stream needs to be revised. Gazprom supports introducing a phased release of the revenue stream, ensuring NGG only recoups revenue consistent with its expenditure profile. The introduction of greater flexibility within the revenue stream is beneficial for both users of the NTS and end consumers through removal of the risk of NGG receiving windfall gains.

To conclude, Gazprom believes it is important to pursue the suggested licence changes, i.e. automatic reopening of licence parameters and phased revenue stream to complement the credit regime, even under the existing regime. However, Review Group 221 highlighted the inappropriate length of time between a user committing to buy QSEC and the user financially supporting this commitment. This industry concern became of greater importance when considering future potential parties being single site users. Gazprom believes UNC 246B addresses this particular concern without the adverse impacts of retrospective changes introduced through UNC 246 and UNC 246A.

I hope the above comments are useful. If you have any queries please do not hesitate to contact me on ++ 44 20 8614 3036 or at alex.barnes@gazprom-mt.com.

Yours sincerely,

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