



Commission for Energy Regulation

An Coimisiún um Rialáil Fuinnimh

Access Tariffs and Financing the Gas Transmission System

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Abstract:

The Commission for Energy Regulation (CER) is consulting on two matters:

- 1: A proposal to remove secondary capacity transfers at the exit;
- 2: A proposal to remove the ability to buy/transfer capacity “within day” at the exit.

The Commission for Energy Regulation is confirming its earlier decision to restrict secondary capacity transfers at the exit from 01 October 2013.

Related Documents:

- Gaslink Code of Operations
- **CER/07/115** - Short-Term Capacity Products Decision Paper
- **CER/10/089** – Decision on Transmission Exit Capacity Transfers in the Gas Market
- **CER/13/034** – Interim Review of BGN Allowed Revenues and Gas Transmission Tariffs for 2012/13 – Consultation
- **CER/13/080** - Interim Review of BGN Allowed Revenues and Gas Transmission Tariffs for 2012/13 – Decision

Responses to this consultation should be returned by email, post or fax and marked for the attention of James Mc Sherry (jmcsberry@cer.ie) at the CER.

The CER intends to publish all submissions received. Respondents who do not wish part of their submission to be published should mark this area clearly and separately or enclose it in an Appendix, stating the rationale for not publishing this part of their comments.

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Executive Summary

The gas network system provides the necessary infrastructure for gas to flow throughout the country, which ensures gas goes to homes and businesses as well as to the electricity generators that are needed to keep the lights on. The gas transmission system constitutes a significant part of the overall gas network, and capacity bookings on this system have been in serious decline for some months now. Bord Gais Networks (BGN) noted that decreases in capacity bookings were leading to a significant under-recovery in their 2012/13 allowed revenues. BGN forecasted a significant drop in exit capacity bookings in 12/13, falling by 18.5% on 11/12 levels at the Moffat Entry point. BGN noted that the decrease in bookings was directly related to the Power and Daily Metered (DM) sectors radically reducing their firm bookings.

As a result of this, tariffs for access to the natural gas transmission system have risen significantly since October 2012. A key driver has been the above noted significant reduction in primary capacity bookings. Tariffs are set by dividing the allowed fixed revenues by the expected bookings; if expected bookings decline, the tariff will rise. The recent unprecedented drop off in primary capacity bookings is, in the CER's view, unlikely to be a short term phenomenon. The gas network needs to be paid for if consumers, businesses and electricity generators want safe and secure supplies of gas. If the current pattern of capacity bookings continues, then without any remedial action there will continue to be increases in gas networks tariffs to the detriment of consumers. The CER, therefore, is consulting on measures that it considers will ensure that these increases in tariffs do not take place.

Another key consideration in carrying out this review is ensuring that the gas network system is remunerated in a fair and equitable way with any financial burden placed on customers being in proportion to the service provided to them. It is important that those who benefit from having access to the network pay their fair share of the cost of the network. It could be argued that the current levels of flexibility push the payment for infrastructure on to those who are either not offered any flexibility or who are not in a position to avail of this degree of flexibility.

The Decision Paper CER/13/080 sought to mitigate the under-recovery in transmission revenues by directing a mid-year increase in the transmission tariffs. It did not address any underlying issues relating to the drop off in bookings. This paper commences a consultation process which addresses potential structural changes on the demand side.

Primary capacity bookings are the core revenue base for financing Ireland's gas transmission system and will continue to be for the foreseeable future. Given this, this paper proposes to reduce the amount of flexibility offered to system users as a necessary means of increasing primary capacity bookings and restoring the transmission system revenue base on an equitable basis.

This consultation examines and consults on two primary issues in the gas transmission tariffs regime, both of which apply at the exit only:

- the potential removal of secondary capacity transfers at the exit from the gas transmission system.
- the potential removal of within day purchases/transfers of short term (including within day) capacity at the exit .

A number of alternative options to the above are also advanced for consideration. While the CER is not minded, at this stage at least, to implement these particular options (outlined in section 7), this thinking will be reviewed in light of comments received from the consultation exercise.

This paper also confirms that the decision in CER/10/089 "Decision of Transmission Exit Capacity Transfers in the Gas Market" to restrict secondary capacity transfers at the exit from 01 October 2013 still stands. This refers to capacity transfers within the same customer category i.e. Large Daily Metered (LDM) to LDM and DM to DM.

The transmission system is built to meet the 1 in 50 peak day requirements. This means that at most times there is a "surplus" of capacity on the system. This is costly. However, given the importance of ensuring a reliable supply of gas, it is appropriate, for security of supply reasons, to continue to build out the system to meet this standard. Continuing to ensure there is generally "surplus" capacity at the exit, while at the same time allowing surplus exit capacity to be transferred, reduces bookings on the exit and leads to higher tariffs and is (prima facie at least) economically inefficient. This is a key consideration in the potential removal of secondary capacity transfers at the exit.

The Joint Gas Capacity Statement 2012 indicates that power sector demand in Ireland will consistently be over 50% of the peak day demand out to 2021. The gas sector in Ireland has been built out in large part to meet the needs of the power sector. It was also noted in CER/13/034 that power bookings had fallen by 14%. Clearly if the power sector is booking less capacity then the burden of this will fall on the Industrial and Commercial (I&C) and residential

sectors. This is a key consideration in the potential removal of within day purchases and transfers of capacity at the exit.

To be clear, if secondary capacity transfers at the exit from the gas transmission system are removed as a result of this current consultation process, no secondary transfers at the exit shall be permitted, including those between the same category of customer outlined as part of CER 10/089.

1. Introduction and Background

1.1. *Introduction*

In January 2013 BGN made a formal submission to the CER requesting a mid-year tariff adjustment along with proposals which seek to redress this situation. BGN also outlined several factors which it considered contributed to the drop off in capacity bookings:

- Secondary capacity availability,
- Reduction in price for short term capacity during summer starting in 2013,
- Wind displacing gas off the merit order in the SEM,
- East West Electrical Interconnector (EWIC),
- Coal & Peat being in merit more than gas.

In CER 13/034 “Interim Review on BGN Allowed Revenues and Gas Transmission Tariffs for 2012/13” in February 2013 regarding the recent drop off in bookings and consequent erosion in transmission tariff revenues. A decision paper, CER 13/080, issued on this matter, outlining a 10.2% effective increase in gas network tariffs. This was implemented as an interim measure to raise tariffs in order to allow BGN recoup some of its expected under recovery while at the same time trying to mitigate and potentially negate future significant tariff rises.

The CER is concerned by the drop off in capacity bookings and erosion of this core revenue base.

The CER considered a number of means by which the under recovery could be addressed, such as;

- Raise network tariffs;
- Structural changes on the demand side;
- Reprofile revenues.

This current paper examines structural changes on the demand side, the potential removal of secondary capacity transfers at the exit, the potential removal of within day purchases of short term capacity at the exit and the

removal of within day secondary capacity transfers at the exit¹. These matters are examined in the context of the June 2010 CER decision paper CER/10/089 “Decision on Transmission Exit Capacity Transfers in the Gas Market”.

The CER would like to clarify that this paper considers the removal of secondary capacity **transfers** at the exit. Secondary capacity **trading** at the same exit point will be allowed to continue. For the purposes of this paper we define the following terms below²:

Capacity Transfer - An Exit Capacity Transfer is where a shipper transfers Primary exit capacity from one geographic location to another geographic location.

Capacity Trading - Capacity Trading refers to the trading of capacity (typically between shippers) at a single geographic location.

¹ In the event that secondary capacity transfers are removed this element may not be applicable

² More detailed definitions of these concepts, drawing from the Gaslink Code of Operations are available in Appendix A.

2. The Existing Regime

The facility to transfer transmission exit capacity was implemented in 1998 (before CER came into being in 1999 and was given gas regulatory functions in 2002) as part of the first transmission code of operations and there have been significant changes in the sector since then. At that time there were only ten or so third party access sites in the market and only annual primary capacity was available. Some of the customers had loads that peaked outside of the winter such as the sugar processing plants and the facility to transfer exit capacity was considered appropriate for those customers' specific needs. Since then a suite of regulated short term Monthly and Daily capacity products were implemented in 2007³ which give significant flexibility to the market.

The existence of secondary capacity also impacts on areas of the Connections Policy. Under the Connections Policy appraisals for new connections and new towns assume that primary annual capacity will be booked by all new customers and will not be transferred away from the site. However in some cases the new sites may not be booking primary annual capacity and in other cases the capacity may be transferred on. This can have an impact on the viability of new connections and can create a burden on other system users. Options to deal with this issue are to change the Connections Policy or change the policy on secondary capacity transfers at the exit.

Currently the transmission system is built to meet the 1 in 50 peak day requirements. The gas network system has been used to its fullest capacity, most notably on two occasions in 2010 when the 1 in 50 conditions occurred. The 1 in 50 requirement does mean, however, that at most times there is a "surplus" of capacity on the system. This is more costly than constructing the system to less than a 1 in 50 standard, but it is necessary, for security of supply reasons, to continue to build out the system to meet this standard. For instance, the network needs to be able to support high usage of gas in a severe weather period where consumers will use large quantities of gas to stay warm and generators will use large quantities to ensure the lights stay on in a situation of high electricity demand. Continuing to ensure there is generally "surplus" capacity at the exit, while at the same time allowing surplus exit capacity to be transferred, reduces bookings on the exit and leads to higher tariffs and is (prima facie at least) economically inefficient.

Table 1 below illustrates the difference between the 2012/13 expected bookings for certain sectors and the expected bookings at an average year

³ Short Term products from the transporter (monthly, daily, within-day1) were made available from 1st October 2007 following CER decision paper CER/07/115.

peak and a 1 in 50 year peak. It is expected that power generation will book only 70% of its projected peak capacity in 2012/13, compared to 98% of its actual peak in 2011/12.

| <i>Sector</i> | <i>Unit</i> | <i>2012/13 1-in-50 Peak Demand</i> | <i>2012/13 Average Year Peak Demand</i> | <i>2012/13 Expected Average Capacity Bookings</i> | <i>2012/13 Cap/Ave Peak</i> | <i>2012/13 Cap/1-in - 50 Peak</i> |
|-----------------|-------------|--|---|---|-------------------------------------|---|
| EXIT CAP | | | | | | |
| Total Power | MWh/d | 147,918 | 124,890 | 87,208 | 70% | 59% |
| DM I/C | MWh/d | 29,598 | 28,236 | 10,954 | 39% | 37% |
| NDM | MWh/d | 98,414 | 69,257 | 98,414 | 142% | 100% |
| Shrinkage | MWh/d | 5,307 | 5,307 | 5,307 | 100% | 100% |
| ROI Exit | MWh/d | 281,237 | 227,690 | 201,882 | 89% | 72% |

Table 1: 12/13 actual bookings V peak and average year expected demand

Transmission exit capacity is booked by shippers in accordance with their requirements and more specifically with Part C of the Code of Operations.

- Non Daily Metered (NDM)⁴ customers must book NDM exit capacity as advised by the transporter. Temperature sensitive customers must book capacity for a 1 in 50 year peak day adverse conditions. This means that at most times during the year the NDM sector has spare capacity that it isn't using.
- Daily Metered (DM)⁵ customers have discretion on the amount of capacity they book. They are however issued a transporter recommended exit capacity amount which they are not obliged to book.
- Large Daily Metered (LDM)⁶ customers book capacity in line with their own requirements subject to the transporter respecting overall system integrity.

At present shippers have the ability to transfer exit capacity as per the Code of Operations. Transfers currently can occur between shippers, between sectors and between individual LDM and DM sites.

There are significant volumes of exit capacity transfers executed within the gas market at present and the quantity has been increasing. Data from BGN has demonstrated that shippers are increasingly booking only 1kWh at the exit

⁴ NDM customers generally represent all the residential customers and the smaller Industrial & Commercial (I&C) customers.

⁵ DM customers represent the larger set of I&C customers.

⁶ LDM customers generally represent the power sector and a small number of the very largest industrial customers.

for their customers (and it is presumed booking secondary capacity and/or short term capacity at the exit).

While there may be benefits to the given suppliers and/or their customers this practice is pushing up the overall transmission tariff for everybody else as fewer firm bookings are made.

The CER is also concerned with what was termed “The Equity Issue” in CER 13/080⁷, quoted in part below:

‘A number of respondents considered “the inequity of energy users in the Daily Metered market segment and the domestic market who have not benefitted from lower capacity bookings made by suppliers now being asked to pay a tariff increase as a result of the reduction in capacity bookings in the Daily Metered segment and in the power generation sector”.’

Clearly if certain market sectors/customers book less primary capacity, then the burden of paying (for the full amount of capacity made available) will fall to the remaining sectors/customers. In other words a key consideration in carrying out this review is ensuring that the required system is remunerated in a fair and equitable way across customer categories with any financial burden placed on customers being in proportion to the service provided to them.

In February 2010, the CER published a Consultation Paper CER/10/037 “Review of Transmission Exit Capacity Transfers in the Gas Market” in which the current regime for secondary transfers of exit capacity was examined. Among the key issues which the Commission sought to address in this review was whether the rationale remained for continuing to allow such secondary transfers at the exit. The CER also questioned whether the use of such secondary transfers at the exit was efficient and equitable across the major categories of gas customers.

In June 2010 CER published a decision paper (CER/10/089) “Decision of Transmission Exit Capacity Transfers in the Gas Market” which announced a stepped increase in the price of secondary capacity at the exit. The CER also decided that secondary capacity transfers at the exit would only be permitted within the same customer sector with effect 1st Oct 2012.⁸ As part of this decision the CER stated *“it will continue to monitor closely trends in exit capacity bookings, as well as their potential impact, following this decision”*.

⁷ CER 13/080 section 2 page 10 “The Equity Issue”

⁸ CER/12/033 “the CER has decided to defer its implementation for 12 months, i.e. to October 2013.”

The CER notes that the PC3 decision proceeded, *inter alia*, on the basis that secondary capacity transfers would be restricted from 1st Oct 2013. CER/13/080 “Interim Review on BGN Allowed Revenues and Gas Transmission Tariffs for 2012/13” also proceeded on this basis.

For further background information and detailed explanations of how secondary capacity transfers at the exit works please see CER/10/037 “Review of Transmission Exit Capacity Transfers in the Gas Market”.

In summary, the proposals in this paper seek as a necessary, if potentially regrettable step, to reduce the amount of flexibility offered to system users under the existing regime, with a view to increasing primary capacity bookings. The CER is of the view that this will ensure the gas network can be efficiently financed and operated, as well as leading to a more equitable system of remuneration across the customer segments in proportion to the service provided.

3. Legislative Basis

Electricity Regulation Act 1999 (as amended)

Section 9 of the Electricity Regulation Act 1999 outlines the Commission's responsibilities with respect to natural gas. In carrying out the duty to perform its functions in a manner which protects the interests of final customers of gas (or electricity and gas),⁹ the Commission shall have regard to the need to secure that, inter alia,

- Licence holders are capable of financing the undertaking of licensed activities
- there is sufficient capacity in the natural gas system to enable reasonable expectations of demand to be met, and
- to secure the continuity, security and quality of supplies of natural gas.¹⁰

In carrying out its duties the CER shall also have regard to the objective to:

- develop competitive and properly efficient and reliable functioning regional electricity and gas markets,
- eliminate restrictions on trade including developing appropriate cross border transmission capacities to meet demand,
- promote system adequacy; and
- in fixing and approving tariffs or methodologies to ensure that system operators and system users are granted appropriate incentives, in both the short and long term to, inter alia, foster security of supply.¹¹

Furthermore, section 19A of the Gas (Interim)(Regulation) Act 2002 sets out the functions of the CER to protect security of supply of natural gas and to establish policies to ensure adequate levels of security of supply.¹²

European Union Law

The CER must perform its gas regulatory functions in compliance with relevant EU legislation. European legislation imposes requirements to facilitate **trading** of capacity at interconnection points, i.e. those points that connect two systems. As previously outlined, this paper refers to the removal of **transfer** of capacity between exit points. Transfer of capacity at the exit is not covered under this legislation.

⁹ See section 9(3) Electricity Regulation Act 1999 (as amended by section 6 of the Gas Interim Regulation Act 2002.

¹⁰ See section 9(4)(a) Electricity Regulation Act 1999 (as amended by Regulation 40 of SI 630 of 2011.

¹¹ See section 9(5) Electricity Regulation Act 1999 (as amended by Regulation 40 of SI 630 of 2011.

¹² See section 19A of the Gas (Interim)(Regulation) Act 2002 as inserted by Regulation 5 of SI 697 of 2007

Regulation No. 715/2009 EC ('the Regulation') on conditions for access to the natural gas transmission networks has two specific articles which concern secondary trading and transfers:

- Article 16 – 3(b) *“network users who wish to re-sell or sublet their unused contracted capacity on the secondary market shall be entitled to do so”*
- Article 22 – *“Each transmission, storage and LNG system operator shall take reasonable steps to allow capacity rights to be freely tradable and to facilitate such trade in a transparent and non-discriminatory manner. Every such operator shall develop harmonised transport, LNG facility and storage contracts and procedures on the primary market to facilitate secondary trade of capacity and shall recognise the transfer of primary capacity rights where notified by system users.”*

Article 16 deals with cross borders trades¹³. Article 16 does not, therefore, apply to this CER proposal to remove secondary capacity transfers at the exit. The Article specifically relates to procedures which “facilitate cross-border exchanges in natural gas”. From this reading of the Regulation, Article 16 requires network users be allowed to conduct secondary trade of capacity at interconnection points. Removing capacity transfers at the exit in Ireland would not impact on the application of Article 16 of the Regulation in Ireland.

The *Third-party access services concerning transmission system operators*, Guidelines in Annex 1 of the Regulation state:

1. *Transmission system operators shall offer firm and interruptible services down to a minimum period of one day.*

The CER considers that the proposal to remove the ability to buy/transfer capacity “within day” at the exit does not contravene this.

¹³ This is clear from the opening sentence of Articles 16.3, which states:
The transmission system operator shall implement and publish non-discriminatory and transparent congestion-management procedures which facilitate cross-border exchanges in natural gas on a non-discriminatory basis....

4. Restriction of Capacity Transfers at the Exit

This paper confirms that the decision in CER/10/089 “Decision of Transmission Exit Capacity Transfers in the Gas Market” to *restrict* secondary capacity transfers at the exit from 01 October 2013 still stands¹⁴. This refers to capacity transfers within the same customer category i.e. LDM to LDM and DM to DM etc.

The reasons for the above decision have been set out in CER/10/089.

The CER is of the view that no clear evidence has emerged to suggest that this decision should be rescinded or reconsidered. In fact the recent significant decline in bookings and the consequences of this decline emphasise the need for reform of secondary capacity transfers at the exit as decided in CER/10/089 and indeed this paper consults on further changes to such transfers.

If secondary capacity transfers at the exit from the gas transmission system are *removed* as part of this current consultation process, no secondary transfers at the exit shall be permitted, including those between the same category of customer outlined as part of CER 10/089.

Secondary capacity trading at the same exit point will be allowed to continue as trading is not under examination in this consultation.

¹⁴ The consultation CER13/034 which highlighted potential tariff rises, assumed that the decision to restrict secondary capacity at the exit would be implemented. If the decision to restrict secondary capacity was reversed it would be expected that the tariff rises would have been higher than those in that paper.

5. Proposal 1: Removal of All Secondary Transfers at the Exit

If secondary capacity transfers at the exit were removed, primary capacity bookings could be expected to increase. This in turn would help to lower the unit tariff for gas transportation from what it would otherwise be. It would go some way to address the equity issues as described in section 2.

CER/10/089 “Decision of Transmission Exit Capacity Transfers in the Gas Market” allowed secondary capacity to continue to be transferred with the restriction that it could only be transferred from one DM site to another or from one LDM site to another.

In this section we examine some of the reasoning outlined for allowing these transfers to continue. Issues from the 2010 paper are highlighted and the CER response in 2010 is given. The CER’s updated views on the issues are added in boxes.

The responses to the 2010 consultation process (CER/10/089) cite several¹⁵ reasons for allowing secondary transfers to continue, these were discussed under the following broad headings:

- Developments in Electricity Power Generation
- Barrier to Entry
- Interaction between secondary trading and the retail market.
- Use of Excess Exit Capacity
- Impact of Secondary Capacity regime on the Connections Policy
- Restrictions on Within Portfolio Capacity Transfers

Taking each point in turn we look back at the issues and identify (initial) updated CER views.

Developments in Power Sector Generation¹⁶

Issue considered in CER 10/089:

Power generators noted that gas fired plants are increasingly moving away from operating under base loads conditions due to high levels of renewable generation entering the electricity market. Generators therefore argued that given this circumstance generator should be allowed to transfer spare capacity if they were not called on to run.

¹⁵ Please note not all reasons from section 4 of CER/10/089 will be discussed as some of them were specific to the old BG Energy RTF tariff product.

¹⁶ Section 4.2 (i) of CER/10/089

Respondents argued that not allowing this flexibility would in turn push up electricity prices for end consumers.

CER response in CER 10/089:

In CER/10/089 the CER said it was minded to allow transfers within the same customer sector e.g. secondary capacity may pass from one LDM exit point to another LDM exit. This was regarded as an efficient use of capacity at that time.

2013 Update

The CER has monitored power sector bookings over the past three years. Since the decision in 2010 to restrict secondary capacity transfer to between sectors, the use of secondary capacity has become more prevalent. This has resulted in a large drop off (projected Power gen will book only 70% of its required capacity in 2012/13 down from 98% of its actual peak in 2011/12) in capacity bookings. This paper is consulting on the removal of secondary capacity transfer between exit points. This will mean a power station which holds exit capacity cannot transfer its spare capacity to another LDM. As outlined in Table 1 in Section 2, power stations are booking just 59% of the 1 in 50 peak amount.

The removal of the ability to transfer exit capacity from one LDM to another LDM would certainly reduce the flexibility offered to power stations (and other LDM customers). It should be noted that as this consultation only refers to exit capacity, power stations would still be able to freely trade capacity they hold at entry point to eligible parties at that point. It could be argued that providing for the current levels of flexibility simply pushes the payment for infrastructure to those who are either not offered any flexibility (NDM customers in particular) or to those who cannot profit from using the flexibility.

Barrier to Entry¹⁷

Issue considered in CER 10/089:

Some market players have said that access to secondary capacity has allowed for competition to develop in the gas retail market. On the other hand there are others who said the secondary capacity can create a barrier to entry. Another noted that in the long term if little margin is available to shippers as a result of changes to the market (such as the removal of the secondary capacity regime), shippers may need to be in the gas production sector and competition would be limited to such parties.

¹⁷ Section 4.2 (ii) of CER/10/089

CER response in CER 10/089:

In CER/10/089 CER recognised that not all shippers in the market utilise secondary capacity transfers and therefore do not currently benefit from its use.

CER also noted that if exit capacity transfers are restricted to within the relevant sector (i.e. LDM to LDM and DM to DM), this would remove the barrier to entry that could otherwise exist where it would be necessary to have access to NDM secondary capacity to compete in the DM sector.

Further to the above the CER stated “it will continue to monitor closely trends in exit capacity bookings, as well as their potential impact, following this decision”.

2013 Update

As can be seen from CER market publications since 2010, competition has increased; Airtricity and Electric Ireland have both entered the gas retail market and taken considerable share away from BG Energy. This increase in competition has occurred while secondary capacity transfers were still allowed (and unrestricted) at the exit. This might question somewhat, the importance of such transfers as a barrier to entry.

Nevertheless in 2010 it was noted that disallowing transfers of “spare” exit capacity out of the NDM sector might remove a barrier to entry as noted above. To the extent that there is any barrier to entry created by such transfers, continuing to allow capacity to be transferred between LDM sites may simply leave another barrier to entry, where it is necessary to have existing LDM customers in order to gain any new LDM customers. This current consultation is examining the removal of all secondary capacity transfers at the exit, including those transfers between customers belonging to the same category.

Use of ‘Excess’ Exit Capacity¹⁸

Issue considered in CER 10/089:

A number of respondents on this matter put forward instances in which transfers of secondary capacity are appropriate and should be maintained. Two respondents stated that suppliers should be permitted to sell on firm exit capacity that they deem surplus to requirements and

¹⁸ Section 4.4 (ii)

that this should be treated separately to interruptible '1 in 50' exit capacity offered by NDM shippers. Another party noted that this approach is particularly warranted in order to manage customer movements, for example where a supplier loses a customer, they should be able to sell on this surplus exit capacity.

CER response in CER 10/089:

The CER considered that secondary sales of exit capacity may be acceptable in cases where the original user of the capacity is effectively substituted by another party, i.e. when a customer moves from one shipper to another, or the shipper's net portfolio benefit changes, or when one gas-fired generating station replaces another that has come offline. As was noted by Bord Gáis Networks, the transfer of exit capacity by shippers in this manner is not economically inefficient provided that the aggregate capacity held does not exceed the physical capability of the exit point. In other words to create a situation where say 2 shippers held 100 units of capacity each for a particular site which had a demand of only 100 units would be inefficient]

2013 Update

It would seem appropriate that where a customer holds capacity at a given point (or has capacity held for them at that point), and changes shipper, then this capacity should move with the customer. This is (broadly) how capacity is dealt with on change of shipper at the NDM level. This is colloquially called the "rucksack rule", the customer carries the capacity with them when they move.

Rather than retain secondary capacity transfers at the exit to deal with such changes of shipper, the CER's initial thinking is that it would be better to implement a similar "rucksack rule" for DM and LDM capacity.

Impact of Secondary Capacity regime on the Connections Policy¹⁹

Issue considered in CER 10/089:

One party noted that the Transporter should take into account likely activity in the secondary capacity market when developing the network. Two respondents proposed that a limitation be placed on the amount of secondary capacity available at each exit point and two other respondents suggested the introduction of restrictions on the use of secondary capacity at new connections until the connection cost has been recouped. One of these stressed that, where a pipeline is built to service a given load of a customer, it should be the responsibility of that

¹⁹ See section 4.4 (v) of CER/10/089

customer to pay for this additional capacity. This proposal was taken further by another respondent who noted that, in conjunction with such a restriction, an obligation could be introduced on the customer to fund a fixed element of the total cost over a seven year period. Alternatively, additional charges could be levied on exit capacity that is transferred away from the new connection

CER response in CER 10/089:

CER is interested in the proposals made regarding potential changes to the connection Policy. These proposals may be beneficial in ensuring that new pipelines are built to service a given load. Nevertheless, it is not considered that modifications to the Connections Policy would in themselves resolve all of the inefficiencies associated with secondary capacity.

2013 Update

The existence of secondary capacity impacts on areas of the Connections Policy. Under the Connections Policy appraisals for new connections and new towns assume that primary annual capacity will be booked by all new customers and will not be transferred away from the site. However in some cases the new sites may not be booking primary annual capacity and in other cases the capacity may be transferred on. This can have an impact on the viability of new connections and can create a burden on other system users.

It could be said that making changes to the connections policy while retaining the ability to transfer capacity at the exit would be to treat a symptom (the connections policy) rather than dealing with the underlying issue (the presence of transfers at the exit). In other words modifications to the Connections Policy would not in themselves resolve all of the inefficiencies associated with secondary capacity.

The CER considers that it is more appropriate to change the policy on secondary capacity transfers rather than changing the connections policy in light of the continuing presence of secondary capacity transfers at the exit.

Restrictions on Within Portfolio Capacity Transfers

Issue considered in CER 10/089:

There was no consensus amongst respondents regarding restricting the transfer of exit capacity within a shipper's portfolio.

One respondent strongly rejected any such requirements. Another argued that such a modification is necessary in the event that the ability to transfer capacity to other suppliers is also removed. A separate shipper stated that, should the ability to transfer capacity from one shipper to another be removed, it is imperative that such transfers within a supplier's portfolio are also prohibited due to the competitive advantage that would be afforded to BG Energy.

CER response in CER 10/089:

The Commission considered that common sectoral rather than shipper focussed restrictions on secondary capacity sales was the minimum required changes at that time and constituted the fairest approach in modifying the current regime. This approach is considered more appropriate as it would remove the cross-subsidisation of NDM capacity by certain industrial customers and power generators.

2013 Update

It is worth noting in the response above that the sectoral change proposed was described as "the minimum required changes at that time". Since then there have been significant changes in the market for transmission capacity, including significant declines in bookings. In the light of these changes the CER considers that it is now appropriate to consider the removal of secondary capacity transfers at the exit.

6. Proposal 2: Restriction on latest time of purchases and transfers of capacity at the exit

In this section the CER considers the case for removing 'within day' products for capacity at the exit. This refers to both primary capacity bookings at the exit and the transfer of secondary capacity at the exit. The objective of removing 'within day' products at the exit is to increase primary bookings at the exit. It is undeniable that the removal of these within day products would reduce flexibility with respect to capacity at the exit, but it may be that the cost of this current flexibility is tariffs that are higher than they otherwise would be.

On 18th April 2008 Code Mod(A)027 was implemented which allowed for within day purchases of short term capacity at the exit (and also at the entry). On 13th October 2010 Code Mod(A)042 was implemented which moved the latest time for purchases of this within day short term capacity at the exit (and also at the entry) to 03:00 on the trading day. This is 1 hour and 15 minutes after the deadline for purchase of secondary capacity at the exit.

Both of these Code Mods were introduced to offer flexibility to those booking gas capacity. Together the two Code Mods allowed shippers to delay finalisation of capacity purchases up to 21 hours into the gas day itself. Further, together the two code mods mean that 19 hours and forty four minutes into the gas day a shipper still has both a primary and a secondary market at which to buy capacity. Even if this deadline is missed the shipper still has further time to purchase short term capacity from the transporter. Given the fact that there is no evidence of congestion at the exit, there is little or no likelihood that capacity will be unavailable to the shipper. In this way, effective assurance that primary capacity can be purchased at the exit with as much as 7/8th of the day gone, means there is very little risk in optimising capacity portfolios.

This flexibility was introduced in response to shipper requests. The flexibility of within day purchases was considered useful in the light of the expected movement of CCGTs to mid merit as wind penetration increased. It is reasonable to conclude that the recent significant drop off in capacity bookings at the exit is facilitated by the presence of both within day primary and secondary capacity sales. In light of these recent issues the CER is considering the removal of the ability to purchase short term capacity at the exit within day. Similarly, the CER is considering the removal of the ability to transfer secondary capacity at the exit within day (this could be effected in place of the removal of such transfers or in advance of the implementation of the removal of such transfers).

For the avoidance of doubt, the CER is not currently considering any changes to either short term capacity purchases or secondary capacity trades at the entry. It is only at the exit that CER is considering any such changes. To be clear, if this proposed change was made, daily short term capacity bookings would still be available at the exit. Similarly, absent the removal of all secondary capacity transfers at the exit (Section 5), secondary capacity transfers at the exit would still be facilitated to periods of a day. Transfers would not be available on the day however.

The question of when to close the window for daily products would then arise. The CER is anxious not to remove a disproportionate amount of flexibility. To this end the CER is proposing to facilitate the purchase of daily products on a day ahead basis (D-1).

The next issue to consider is the time that the windows will close. The matter of when to close the window is particularly relevant for the power generation sector.

The Joint Gas Capacity Statement 2012 indicates that power sector demand in Ireland will consistently be over 50% of the peak day demand out to 2021. The gas sector in Ireland has been built out in large part to meet the needs of the power sector. It was also noted in CER 13/034 that power bookings had fallen by 14%. Clearly if the power sector is booking less capacity then the burden of this will fall on the I&C and residential sectors.

It is clear that a significant proportion of the gas network infrastructure has been made available (and continues to be available) to supply the power sector. Any attempt on the part of CER to increase bookings on the system, will inevitably affect the power sector and certain aspects of any such efforts may focus on the power sector. In considering this particular proposal, the CER is focussing on the power sector and is seeking to increase the level of bookings from the power sector.

Under the prevailing gas capacity regime in Ireland, a gas fired power station has the flexibility to choose to buy gas capacity only when it runs²⁰. In fact the capacity is present and available on the system whether or not the station runs and must be remunerated. Thus it could be argued that the power sector is not booking the appropriate amount of capacity and the cost of offering this flexibility to the power sector falls upon other users in the gas system.

The present proposal would alter the situation such that the station would hold the capacity whether or not it runs. Illustrating this point by an analogy; an oil

²⁰ Conversely if it has capacity and does not run it may sell this capacity to others.

fired power station needs an oil tank and must pay for it, whether or not it runs; a coal fired power station needs a coal bunker and must pay for it, whether or not it runs. It can be said that a gas fired power station needs gas capacity to be available whether or not it runs. The fact that the gas delivery system is owned by another entity and is subject to Third Party Access does not change the fact that the capacity is made available and must be remunerated by some party. This proposal seeks to ensure that the power sector makes appropriate contributions to the remuneration of the gas system.

Increasing the bookings from the power sector may bring long term security of supply benefits to the power sector. While there may be ample capacity available on the gas system at present, this situation cannot reasonably be expected to prevail in the long term if the burden of remunerating the system falls on sectors outside the power sector. Over time the pressure to reduce “high” tariffs could be expected to reduce the overall level of capacity on the gas system (i.e. re-enforcements needed to maintain the current level of security of supply would not be made). Thus in the long term the security of electricity supply (at least that part that is gas fired) could no longer be relied upon.

Currently the rules concerning short term capacity and secondary capacity are different in Ireland and Northern Ireland. In Northern Ireland there is no transfer of secondary capacity and daily capacity must be booked 12 days in advance.

In choosing the latest time to “close the window” for short term capacity and secondary capacity, the CER proposes to move the deadline for purchases of short term capacity and for the transfer of secondary capacity to 09:00 at D-1. The CER considers that the proposal to remove within day flexibility at the exit would assist it in increasing exit bookings on the gas transmission system. This could be justified on the grounds of increasing bookings from the power sector to a level commensurate with the services provided to the power sector.

The proposed removal of within day flexibility may also impact on other users of the system. Shippers might purchase within day capacity to avoid overrun charges on their DM books or at individual LDM sites. Similar to the above, a reduction in flexibility can be expected to increase bookings on the system.

In summary, the CER is considering curtailing the flexibility offered to shippers in an effort to increase primary capacity bookings at the exit generally.

7. Alternative Options to those examined in this paper

This section examines alternative options to address the principal concerns outlined in this paper i.e. the fall in primary capacity bookings at the exit and in this context the remuneration of the system on a fair and equitable basis. The CER is not currently considering these options, though comments from respondents on these alternatives are welcome.

Mandatory Bookings

NDM customers have no flexibility with regard to booking of exit capacity, NDM shippers are mandated to book the transporter determined quantity. An alternative possibility to the removal of secondary capacity transfers at the exit is to bring in mandatory bookings for power generators and/or all customers above NDM.

Mandatory bookings could be considered for the power sector only for security of electricity supply reasons. This could be consistent with the CER's objective to "keep the lights on". Underlying this is the argument posed earlier that oil fired stations need an oil tank and therefore gas fired stations need gas capacity to be available.

If mandatory bookings were applied to the power sector only this would leave the I&C sector as the only sector which had flexibility in bookings.

If mandatory bookings were applied to all customers (Power, I&C in addition to NDM) it could be done for "equity" reasons. In this way it could be considered that all parties would pay their "fair share" of the costs. The key issue would be in determining what is a "fair share".

The key issue with mandated bookings is that the level of these bookings would have to be externally determined (by the Transmission System Operator, for example) on an individual site basis. This would deny individual participants the ability to make their own judgements. The process of checking the level of mandated bookings would not be a straightforward process and could lead to a significant number of disputes.

In conclusion, the introduction of mandatory bookings would likely be problematic and more significantly, would have the effect of removing all flexibility, while the proposals in this paper are limited to reducing flexibility.

Removal of Mandatory Bookings for NDM

An alternative is to consider removing mandatory bookings for NDM, this way all parties can optimise (at the moment, all but NDM can optimise, leaving NDM to pick up the burden left by optimisation).

However decreasing the bookings from the NDM sector may bring long term security of supply issues. While there may be ample capacity available on the gas system at present, this situation cannot reasonably be expected to prevail in the long term. If the “1 in 50” capacity is not being booked, then it is reasonable to expect that over time the capacity may not be in place to meet this demand when the occasion arises. As noted before, over time the pressure to reduce “high” tariffs could be expected to reduce the overall level of capacity on the gas system (i.e. re-enforcements needed to maintain the current level of security of supply would not be made). Thus in the long term the security of supply to residential customers could no longer be relied upon.

An issue of equity would also need to be considered, where the NDM demand can be more variable than, say, the I&C demand. If the system was built to be big enough to supply the 1 in 50 standard and if all parties could optimise, then the I&C sector could be considered to be cross-subsidising the more variable NDM demand.

Long Term Booking Incentives

Consideration could be given to the case for enhanced incentives towards long term bookings (for the above NDM sectors). This could involve changes to multipliers for short term products, to incentivise longer term bookings.

In the EU there is a push towards having the annual cost of short term capacity at Interconnection points between systems in the range of 1 to 1.5 times the cost of an annual strip of the same amount of capacity. In this consultation, of course, it is tariffs at the Irish exit that are under consideration, so any such considerations may not be applicable. The existing multipliers for short term capacity are outlined in **Appendix B**. This includes a (recently introduced) significant discount for summer short term capacity. It would seem logical that increasing short term capacity tariffs would tend to move shippers towards longer term bookings and that any such move could assist CER in its current endeavours.

On the other hand, however, increased use of the gas system in the summer time would increase overall throughput on the system, without incurring any additional infrastructure costs. It is in the light of such potential efficiencies that CER proposed lowering the cost of short term capacity in the

summertime. In the Decision Paper CER 12/143 this was described as being in line with the following objectives:

- the potential for summer peakers to cost-effectively utilise the gas transportation system;
- facilitating greater seasonal utilisation of gas storage by shippers;

The options described in Sections 5 & 6 above seek to promote primary bookings. The options are neutral as regards to these bookings being long term or short term primary bookings.

Rather than tend to increase primary bookings in themselves, increasing the cost of short term tariffs would tend to alter the balance between long and short term primary bookings.

Respondents may consider that the options of changing multipliers for short term tariffs should be considered in depth by CER. In the event of considering changing these multipliers, the CER would be anxious to maintain the recently introduced incentives towards increased utilisation of the gas system in summer months.

8. Responding to the Consultation

The CER invites comments on this topics presented in this paper Comments from interested parties to be submitted no later than 5.00pm on Monday 15th July 2013. Comments should be sent, preferably in electronic format to;

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The Exchange
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Tallaght
Dublin 24
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The CER intends to publish a decision paper following this consultation process whereupon any required modifications to the Gaslink Code of Operations would be commenced as outlined below.

The CER intends to publish all comments received – those respondents wishing for certain sections of their submission to remain confidential should submit the relevant sections in an appendix marked confidential.

Should the CER conclude from this consultation exercise that secondary capacity transfers at the exit should no longer be permitted, it would issue a direction to Gaslink pursuant Section 14 of the Gas (Interim) Regulation Act 2002. The Gas Code of Operations would have to be amended to reflect such a direction.

Should the CER conclude from this consultation exercise that the latest time for purchase of primary capacity at the exit and the transfer of secondary capacity at the exit should be changed, it would issue a direction to Gaslink pursuant Section 14 of the Gas (Interim) Regulation Act 2002. The Gas Code of Operations would have to be amended to reflect such a direction.

Appendix A:

Code of Operations – Relevant Definitions

It is useful to examine the following definitions from the Gaslink Code of Operations:

Part C : 1.1.15

“Secondary Capacity” : Secondary Capacity means capacity of an individual category that is held by a Shipper on a Day pursuant to an Entry Capacity Trade (which shall be made with respect to the same Entry Point) or an Exit Capacity

Transfer in respect of the Day or a LDM Supply Point Capacity Title Transfer (which shall be made with respect to the same LDM Supply Point) for the Day as the case may be;

Part C 8.1.1

“Exit Capacity Transfer” means the transfer by a Transferor Shipper of Retained Primary Exit Capacity to a Transferee Shipper to increase such Transferee Shipper’s Active LDM Exit Capacity or to increase the Active DM Exit Capacity or Active NDM Exit Capacity of the Transferee Shipper.

Part C 3.1.2

"Entry Capacity Trade" means an arrangement between a Transferor Shipper and a Transferee Shipper whereby certain of the rights of the Transferor Shipper in relation to Entry Capacity may be exercised by the Transferee Shipper in accordance with the provisions of this Code and the Transferee Shipper shall be subject to certain obligations in relation to such capacity.

Part C 5.1.

“Entry Point Transfer” means A Shipper may in accordance with the following provisions of this Section 5.1 transfer all, or part, of its Primary Entry Capacity held pursuant to an Entry Capacity Booking which is Multi-Annual or Annual in duration (but excluding any Primary Entry Capacity booked pursuant to a Treaty

Entitlement) from an Entry Point (the "Original Entry Point") to an alternative Entry Point or to a Proposed Entry Point (the "New Entry Point") by way of a transfer of Entry Capacity to such New Entry Point ("Entry Point Transfer") in accordance with Section 5 of the code.

Appendix B Short Term Tariff Information.

Short term capacity is priced at a percentage of primary annual capacity. The short term multipliers are included in the table below.

| Short Term Tariff Multipliers | Monthly | Daily |
|--|--------------------------|--------------|
| October | 13.2% | 0.66% |
| November | 13.2% | 0.66% |
| December | 17.6% | 1.18% |
| January | 30.9% | 2.06% |
| February | 35.3% | 2.35% |
| March | 26.5% | 1.76% |
| April | 13.2% | 0.66% |
| May | 1.0% | 0.05% |
| June | 1.0% | 0.05% |
| July | 1.0% | 0.05% |
| August | 1.0% | 0.05% |
| September | 1.0% | 0.05% |
| Total Percentage of Annual Tariff | 155%²¹ | 289% |

²¹ Any difference in the total is due to rounding.

