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Dear Tim,

Consultation Response: Code Modification Proposal No. 0120, “Introduction of an SO Commodity Charge for NTS Storage Exit Flows” & NTS GCM 03, “Introduction of an SO Commodity Charge for NTS Storage Facilities”

E.ON UK does not support this proposal in its current form. We consider that Modification Proposal 0120 is not wholly cost-reflective. We believe that there is a need for “netting-off” of input and offtake quantities, which the proposal as stated currently, does not provide for. It is our view that this SO commodity charge needs to be based on *actual* net physical offtake flows rather than contractual offtake allocations.

We have additional concerns that the level at which the commodity charge is levied raises a possible question of discrimination between NTS Users. We also believe that this Modification Proposal could inhibit the overall market efficiency of gas storage. These points will be considered with more detail in our response, below.

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Impact on Gas Storage Competitiveness

We believe that the changes put forward in this Modification Proposal could add to the cost of utilising gas storage facilities and could inhibit the future development of, and investment in, storage facilities in the UK. To this extent we consider that an additional charge for the use for storage could detract from market effectiveness and competitiveness. Storage is an important part of the Gas Transmission system and its effective use supports security of supply. If this Modification Proposal is approved, we would expect any future Commodity price changes, post-April 2007 to reflect the value and benefits to be gained from storage facilities and not to inhibit its development.

The Relevant Objectives

A11.1 (c) the efficient discharge of the licensee's obligations under their licence

It could be considered that this proposal does not further the Relevant Objective 1 (c). In treating offtake points differently in terms of charging, this Modification Proposal could be considered discriminatory.

We are able to see the logic behind the reasons cited by National Grid for excluding certain elements of the commodity charge and agree in principle with the exclusion of compressor gas and operating margin costs. We would contend, however, that it is not entirely clear whether this is done simply to avoid double counting (in the case of shrinkage costs) or to potentially treat NTS Offtakes in different ways (in the case of 'Internal Costs' – a "portion of the costs should be attributed..."¹). Although we have no objection to levying different commodity rates on Storage Operators to other Users, we would question whether this is consistent with Ofgem's previously stated views on NGG's licence and Gas Act obligations to avoid any undue discrimination in its transportation business. For example, the proposed Enduring Offtake arrangements are based on the assumption that all NTS Offtake Users should be treated the same. It is our contention that this is not appropriate, as stated in Modification Proposal 116a:

E.ON UK has obtained a legal view from counsel which amongst other matters concludes;

"Proper application of the non-discrimination provisions;

- Requires answering two questions: (a) are the users or classes of user materially comparable; and (b) is there a valid reason, or objective justification, for any difference in treatment.*
- May not only permit but actually require that material differences between classes of user be reflected in appropriately different treatment."*

E.ON UK believes the various classes of NTS User are not materially comparable, that there are valid reasons for their different treatment and as such different

¹ NTS GCM 03, 'Introduction of an So Commodity Charge for NTS Storage Facilities', page 3

treatment is appropriate.

*Gas DNOs are subject to price control regulation, whilst shippers who ship gas to direct connects, **storage facilities**² or export gas through interconnectors operate in the competitive market. Shippers are not in a position to be able to fairly 'compete' with DNs for access rights, nor are they necessarily able to provide long term commitments in the same way as such monopoly network businesses whose income stream it ultimately secured through the price control process. In addition, the 'connected facilities' themselves are also subject to a variety of different licensing and exemption regimes reflecting their different circumstances.*

Our view described above, therefore leads us to conclude that Modification Proposal 0120 in its current format would support our argument for validly treating NTS Offtakes differently, through positive discrimination, by levying a reduced commodity charge rate on storage flows.

If you have any questions or queries regarding this response, please do not hesitate to contact me.

Yours sincerely

Richard Fairholme
Trading Arrangements
E.ON UK

² Our bold highlighting