Deliberation

Deliberation of the French Energy Regulatory Commission (CRE) dated 14 January 2010 approving the open season procedure for the Fos Tonkin LNG terminal continuation project

The following Commissioners attended the meeting: Philippe de LADOUCETTE, Chairman, Michel LAPEYRE, Vice-Chairman, Maurice MEDA, Vice-Chairman, Eric DYEVRE, Hugues HOURDIN, Pascal LOROT and Emmanuel RODRIGUEZ, Commissioners.

The French Order dated 20 October 2009 approving the tariffs for the use of LNG terminals provides for the application of tariff visibility and investment incentive principles to LNG terminals "*for extensions of existing LNG terminals and new terminals, as long aswhere the increase in regasification capacity represents at least 20% of the infrastructure's initial capacity of the infrastructure and that newly created capacity is allocated using rules previously approved by CRE".* Elengy submitted the open season procedure for the Fos Tonkin LNG terminal continuation project, made up of the Information Memorandum (Appendix A) and Allocation Rules (Appendix B) to the French Energy Regulatory Commission (CRE) for approval.

Located in Fos-sur-Mer along the Mediterranean coast and operated by Elengy, the Fos Tonkin LNG terminal can handle Med-max LNG tankers transporting up to 75,000 m^3 of liquefied natural gas (LNG).

The terminal currently has regasification capacities of 7 Bcm/year. Capacity is set to drop to 5.5 Bcm/year once the Fos Cavaou terminal is commissioned. Its commercial operation is planned until October 2014. No capacity has been marketed after this date.

After 2014, two of the three tanks from Fos Tonkin LNG terminal could be dismantled and the facilities will be refurbished in order to ensure a minimum send-out capacity of 3 Bcm/year.

To maintain regasification capacities of 5.5 Bcm/year or ramp up capacities to 7 Bcm/year, the terminal requires significant investments (building of a new tank, refurbishment of the tanker berth and of other facilities) currently estimated by Elengy at €340M and €430M respectively.

Against this background, Elengy invites the market to subscribe capacity of up to 7 Bcm/year at the Fos Tonkin terminal from October 2014 for a period of up to 20 years.

Elengy is considering two continuation scenarios:

- a "Higher-Capacity" project, enabling Elengy to offer capacities up to 7 Bcm/year,
- a "Lower-Capacity" project, enabling Elengy to offer capacities up to 5.5 Bcm/year.

The open season procedure proposed by Elengy can be broken down into three major steps:

1. eligibility of subscribers registered in the open season procedure;

2. allocation of capacities:

   - submission and simulated allocation of non-binding subscription requests;
   - submission and allocation of binding subscription requests;
   - allocation of capacities and conclusion of subscription agreements.

3. decision to implement the Fos Tonkin LNG terminal continuation project depending on the open season results.

I. Background

1) Current tariff framework

According to the French amended law No. 2003-8 dated 3 January 2003 on the electricity and gas markets and on the energy public service, access to the Fos Tonkin, Montoir and Fos Cavaou LNG terminals is regulated. As Elengy has not requested TPA exemption under article 7-1 of the aforementioned law for its continuation project for the Fos Tonkin LNG terminal, access to the terminal after the date of continuation is also subject to a regulated regime.

i. Tariff visibility

The French Order dated 20 October 2009 approving the tariffs for the use of LNG terminals states that a tariff specific to each LNG terminal will apply for a period of three years starting on 1 January 2010 for the Fos Tonkin and Montoir LNG terminals and as soon as it is commissioned for the Fos Cavaou LNG terminal.

These new tariffs introduce principles in favour of the development of new regasification capacities: the Order dated 20 October 2009 states that "*for extensions of existing LNG terminals and new terminals, as long as the increase in regasification capacity represents at least 20% of the infrastructure's initial capacity of the infrastructure and that newly created capacity is allocated using rules previously approved by CRE:*

- *the method for calculating the rate of return is fixed for 20 years. The rate is equal to the base rate applicable to natural gas transmission assets, which may change during the period depending on future tariff decisions relating to transport on gas transmission networks, plus the additional 200 basis points specific to LNG;*
- *an additional bonus of 200 basis points is awarded for 10 years."*

ii. Regasification services

The French Order dated 20 October 2009 approving the tariffs for the use of LNG terminals defines the basic regasification services provided at the three French regulated LNG terminals:

"Continuous" service*: This service is intended for shippers that unload on average ten or more cargos at a terminal in the course of the year. For this service, the operator provides continuous send-out over the contractual period. Send-out is made as regular as possible for the user, given the overall schedule of unloading operations in the terminal […].*

Send-out service in 30-day bands:

- **"banded" service***: this service is intended for shippers that unload at most one cargo per month, averaged over the year, at a terminal. For this service, each cargo is sent out as a constant band that continues for 30 days after the date when unloading finishes;*

- **"spot" service***: this service is intended for cargos unloaded in month "m" that were booked after the 20th of month "m-1". Subscriptions are for slots that were vacant in the monthly schedule at the time of the booking. Each cargo is sent out as a constant band that continues for 30 days from the end date of the unloading.*

The Order also specifies that "*When several users book the continuous send-out service with a LNG terminal operator, the operator submits draft rules for sharing regasification capacity between those users for CRE's approval*."

To date, Elengy has only one "continuous" service customer at each LNG terminal.

The project to ensure the continuation of the Fos Tonkin LNG terminal beyond 2014, as well as GDF Suez's proposal to release capacity on the market at the Montoir LNG terminal up to 2 Bcm/year[1], may lead to several "continuous" service shippers on one terminal.

2) The public consultation launched by CRE concerning the open season procedure for the Fos Tonkin terminal

In order to prepare this deliberation, CRE granted an audition to Elengy on 5 November 2009 and 7 January 2010 and organised a public consultation from 30 November to 24 December 2009 concerning:

- the Preliminary Information Memorandum published by Elengy describing the framework of the project and the allocation rules ;
- additional proposals under consideration by CRE ;
- the project proposed by Elengy on the rules for sharing send-out among several "continuous" service customers.

11 replies were received. The summary of the public consultation and non-confidential individual replies are published together with this deliberation.

Following its audition, on 7 January 2010, Elengy sent a new version of the Information Memorandum (Appendix A) and allocation rules (Appendix B) to CRE on 14 January 2010.

II. Analysis of the open season procedure for the Fos Tonkin terminal continuation project

CRE presents hereafter its analysis of the open season procedure as described by Elengy in the Information Memorandum (Appendix A) and the Allocation Rules (Appendix B) dated 14 January 2010, particularly in light of responses from market players to the public consultation organised by CRE.

1) The timetable of the capacity allocation phase

The timetable of the capacity allocation phase, as presented by Elengy, can be broken down into:

- a non-binding phase, between 14 October 2009 and 12 February 2010,
- a binding phase, between 18 February 2010 and 18 March 2010,
- a negotiation phase between subscribers and Elengy, in the event of an unsuccessful economic test and provided that the capacity requested is greater than 36 TWh/year.

The introduction of a non-binding phase will enable Elengy to estimate the dimension of the project and obtain feedback on the allocation rules.

It has emerged from the public consultation that most shippers are not satisfied with the timetable. The arguments put forward are:

- the timetable is too tight in view of the necessary timeframes for the LNG supply chain, the specific characteristics of the Fos Tonkin LNG terminal (limitation of the size of vessels that can unload at the terminal) and the partially binding nature of the non-binding phase given the existence of an incentive-based contribution requested from shippers by Elengy ;
- the timetable is concomitant with GDF Suez's plan to release capacity on the market at the Montoir and Fos Cavaou LNG terminals, for which allocations are set to take place before 7 March 2010 and 7 June 2010 respectively. This leads to high uncertainty for market players.

Elengy believes that putting back the timetable would compromise the completion of the project, as it would delay the engineering studies and the investment decision date, scheduled for October 2010. This could lead to the LNG terminal not being operational as planned.

However, Elengy accepts to move the timetable back one month, postponing the non-binding request submission deadline to 16 March 2010 and that of binding requests to 16 April 2010.

[1] Notice published by the European Commission on 9 July 2009 pursuant to case COMP/B-1/39.316

CRE agrees with market players and considers that the timetable should be extended. However, it believes that a too significant postponement, implying that the end of the allocation process would be after April 2010, would compromise the completion of the project in the allotted time.

Moreover, it is important to take into account the timetable of the open season concerning French interconnections with Spain beginning in the first quarter of 2010 and including the sale of capacities between the South and North zones operated by GRTgaz. It would be preferable for the results of the open season for the Fos Tonkin LNG terminal continuation project to be published prior to this open season, in order to enable subscribers to capacities on the Fos Tonkin terminal to take part, if they so wish, in full knowledge of their regasification capacity allocation on the Fos Tonkin terminal.

2) The project's financial and technical data

The answers show that market players ask for more information on the scope of investments and the dimensioning scenarios. In particular, the respondents request further information on the dimension of the project in the negotiation phase, should there be one.

During its meeting with CRE on 7 January 2010, Elengy stated that the negotiation phase with subscribers would not result in a revision of the dimension of the project, as only two scenarios are planned (the project for 7 Bcm/year or the project for 5.5 Bcm/year). Negotiations will concern:

- either a revision of the subscriptions requested to satisfy the test,
- or an increase of the indicative maximum unit tariff of 1.5 €/MWh.

Elengy has also modified its Information Memorandum (Appendix A), which now includes the type and amount of investments related to each dimension scenario.

CRE believes that these points will give a better understanding to potential subscribers taking part in the open season procedure.

3) Incentive-based contribution

To avoid the eventuality of potential subscribers submitting non-binding requests that are considerably different from later binding requests, Elengy asks these subscribers to undertake to pay an "incentive-based contribution" of €100,000.

Most market players are against the implementation of such a contribution. Some players consider that no contributions should be paid by shippers should the project go ahead.

Elengy believes that this contribution is necessary so that the non-binding phase is representative of real market demand. Elengy states that the amount is low compared to the cost of the minimum annual regasification service to be subscribed (i.e. 5 TWh/year).

However, Elengy accepts to no longer base the payment of the incentive-based contribution on the failure of the economic test. In its new version of the Information Memorandum (Appendix A), Elengy proposes to cancel the payment of the contribution if capacities are allocated at the end of the allocation process.

CRE believes that this type of contribution is necessary for the non-binding phase to be effective.

III. CRE guidelines concerning future access conditions to regulated LNG terminals

The current tariffs for the use of regulated French LNG terminals (ATTM3 tariffs) approved by French Order dated 20 October 2009 apply for a three-year period:

- From 1st January 2010 for the Fos Tonkin and Montoir terminals (operated by Elengy) ;
- And as soon as the Fos Cavaou terminal is commissioned (operated by STMFC).

When the Fos Tonkin terminal continuation project is set to be commissioned, scheduled for October 2014, the LNG terminals operated by Elengy will be subject to new tariffs.

Furthermore, it will be necessary to adapt the existing services in the terminals operated by Elengy to the operating methods of a LNG terminal with several "continuous" service customers.

In order to provide all necessary information to shippers wishing to take part in the open season for the Fos Tonkin LNG terminal continuation project, CRE hereafter specifies its guidelines concerning future access conditions to LNG terminals.

1) Introduction of a releasable capacity system

In the public consultation dated 30 November 2009, a question was raised concerning the implementation of a releasable capacity mechanism on the Fos Tonkin LNG terminal as of October 2014.

This mechanism stipulates that, for any shippers who have subscribed over two thirds of the annual capacity marketed at the Fos Tonkin LNG terminal, the proportion of subscribed capacities above the two thirds of marketed annual capacity will be considered as potentially releasable.

The shipper with releasable capacity allocated at the Fos Tonkin terminal must commit to release this capacity to Elengy, in the event of another shipper's request that cannot be fulfilled due to lack of available capacity.

According to the principles proposed in the public consultation, a third-party shipper may subscribe to releasable capacity at the Fos Tonkin LNG terminal:

- under a notice period of 9 to 12 months,
- with a start date set on 1 October each year,
- for a minimum duration of 5 years, subject to availability of releasable capacity,
- for a minimum volume of 5 TWh/year.

These releasable capacities will be subject to the regulated tariff in force at the Fos Tonkin terminal.

Most market players are in favour of a releasable capacity mechanism. Only one shipper considers that the implementation of such a mechanism would threaten the success of the open season procedure for the Fos Tonkin LNG terminal continuation project.

Elengy believes that the implementation of such a mechanism would threaten the success of the open season. However, if the mechanism is adopted, Elengy states that it considers the proposed notice period to release capacity too short.

In order to prevent the allocation of more than two thirds of the capacities of the terminal to a single shipper[2], CRE intends to issue a deliberation on the introduction of releasable capacities according to the aforementioned mechanism, if justified by the open season results. The notice period to release capacity will be reassessed if necessary.

[2] Principle stipulated in the CRE deliberation dated 15 December 2003 on the protocol between Gaz de France and Total and referred to in the conclusions of the Working Group on the Regulation of LNG Terminals chaired by Colette Lewiner

2) Return on investment framework

i. Management of possible cost or deadline overruns

Significant investments will be required for the continuation of the Fos Tonkin LNG terminal. The forecast amounts provided by Elengy are as follows:

- €430M for the "High-Capacity" project, of which €210M for the construction of the new 160,000 m^3 tank (known as RV4), €140M for renovation work scheduled for the 2010-2016 period and €80M for the 2016-2020 period,
- €340M for the "Low-Capacity" project, of which €160M for the construction of the new 80,000 m^3 tank (known as RV4), €120M for renovation work scheduled for the 2010-2016 period and €60M for the 2016-2020 period.

At the end of the call for subscriptions procedure, shippers with capacities allocated on the Fos Tonkin terminal will have to sign subscription agreements at the beginning of May 2010 at the latest. When these agreements are signed, the tariffs for the use of the LNG terminal that apply to the period under agreement will not be known. These tariffs will depend on the level of investments, operating costs, subscription volumes and commissioning date.

Given Elengy's proposals, future users of the Fos Tonkin LNG terminal would therefore face the risk of a tariff increase, should the costs or schedule of the project overrun.

Consequently, in order to encourage the terminal operator not to exceed the investment estimation chosen for the completion of the Fos Tonkin LNG terminal continuation project presented to CRE by Elengy, CRE proposed in its public consultation a solution to manage cost or deadline overruns in relation to the reference investment estimation:

- if actual investments exceed the reference cost estimation and if this overrun is not due to a *force majeur* case, the costs overruns will not receive the bonus of 200 basis points provided for in the French Order dated 20 October 2009 approving the tariffs for the use of LNG terminals, within the framework of tariff visibility,
- moreover, if the project is delayed excluding *force majeur* cases, current assets will not be remunerated beyond the planned commissioning year.

Most market players are in favour of this proposal and think that this mechanism ensures that risks are better shared out between the operator and shippers. A small number of replies suggest making this framework even more stringent for the terminal operator.

Elengy objects to this principle. It considers the tariff framework currently in force as a strong incentive to optimise the construction timetable. Furthermore, Elengy reminds that, according to the "Specific Subscription Agreement Conditions", the terminal operator will have to inform subscribers regularly about the progress of the continuation project. Elengy also states that operations at the terminal up to the allocated capacities are guaranteed beyond 30 September 2014.

In addition, in order to limit the risk facing capacity subscribers at the Fos Tonkin LNG terminal after 2014, Elengy proposes, in the new version of the allocation rules (Appendices A and B), that subscribers are able to terminate their subscription agreement if the investment amount known at the time of the preparation of the investment decision by Elengy (scheduled for October 2010) varies by more than 25% from the investment amount stated in the Information Memorandum appended to this deliberation (Appendix A).

CRE believes that the risk of cost and deadline overruns should not be borne solely by the shippers in the LNG terminal and that the tariff remuneration terms must encourage the terminal operator not to exceed the investment estimate and the commissioning timetable.

As a result, CRE plans to propose methods to deal with the cost and deadline overruns described above in the future tariff proposal for the use of the Fos Tonkin LNG terminal.

ii. Investment incentives and tariff visibility

Following capacity allocation, CRE intends to apply tariff visibility and investment incentive principles to the Fos Tonkin LNG terminal continuation project for investments required to ramp up from 3 Bcm/year to 5.5 Bcm/year or more, under the conditions described in the explanatory statement of the CRE deliberation dated 16 July 2009 on the tariff proposal for the use of LNG terminals.

3) Adaptation of “continuous” service

The “continuous” send-out service currently provided on LNG terminals operated by Elengy is designed for a single “continuous” service customer on any LNG terminal. It will be necessary to adapt this service when several customers subscribed to it will be present at the same terminal.

The public consultation launched by CRE also concerned the means of adapting “continuous” service, planned by Elengy.

In its proposal, Elengy plans to introduce:

- the sharing of send-out between “continuous” service customers based on a send-out ratio in order to ensure that send-out is shared fairly;
- a storage management system for each “continuous” service shipper to ensure that storage is shared fairly;
- a deficit allowance enabling “continuous” service shippers to have one-off negative storage levels;
- terms for compensation for reductions in send-out that (“continuous” service or “30-day band” service) shippers at the terminal may suffer as a result of a reprogramming by a “continuous” service shipper.

Market players are in favour of the general principle of sharing send-out. However, most players stress that Elengy’s proposal does not take into account the specific characteristics of each terminal and that the details of the mechanism should be clarified.

Elengy proposes to set up a test of the rules for sharing send-out between several “continuous” service customers. This trial would be conducted over one year and would begin when more than one “continuous” service customer is present on one of the terminals operated by Elengy.

CRE is in favour of testing the mechanism for sharing send-out between several “continuous” service customers proposed by Elengy. On the basis of the results of this trial, CRE will then issue a deliberation on the conditions of access to the “continuous” service applying to regulated LNG terminals with several “continuous” service customers.

IV. Decision on the open season procedure for the Fos Tonkin LNG terminal continuation project

CRE approves the open season procedure proposed by Elengy, made up of the Information Memorandum (Appendix A) and Allocation Rules and appendices (Appendix B).

V. Appendices

Appendix A:
"Fos Tonkin Open Season– Information Memorandum" (version submitted to CRE for deliberation – 14 January 2010),

Appendix B:
"Fos Tonkin Open Season – Allocation Rules" (version submitted to CRE for deliberation – 14 January 2010).

Approved in Paris, 14 January 2010

For the Energy Regulatory Commission (CRE)

The Chairman,

Philippe de LADOUCETTE