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Jan Gascoigne
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Thursday, 23 July 2007

Dear Jan,

Re: The Review of the “Incremental Entry Capacity Release (IECR) Methodology Statement” 2007 and Consultation on “The Entry Capacity Substitution Methodology Statement”.

Statoil UK Ltd (STUK) has previously commented on the proposed Entry Capacity Substitution Methodology Statement, highlighting a number of areas where the proposals require further consideration to be structured in a way to allow the economic and efficient use of the network. As a major importer of natural gas into the UK, STUK is interested in the maintenance of a stable, efficient and economic entry capacity regime. STUK has considered the alternative proposals as suggested for implementation within the Incremental Entry Capacity Release process. None of these options strengthens the original proposals in relation to the concerns raised. STUK believes all the alternative proposals create new issues and problems and are not suitable for implementation.

Option 2. Extension of transfers.

As well as suffering from all the problems previously raised with the original proposal and the disadvantages raised by NGG this proposal has a number of major problems which need to be addressed.

It is unclear how this proposal could work efficiently in practice and how competing requests for capacity would be allocated. As the result for an unsuccessful applicant in a competition between two users requiring capacity for a single quarter would be receiving no capacity the



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process would need to be considered carefully to ensure fair an economic allocation. The original proposal (Option 1) does not suffer this problem as once the user passes the IECR test the physical capacity would be provided if substitution cannot be achieved.

As well as creating constantly shifting baselines which could lead to increased volatility in the capacity prices from year to year the proposal would open a route for the deliberate distortion of the capacity market. This proposal if implemented would allow a user to purchase capacity in one location to deliberately create scarcity in another location for a short period of time.

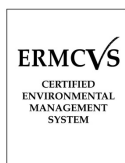
STUK raised concerns under the original proposal (Option 1) that this proposal may see users purchase capacity for a single month to 'lock out' all the capacity at a particular ASEP thus ensuring it cannot be transferred. This proposal could make that situation worse. In certain ASEPs users could deliberately trigger the IECR test for a single quarter to 'lock out' all the capacity in that zone ensuring none of the capacity in the zone was available for substitution in the long term. It is essential for producers that there is a clear transparent capacity system to allow long-term investments and commitments to be made.

Options 3&4. Lower NPV Test and Lower User Commitment

STUK question how realistic these proposals really are. Both these proposals share the same fundamental flaws as the original proposal and both magnify those flaws as they lower the requirements required to pass the IECR test. Neither appears sufficiently developed and neither considers how it relates to the AMSEC auction process, the Transfers and Trades process (enduring regime to be introduced prior to Oct 2008) and the short-term capacity markets.

Having a lower NPV test for incremental capacity provided through substitutions under Option 3 would be extremely difficult to achieve as transfer rates would be ex-ante and therefore unknown at the time of the QSEC auction process. It is unclear how competing requests for capacity would be allocated in a fair and economic manner given that depending on the manner in which the requests are fulfilled, each would be treated differently. It is also unclear that a lower NPV test or user commitment would lead to the economic and efficient distribution of entry capacity within the network. At the time of the auction the location and amount of unbooked capacity would not be known and it would be impossible therefore for users to bid with visibility of the test to be applied.

STUK would like to further understand whether Options 3 and 4 could be considered to create discrimination between users. It could be argued that those users who pass the existing NPV test for IECR and who make the user commitment necessary to gain capacity rights under these proposals will be treated differently from users who benefit from substituted capacity. As both parties receive the same product (incremental capacity) it is unclear what the rationale would be to treat the recipients of this same product differently. As these differences may provide users with a commercial advantage or disadvantage it is of paramount importance that this issue is carefully considered prior to any implementation.



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Conclusion

STUK raised a major concern with the original proposal that as defined it could lead to uneconomic allocation of entry capacity in the mid to long-term and that this could lead to uneconomic investment. STUK also highlighted the concern that this change could impact on the short-term capacity market and therefore the wholesale markets. Other parties have raised concerns that the current IECR and substitution methodology does not take into consideration the changing profile of the UKCS and NCS fields. Prior to any QSEC auction it is of vital importance that these concerns are considered, fully understood and addressed.

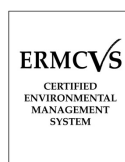
It is clear to STUK that along with the original proposal, neither Options 2, 3 or 4 are sufficiently developed to be implemented. STUK believe the implementation of any of these options would be premature in the current climate of change in the entry capacity regime with an enduring regime for transfers and trades likely to be implemented for October 2008. STUK suggest the regulator should postpone the introduction of these changes for a one year period allowing the industry to better prepare for their implementation and ensure the new regime is fully formed and workable.

STUK trust that our comments will be given due consideration and should you wish to discuss any aspect of this response further please contact me on the above number.

Yours faithfully

Richard Street*
Statoil (UK) Ltd

**Please note as this letter has been delivered electronically this letter is unsigned*



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