

CONSULTATION RESPONSE

to proposed amendments to the regulations of 20 December 2002 no. 1724
relating to the stipulation of tariffs etc. for certain facilities

15 March 2013

CONSULTATION – PROPOSED AMENDMENTS TO THE REGULATIONS OF 20 DECEMBER 2002 NO. 1724 RELATING TO THE STIPULATION OF TARIFFS ETC. FOR CERTAIN FACILITIES

Remarks from Solveig Gas Norway AS ("Solveig"), owned by Canada Pension Plan Investment Board, Allianz and Infinity, a wholly owned subsidiary of Abu Dhabi Investment Authority, and Silex Gas Norway AS ("Silex"), owned by Allianz.

1. SUMMARY

Reference is made to the Ministry of Petroleum and Energy's consultation paper of 15 January 2013 where a reduction of approximately 90% of the capital element (the K-element) of the tariffs in the gas transportation system Gassled is proposed for most of the tariff areas with effect from 1 May 2013.

Solveig and Silex own 32% of the participating interests in Gassled. We became owners in 2012 with the intention of playing an active role as infrastructure owners and providers of long-term capital to the further development of gas infrastructure on the Norwegian continental shelf (NCS). This commitment was based on the understanding that:

- Profits shall mainly be taken out on the producing fields and not in the infrastructure.
- The Ministry has the authority to change tariffs, provided that the requirements related to resource management considerations and securing a reasonable profit for the infrastructure owner are adhered to.

In addition, the investment decision was based on the assumption of:

- A stable and predictable regulatory environment.
- Balanced regulatory changes made in consultation with all stakeholders.

The proposal violates these principles. Further, it does not meet the stated objectives and has several negative consequences.

- **The proposal is not suitable for achieving the goal of best possible resource management.** The proposal sets forth a *general* reduction of the tariffs for *all* gas volumes covered by capacity reservations made after the reduction has been implemented. Substantially all of the gas volumes that will receive reduced tariffs up to 2028, when the license period of Gassled expires, are volumes that will be produced irrespective of the proposal. For the majority of the producing fields the tariff level does not impact production and therefore is irrelevant from a resource management perspective. For new developments no causal link between the reduced tariffs and the production has been substantiated.

More targeted measures exist that are better suited for promoting increased production of socio-economical resources that may not be possible to realize in the future as a result of the tariff level and that does not result in the same negative consequences.

- **The proposal deprives infrastructure owners of their right to receive a reasonable profit.** The proposal results in a loss in income for the Gassled owners of NOK 40 billion. For Solveig and Silex the loss is NOK 13 billion. The loss of income means that the rate of return decreases to some 4%, which clearly does not fulfil the requirement for a reasonable return. It is also far below the commonly accepted level of 7% and fundamentally different from the return of 10.5% set forth by the Ministry in the consultation paper.

The 10.5% figure is in any event irrelevant and misleading as it refers back to an inappropriate time period (1975 to 2028) and is distorted by assets operated under a different regulatory regime (Norpipe and Statpipe).

The proposal is in breach of established regulation policy and practice, the basis for the establishment of Gassled and setting of tariffs in 2003, as well as subsequent tariff determination in connection with mergers of new facilities into the system. When Gassled was established and when new facilities were subsequently merged into the system, the determination of values and tariffs was based on the net present value of expected *future* cash flows without taking into account *historical* cash flows.

The unprecedented approach adopted by the proposal places decisive emphasis on *historical* cash flows received by previous owners when assessing what constitutes a reasonable return going forward. This deviation from established practice represents a retroactive intervention and a clear breach of the infrastructure owners' legitimate expectations, which were based on available information and dialogue with relevant parties.

- **The proposal results in an unwarranted substantial value transfer from the infrastructure owners to the shippers.** The real effect of the proposal is that the shippers receive an unwarranted windfall gain through a transfer of value of approximately NOK 40 billion from the Gassled owners to the shippers, without it contributing to increased production and without the shippers having expressed a need for reduced tariffs.
- **The proposal undermines Norway's reputation as having a stable and predictable investment environment.** The proposal introduces political and regulatory risks that have significant negative effects on Norway's reputation for having a stable and predictable investment environment. This is already evidenced by the reactions to the proposal from the international credit rating institutions Moody's and Standard & Poor.
- **The proposal endangers the access to infrastructure capital with negative effects for resource management.** Infrastructure capital with lower required rate of return enables oil and gas companies to allocate capital to upstream projects which yield a higher rate of return. Use of infrastructure capital would facilitate more efficient resource management and increase the ability to develop marginal fields. The proposal limits access to such capital.

If the proposal is implemented, the shareholders of Solveig and Silex will not support further investments in expansions of the system beyond the contractual obligations of Gassled owners.

- **The proposal is the result of an inadequate and inappropriate process.** One of the characteristics and a success factor behind the development of Norwegian petroleum activities has been a tradition for extensive interaction with affected parties before important regulatory changes are formally proposed.

Given that the intention to review the tariff level was initially communicated by the Ministry in the beginning of 2012, shortly after the approval of the transactions, it is inconceivable that the Ministry did not communicate that a fundamental change which this proposal represents was under consideration during the extensive meetings we had with the Ministry as part of executing the transactions.

Furthermore, the current proposal has been prepared in isolation by the Ministry despite our requests for a dialogue. In addition, a proposal with such wide-ranging and long lasting implications should not be rushed through. This is in clear contradiction with established practice and will inevitably result in a lack of trust in such processes going forward.

- **The proposal lacks legal basis.** We always recognised that the Ministry may stipulate and change tariffs within the legal limits. However, this proposal is outside the Ministry's legal boundaries, highly invasive and implies a significant retroactive effect. The proposal represents an unwarranted intervention of the infrastructure owners' legally protected rights and expectations.

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We believe that the Ministry's stated objective should be met through more targeted measures which avoid the negative effects of the existing proposal. The development and timing of the implementation of such measures require an appropriate process of consultation that involves relevant stakeholders in accordance with common practice. Solveig and Silex are ready to participate in such a process.

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2. INTRODUCTION

Gassled was established with effect from 1 January 2003 through a negotiation-based unitization of the relevant gas infrastructure on the NCS based on a request from the authorities to ensure a uniform ownership.

Gassled has been a success in the ten years that the system has existed. A uniform ownership in the major part of the gas transportation system on the NCS has provided a cost-efficient and competitive transportation system. This has been an important part of promoting best possible resource management of the petroleum activities. The system has also proved to be well-functioning in terms of merging new pipelines and processing facilities into the system. The historical stability and predictability of the Gassled system has enabled it to attract long-term infrastructure capital with a lower required rate of return than the ones of the oil and gas companies. Due to their lower required rate of return infrastructure owners are, unlike the oil and gas companies, willing to tie up long-term capital in infrastructure. This facilitates increased new investments in the system, which in turn will contribute to the development of more fields.

The proposal represents a risk of jeopardising the success of Gassled and would result in significant negative consequences if implemented as further described below.

3. THE PROPOSAL IS NOT SUITABLE FOR ACHIEVING THE GOAL OF BEST POSSIBLE RESOURCE MANAGEMENT

3.1 Background

We support the policy objective of producing as much of the socio-economical resources on the NCS as possible.

The consultation paper refers to the fact that the tariff level in Gassled may affect all parts of the value chain for petroleum activities; exploration, development of new discoveries as well as measures for further exploitation of existing fields. The proposal is based on the hypothesis that reduced transportation costs will result in increased production of petroleum resources from the NCS.

However, the proposal is in its current form to a limited extent suited to promote increased production of petroleum resources. In this perspective, the scope and timing of the proposal seems inappropriate, particularly in light of its negative effects.

3.2 The proposal benefits mainly existing fields and volumes that will be produced in any event

The purpose of the proposal is to contribute to increased production. However, it is clear that the capacity in Gassled through to the end of the current license period will be largely utilised by gas volumes from existing fields and from fields which would be developed based on the current tariff level. These volumes will be produced irrespective of the proposed tariff reduction.

This conclusion is also supported by analyses carried out by Pöyry Management Consulting ("Pöyry"), based on the volume assumptions of Gassco and Norwegian Petroleum Directorate and the current capacity situation in Gassled.

Therefore the proposal is not suitable to contribute to increased production. The proposal represents an unwarranted windfall gain for the shippers of NOK 40 billion from 2013 up to the expiry of the license period in 2028 (expressed in net present value before tax with 7% real discount rate). This is a substantial value transfer to the shippers without contributing to increased production and the shippers have not expressed a need for reduced tariffs.

3.3 The current tariffs do not prevent increased production at this point of time

In addition to the fact that the proposal to a large extent is targeted towards volumes that will be produced irrespective of the current tariff level, the consultation paper does not substantiate a causal link between the proposal and increased production.

The starting point for the assessment of whether reducing the tariffs is required in order to promote increased production is that a field must be able to carry reasonable transportation and processing costs, in order to be profitable from a socio-economic perspective. This has also been explicitly assumed by the Ministry in White Paper no. 46 (1987-1988) in which principles and framework conditions for development of new transportation capacity were established:

The transportation structure should to the least possible extent deviate from what is most profitable in a socio-economic perspective. It should not prevent fields from becoming developed if they are profitable in a socio-economic perspective, but nor should they subsidize a development. (page 67)

The transportation tariffs in the existing system are relatively low and the K-element constitutes a limited part of the total costs for bringing natural gas to market. Analysis performed support that as of today the transportation costs do not prevent increased gas production.

As *exploration* is concerned, a decision to explore for petroleum will depend on an assessment of a number of factors. Attractive exploration prospects will be pursued irrespective of the tariff level, and marginal prospects will in principle not change character as a result of the proposed tariff reduction. On the other hand, the *existence* of infrastructure, rather than the tariff level, will be of importance to the exploration activities. The current proposal will reduce the access to relatively low cost infrastructure capital that would have had a positive effect in terms of cost-efficient development of the infrastructure on the NCS.

The fact that the K-element of the tariffs constitutes a relatively minor part of the total operating costs also implies that a reduction will be of limited importance for decisions concerning *development* of fields. This applies to both major and marginal discoveries.

Further, the proposal does not seem to affect the implementation of measures for further exploitation of *existing fields* in any material way. Measures for increased extraction are often of a marginal nature and costs have a greater effect on such measures. However, the cost level is to a great extent affected by the actual measure being implemented to increase production. A reduced K-element in the transportation tariffs will result in marginal changes to the project economics.

The limited impact of transportation costs for increased production is supported by a number of public policy documents. The consultation paper's focus on the importance of transportation costs does not seem aligned with the Ministry's view in the White Paper no. 28 (2010-2011), (the "2011 White Paper"). The main focus of the 2011 White Paper is to present different measures that the Åm Committee had pointed to in its report on "Increased production on the NCS". Based on the expert committee's conclusions, the 2011 White Paper proposes a number of measures *without* mentioning changes to the tariff level in Gassled and includes the following statement:

Given the major investments required to build new gas infrastructure and the relatively low transport costs in existing systems, the oil and gas companies will have incentives to use existing gas infrastructure when considering different transportation alternatives for new gas. (page 66)

Furthermore, the tariff level was not an issue in connection with the broad review of the access regime for gas transportation that the Ministry initiated and that resulted in a number of amendments both to the Petroleum Regulations 27 June 1997 no. 653 and the Tariff Regulations 20 December no. 1724 in 2011.

Based on the above there is currently limited evidence suggesting that the proposal will result in increased production. This does not mean that areas cannot be identified in which the tariff level may have a positive impact on the production of socio-economical resources in the future, for instance in connection with tail-end production or volumes from the Barents Sea.

4. THE PROPOSAL DEPRIVES INFRASTRUCTURE OWNERS OF THEIR RIGHT TO A REASONABLE RETURN

4.1 Overview

Solveig's and Silex' entry into Gassled has been based on the fundamental assumption for Norwegian petroleum politics that the profits shall mainly be taken out in the fields and not in the infrastructure due to resource management considerations. This principle is reflected in the current tariff level, which gives the infrastructure owners a rate of return that is substantially lower than the required rates of return used by the participants in upstream activities.

The proposal for tariff reduction deprives the infrastructure owners of their right to receive a reasonable return. In this respect we would like to highlight that:

- The proposal contradicts Norwegian price regulation policy.
- The proposal contradicts the Ministry's own practise in Gassled.
- The proposal results in a 4% return which does not fulfil the reasonable return requirement and is far below the generally accepted level of return of 7%.
- The proposal is based on an irrelevant and misleading reference to a rate of return that gives a "super profit" of 10.5%, which is calculated based on an irrelevant time period (1975-2028) that takes into account *historical* cash flows as opposed to *future* cash flows.

4.2 The proposal contradicts with Norwegian price regulation policy

When the authorities make changes within regulated sectors for instance with respect to taxes, levies and regulated prices, these have consistently been made in the form of adjustments of an existing level. In addition, such adjustments are carried out with effect going forward, without the *forward-looking* change aiming to correct the previous level that in hindsight might be regarded as being too high.

The proposed 90% reduction of the K-element, based on a retroactive correction of an allegedly excessive rate of return for a long period back in time, is extraordinary and inconsistent with previous regulation policy. Previous owners' historical excessive return is used as a basis for reducing the rate of return of current infrastructure owners accordingly. The consequence is that the Ministry does not assess the tariff level based on what is presumed to give a reasonable rate of return going forward. It is unreasonable and unjustified that the tariff level is reduced to a level that is much lower than what represents a reasonable level. Using such method is unprecedented in Norwegian price regulation policy.

A tariff reduction of 90% has no parallel in other regulated parts of the energy sector. An obvious example is the capital element in the electricity net tariff.

This element has evolved slightly over time, but it has never been subject to dramatic changes similar to what is now being proposed for the tariffs in Gassled, see Regulations 11 March 1999 no. 302 regarding economical and technical reporting, income frames for net based activities and tariffs, article 1-4 and chapter 7 and 8.

4.3 The proposal contradicts the Ministry's own practise in Gassled

4.3.1 The stipulation of tariffs at the establishment of Gassled

Gassled was established through an unitisation of the relevant infrastructure. The stipulation of tariffs and distribution of participating interests among the different licensees was mainly determined based on discounted *future* cash flows in the different facilities. Previous owners' investments and rates of return were not taken into account.

All the way back to the approval of Zeepipe in 1988 and up to the establishment of Gassled, a principle of 7 % real pre-tax rate of return was used. The principle has later been repeated on a number of occasions, including in the 2011 White Paper, which is also referred to in the consultation paper.

The K-elements in the Gassled tariffs were determined to regulate the participants' future earnings and to provide the owners a reasonable return. Previous investments or rates of return were not included in the calculation of the *future* tariff level in a *price-regulated* system such as Gassled. If previous owners' rates of return had been included when stipulating the tariff in 2003, the K-element should already at this point have been set to zero or close to zero in order to reflect the 7% return principle. If this approach had been taken, the unitisation would most likely not have taken place. This raises the question of why Gassled has been allowed to exist for about 10 years based on the stipulated tariffs before the Ministry has taken the initiative to change the tariffs or made any statements regarding the achieved return in the system as such.

The fact that historic return is now made to be the decisive factor for the assessment of what constitutes a reasonable return going forward is in violation of the fundamental assumptions for the establishment of Gassled in 2003 and also the basis on which new facilities have subsequently been merged into the system.

4.3.2 The stipulation of tariffs in connection with subsequent mergers into Gassled

Several new facilities have been merged into Gassled after its establishment, including Langeled in 2006 and Gjøa in 2010. The Ministry has adjusted or established a new tariff in the relevant tariff area based on expected *future* volumes and a 7% rate of return for every new merger, as this is considered to give a reasonable return. In other words, even after 2003 the Ministry has solely focused on net present value of *future* cash flows when valuing Gassled. As in 2003, realised return up until the time of merging new facilities into the system was not taken into account on these occasions either.

New facilities were merged into Gassled under the assumption that these owners would realise their return through an interest in the total Gassled system. This assumption is also referred to in the Ministry's letter 20 December 2002 approving the Gassled establishment, where it is emphasised that the Ministry may order the merger of additional pipelines into Gassled conditioned upon ensuring protection of the investments made:

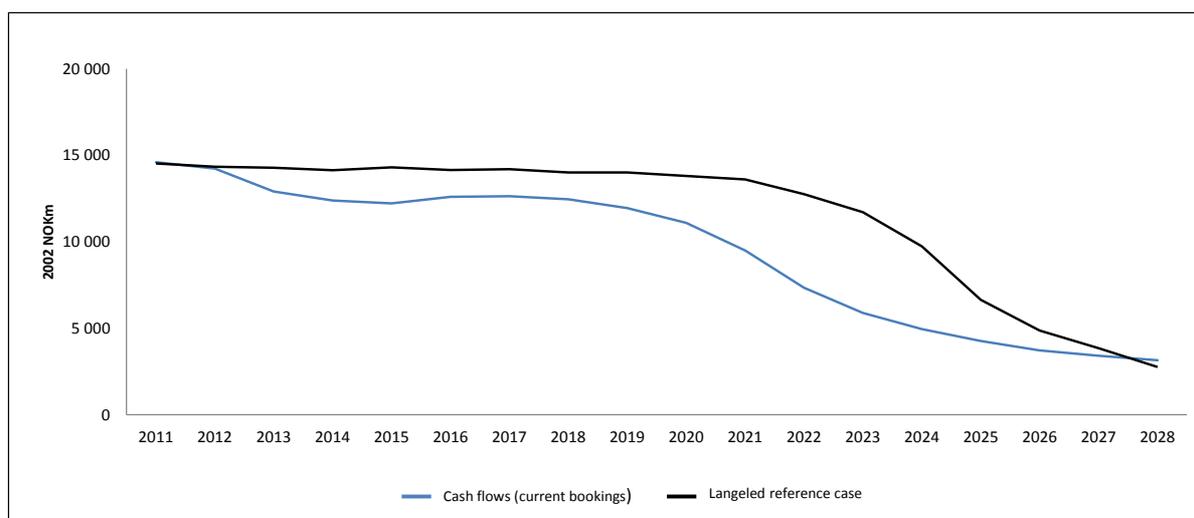
The Ministry may require that other joint ventures or companies shall be merged into Gassled due to important resource management considerations or other specific reasons.

If the participants do not agree to the changed ownership interests following from such merger within a reasonable period of time, the Ministry may adjust the ownership interests in Gassled, as well as stipulate the terms for the merger.

The Ministry will not stipulate ownership interests or terms related to such mergers that will result in a lower return on investments than the return that the ownership interests in the Ministry's view may be expected to give based on existing transportation agreements and expected future agreements. (our underlining)

The current tariff reduction proposal implies that there will be a substantial deviation between the cash flows that the valuation of Gassled was based on in connection with the mergers of new facilities, and the cash flows that can be expected from the proposal going forward. This can be illustrated by a comparison between the cash flows related to the K-element assumed in the Langeded merger and the cash flows related to the K-element that is assumed will be achieved as a consequence of the proposal:

Figure 1: Comparison of cash flows



Due to the significant tariff reduction, the cash flows related to new bookings will be marginal.

New owners in Gassled, both the ones who became owners when new facilities were merged in and those who have subsequently acquired ownership interests, have legitimate reason to expect to be able to realize the cash flows that had been assumed both by the owners in Gassled and by the authorities in connection with the approval of the mergers.

A stipulation that is based on the expected income stated in the reference cases, including for Langeded as described above, and that is now being corrected to reflect the proposed tariff reduction, indicates a return for the infrastructure owners of around 4% based on existing bookings. This calculation is *not* based on our respective purchase prices.

4.4 The proposal relies on irrelevant and misleading return calculations

The proposed tariff reduction is extraordinary in size and is based on an approach that deviates from the method used in other comparable cases. The proposal is based on a *dramatic new price regulation principle*, namely assessments of a "total rate of return", that allegedly show that the return from the 1970s and up to 2012 is 10% and will constitute 10.5% up to 2028. This is a totally different approach to price setting compared to (i) other government price regulations, (ii) the method used by the Ministry at the establishment of Gassled in 2003 and (iii) the method used in subsequent mergers of new facilities into Gassled. This changed approach has taken place at the same time as the principle for the tariff calculation – the owners' right to a reasonable return – is the same.

It is extraordinary that the Ministry in 2013 proposes to use the same legal basis to correct alleged *historic* excessive return when the Ministry previously has determined a reasonable return based solely on expected *future* cash flows.

The new owners who have entered into Gassled in the recent years have based their entry into the system on the principles for determination of tariffs that were used upon the establishment of Gassled in 2003 and upon subsequent mergers of new facilities. These are principles and assessments that have been used consistently and that are available and transparent, as opposed to the historical return dating back to the 1970s.

A system that allows for ownership changes on the basis of the Ministry's approval should take into consideration that new owners have not been able to benefit from previous owners' alleged excessive return. In this respect, it is a separate point that those who acquire interests should be able to expect that the principles for tariff calculation are the *same* for them as for the previous owners.

The *retroactive* approach that the Ministry is now using when considering a reasonable return *going forward* is contrary to the legitimate expectations that have been created. This must not be confused with expecting assistance from the authorities to achieve a certain level of interest on the purchase price. This is a matter of not radically worsening the framework conditions for new owners when changes of ownership are allowed and even seemed wanted, including in connection with the approval of ExxonMobil as the first oil and gas company to divest its Gassled interest. In the approval letter from the Ministry 1 February 2011 related to this transaction it was stated that:

[t]he Ministry focuses on diversified ownership in Gassled, one of the reasons being to distribute the financial liability between several participants. The Ministry will emphasise this in future applications, if any, for consent to transfer of ownership interests in Gassled.

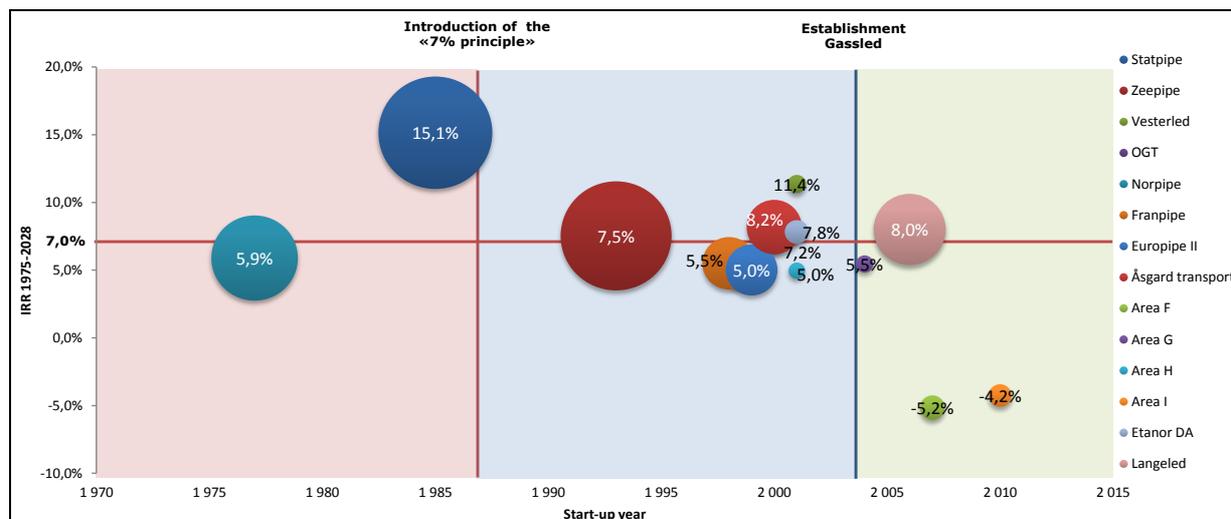
The change of approach when determining tariffs would also represent an unreasonable differential treatment of the Gassled owners. The owners that have received income from the transportation systems long before the establishment of Gassled, in particular in combination with having divested their interests in Gassled in full or in part just before the proposal was put forward, will benefit greatly from the proposal. This includes Statoil in particular. Statoil has by far sold the largest interest in Gassled. In addition to the consideration in connection with the sale, Statoil will benefit from a net windfall gain of approximately NOK 15 billion (expressed in net present value before tax with 7% real discount rate) in saved transportation costs as a result of the proposal. These benefits are achieved at the expense of companies that became owners through merging the new facilities into Gassled or through acquisition of interests.

In addition to the fact that the 10.5% return is irrelevant and misleading because it relates to a period in time that is not relevant to the assessment as to whether the current infrastructure owners receive a reasonable return, the Ministry's calculation is also unjustifiably influenced by transportation systems operating under a totally different regulatory regime, including Statpipe. The transportation system Statpipe deviates greatly from the rest of the Gassled system in the sense that the Ministry accepted, from start-up of operations in 1986 and until Gassled was established, a level of return that was approximately twice as high as the average for the other transportation systems. As a result of the substantial cash flows generated through Statpipe, the level of return in this transportation system has a major effect on the total return from 1975 and until 2012 and 2028, respectively.

This means that the Ministry is now using a previously approved high historical return that only the Statpipe owners, including Statoil, have had, as a basis for reducing the return of the current owners going forward. It is contradictory and lacks legal foundation to include this element when stipulating the tariff level going forward.

Statpipe's higher return is illustrated below¹.

Figure 2: The rate of return in the different pipeline systems 1975-2028



Statpipe and Norpipe, both of which were established in a period in which the tariffs were stipulated with more limited regulation, have a considerable impact on the total return. Based on numbers received from Gassco, the return will, if these two systems are disregarded, be 4.2% and 7.2% up to 2012 and 2028 respectively, instead of 10% and 10.5%. This demonstrates that the current tariff level will not result in any "super profit" and that it is consistent with the regulation principles that currently apply to the stipulation of tariffs.

5. THE PROPOSAL UNDERMINES NORWAY'S REPUTATION AS HAVING A STABLE AND PREDICTABLE INVESTMENT ENVIRONMENT

The proposal introduces political and regulatory risks that have significant negative effects on Norway's reputation for having a stable and predictable investment environment. This is already evidenced by reactions to the proposal from the international credit rating institutions Moody's and Standard & Poor.

In a recent published credit rating of 4 March 2013 the following assessment is made of the effects of the MPE's proposal:

On January 15th 2013, the Norwegian Ministry of Petroleum and Energy (MPE), unexpectedly published proposed revisions to tariffs that will apply when current bookings expire. This has somewhat reduced our confidence in the predictability of the regulatory regime, particularly as it comes soon after the sale of a stake in Gassled by a Norwegian government owned entity, after a very long period of stability. The proposed change in regulation differs from the increased return on equity that the Norwegian electricity grid operator, Statnett SF (A2 Stable), will be able to earn on its assets from 2013 onwards.

The increased regulatory and political risk may also result in increased capital costs in the form of increased risk premium as well as downgrading of debt.

This may have a negative effect for the development of marginal fields, as well as a negative tax effect as a consequence of higher interest deduction and reduced proceeds due to lower investments. These effects have already materialised through the notification of a potential downgrading of the bonds that some of the Gassled owners have issued.

¹ The circles represent the different transportation systems, and the size of the circle indicates the relative size of the investments in the transportation system in question. The circles are also placed on a timeline that shows when the relevant systems became operational.

The rating agency Moody's reported in a notice of 19 February 2013 that it is very likely that Solveig's bonded debt will be downgraded. The downgrading will result in increased borrowing costs. In addition, there are the negative consequences for Norwegian and international bond holders as a result of the reduced value connected to downgrading.

The proposal is also in conflict with recognised international law principles for foreign investments. It is a recognised principle in international law that foreign investments should enjoy stable and predictable framework conditions. Energy Charter Treaty Article 10 embodies the principle:

Each Contracting Party shall, in accordance with the provisions of this Treaty, encourage and create stable, equitable, favourable and transparent conditions for Investors of other Contracting Parties to make Investments in its Area.

Such conditions shall include a commitment to accord at all times to Investments of Investors of other Contracting parties fair and equitable treatment. Such Investments shall also enjoy the most constant protection and security and no Contracting Party shall in any way impair by unreasonable or discriminatory measures their management, maintenance, use, enjoyment or disposal.

The principle that this provision is built on is a part of international law and the treaty has wide support. It is formally signed, but not ratified by Norway. The Norwegian authorities have previously ensured that international principles for foreign investments are not challenged, among others by consulting affected parties in due time before changes are made. Predictability and stable framework conditions are prerequisites for foreign investments. The proposed change of the Tariff Regulations violates the principle of protection of foreign investments and the authorities' practise in this respect both with regards to process and result.

6. THE PROPOSAL ENDAGERS ACCESS TO INFRASTRUCTURE CAPITAL WITH NEGATIVE EFFECTS FOR RESOURCE MANAGEMENT

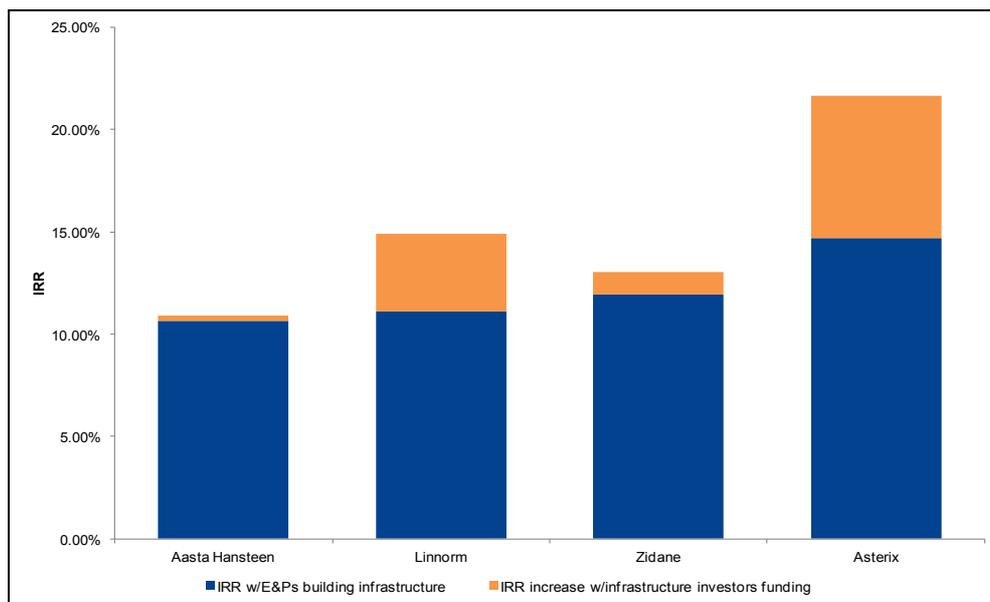
From a resource management perspective the proposal may be detrimental to further investments from existing and potential new infrastructure investors. This reduces the flexibility with respect to implementation of new projects and decreases the ability to develop marginal fields, as the oil and gas companies as a starting point will have to carry these investments on their own going forward. These companies have significantly higher rate of return requirements than pure infrastructure owners.

The fact that the rate of return from infrastructure is significantly lower than their general required rate implies that the economy in the field development part of the project must be correspondingly higher in order to achieve sufficient overall profitability required for project implementation.

If the infrastructure investments have to be included in the project economics of the upstream companies, this could lead to non-development of projects that are otherwise profitable from a resource management perspective. A positive measure in this respect would be to ensure that this type of investment can be made by infrastructure owners. This will contribute to the goal set forth in the consultation paper. To achieve this it is however important that Gassled is maintained as a safe and secure infrastructure investment that is able to attract capital with lower rate of return requirements than what the oil and gas companies can offer.

Pöyry has analysed the positive effect for development of marginal fields in the Norwegian Sea if infrastructure capital is available for developing the new pipeline Polarled, as opposed to the situation where the field owners have to carry the investment. The analysis shows a clear improvement of the internal rate of return in relation to all fields.

Figure 3: The effect for marginal fields in the Norwegian Sea



This substantiates that the access to infrastructure capital will contribute positively to the resource management on the NCS.

The fact that the proposal in practise presupposes the re-entering of the oil and gas companies in Gassled is not ideal from a governance perspective. Just by including for instance Polarled, the number of owners will increase by eight. This results in a more complex ownership structure, in addition to the fact that many of the potential new owners will be oil and gas companies that have defined infrastructure outside their core activities. Some will also be relatively minor companies with a financial solidity that may make it challenging to carry the other investment obligations that come with being a Gassled owner.

7. THE PROPOSAL IS A RESULT OF AN INADEQUATE AND INAPPROPRIATE PROCESS

A close cooperation with the industry has been a cornerstone in the development of Norwegian petroleum activities, also with respect to regulatory changes. This is underlined by the Ministry in a presentation of the Norwegian model for petroleum activities published on the Ministry's website:

What is important to take note of is however that adjustments and developments in the legislation are done in close contact with the industry and with OLF.

This is based on a firm belief that the best decisions are made when the authorities has sufficient information and a good understanding of the industry's needs and viewpoints.

The importance of interaction has been emphasised by the Ministry in a number of contexts, including in the 2011 White Paper:

The petroleum activities on the NCS are regulated through an extensive legal framework based on interaction between authorities and rights holders. (page 55)

Until recently this has been standard practice, including in connection with the recent regulatory changes implemented in the Regulations 20 December 2005 no. 1625 relating to the use of facilities by others. It follows from the related consultation paper that the Ministry notified in advance that changes would be considered and that the proposal has been based on broad consultation with the industry:

In the White Paper no. 28 to the Storting (2010-2011), "An industry for the future – regarding petroleum policy", the government said that they will change the regulations relating to the use of facilities by others with a view to achieving efficient exploitation of resources and to ensure that as much profit as possible is realised in the field. (...)

The Ministry has had a series of meetings with companies that have been negotiation leaders in reported negotiations, as well as other important companies.

The purpose of these meetings has been to get an overall impression of the industry's experiences with and attitude towards the regulations.

The fact that this is how the Norwegian model works was also underlined in the communication that Solveig and Silex had with the Ministry during the approval processes related to the purchase of Gassled interests from Statoil, TOTAL and Eni in 2011 and 2012. On this basis and taking into account that the intention to review the level of tariffs was notified by the Ministry in the beginning of 2012, shortly after the approval of the transactions, it is inconceivable that the Ministry did not communicate clearly that a fundamental change which the proposal represents was under consideration during the relatively extensive approval process. Instead emphasis was put on a possible future need for redistribution of tariff income in connection with an extension of the license period through a negotiated solution by the affected parties, in order to ensure the best possible resource management.

It is difficult to comprehend why a proposal as invasive as this one has been dealt in a seemingly urgent manner and is prepared without involvement from the industry, also taking into consideration that this has been a clearly expressed request from the owners' side to be allowed to participate in the process.

The process represents a breaking point in terms of the development of Gassled and Norwegian petroleum activities. The Gassled owners have on this basis been left with a number of unanswered questions. What is the reason for the Ministry's reluctance to involve the industry in this particular matter? Why it was never mentioned that a material change of the K-element was imminent during the approval process? What is the reason for the proposal being put forward almost immediately after the ownership changes in Gassled were completed? Why is the Ministry in such a hurry to implement the proposal? And in light of this – what is the reason that the Ministry finds it necessary to postpone the next booking round, and similarly why give a shorter consultation period than normal for cases of this importance?

The process has in its entirety been conducted in an inadequate and inappropriate manner that will inevitably result in a lack of trust in such processes going forward. Further, the closed process has in our opinion resulted in a proposal that has not sufficiently taken into account all relevant considerations.

8. THE PROPOSAL LACKS LEGAL BASIS

The Ministry has within in the boundaries of the applicable legislation the authority to make changes to the regulated tariff- and access regime to ensure good resource management on the NCS. However, it is equally clear that the legitimate rights and interests of the Gassled owners enjoy legal protection through the petroleum legislation and general administrative law principles.

The proposal goes beyond the legal boundaries for the Ministry's authority and represents an unwarranted and extensive intervention of the owners' rights. Furthermore, it implies a significant retroactive effect related to historical return that is irrelevant for the current infrastructure owners' right to a reasonable return.

In cases like these, strict requirements apply with respect to the legal basis, preparation and reasoning behind the proposal. The current proposal also violates the legitimate reasonable expectations of the owners that the Ministry has created when it comes to stable and predictable framework conditions.

In addition, the preparation of the proposal does not satisfy administrative law requirements.

9. CONCLUDING REMARKS

Solveig and Silex own 32% of the participating interests in Gassled and became owners with the intention of playing an active role as infrastructure owners and providers of long-term capital to the further development of gas infrastructure on the NCS.

We believe that the Ministry's stated objective should be met through more targeted measures which avoid the negative effects of the current proposal. The development and the timing of implementation of such measures would require an appropriate consultation process in order to better identify the causal link to resource management benefits. The Ministry should involve the relevant stakeholders in this process in accordance with common practice. Solveig and Silex are ready to participate in such a process.

Such dialogue should aim to establish long term solutions for the development of the gas infrastructure on the NCS that achieve the resource management objectives, protect the interests of all affected parties and facilitate access to long-term infrastructure capital on the NCS, building on a large range of tools, including:

- **Assess targeted measures suited for promoting production of marginal resources.** The aim would be to contribute to further development of socio-economic profitable resources and create incentives for:
 - Exploration in new areas
 - Development of marginal fields
 - Increase tail-end production from mature fields
- **Considering an extended licence period in order to reduce the transportation costs on the NCS.** This will contribute to resolving the need for prolonged repayment periods for the expected increased need for integrity investments (I-elements).
- **Improve profitability of marginal fields through developing a revised investment model for new infrastructure.** This will allow for more efficient allocation of upstream capital and infrastructure capital in connection with capacity expansions and opening of new areas on the NCS.

Based on the above we encourage the Ministry to initiate a broad and inclusive process to address the questions raised by the proposal and this response.

Solveig and Silex are ready to participate in such a discussion. The discussion should aim to establish a solution with a clear causal link to specific resource management requirements, protect the interests of all affected parties and secure the foundations of a stable and predictable platform for investors on the NCS.

We are looking forward to working with the Ministry in the coming months.
