

NTS Exit Reform

Responses to consultations

Bord Gáis Networks

December 2006

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1. Introduction

This document sets out the response of Bord Gáis Networks (BGN) to the consultation on the Uniform Network Code (UNC) modification proposals “Reform of the NTS Offtake Arrangements” (Ref. 0116V and associated proposals). BGN makes this response in its capacity as operator of the network downstream of Moffat.

There are a number of further consultations associated with NTS exit reform relating to charges (NTS GCD 01/02/03 and NTS GCM01), the Exit Capacity Release Methodology Statement (ExCR), and licence modifications. BGN believes that the issues surrounding NTS exit reform should be considered together rather than separately and its responses to these consultations are therefore also included in this document.

BGN remains concerned over the NTS exit reforms proposed by Ofgem and National Grid NTS on the basis of the adverse impacts on arrangements downstream of the Moffat exit point. More particularly, BGN has serious reservations over two core elements of the proposals:

- The treatment of (flat) capacity and the proposed user commitment approach
- The introduction of a flexibility capacity product

Our detailed comments on these two aspects are set out in the sections 2 and 3 below. We then summarise the BGN position and state our preferences with regard to the various modification proposals in section 4.

2. Flat capacity and the user commitment approach

Overview

Our fundamental concern is that NTS users at Moffat are not best placed to signal forward NTS exit capacity requirements and therefore the proposed user commitment model may not, in the case of Moffat, realise the intended benefits of improved security of supply and reduced stranded assets. On the contrary, we believe that implementation of the proposals in their current form could adversely impact on the security of supply arrangements for the three separate jurisdictions downstream of Moffat, and act as a barrier to new entrants, hindering the development of competitive downstream markets.

Given the extremely high dependency of downstream gas and electricity consumers on capacity availability and gas flows at Moffat it would be unwise to leave Moffat capacity booking processes solely in the hands of NTS shippers. It would clearly be difficult for all individual NTS shippers to make a reliable assessment of, and commitment to, the collective requirement for future Moffat capacity given the dynamic of competitive downstream markets. We note that facing similar (although not identical) issues it was decided that NTS exit capacity for DNs should be booked by the DN operator rather than individual shippers. BGN believe that a single party acting as aggregator at Moffat will be of benefit. However, subject

to on-going Industry discussion in Ireland, there may be a requirement for parties other than the single party to book NTS Exit Capacity. We outline below the changes to the current user commitment proposals that would be required to facilitate the planning and operational processes necessary for the efficient onward transmission of gas downstream of Moffat.

Accommodating both “single party” and “independent” NTS exit capacity bookings

BGN has identified adverse impacts downstream of Moffat associated with the UNC modification proposals (other than mod 0116A) as highlighted in the overview above. For some time now BGN has been discussing potential solutions with industry participants operating downstream of Moffat, the Commission for Energy Regulation, Ofreg, the I.O.M, Ofgem and National Grid NTS.

The concept of a “single party (SP)” (probably a Bord Gáis Éireann (BGE) entity) becoming responsible for booking NTS exit capacity at Moffat on behalf of downstream market participants has been explored and developed. An arrangement was considered whereby the SP reserves NTS exit capacity under an ARCA, leaving NTS shippers to actually book the capacity, but there were some difficulties in ensuring appropriate recovery of capacity costs. An alternative whereby the SP becomes a UNC User and books NTS exit capacity directly is now contemplated and recommended in a recent CER position paper.

The current UNC modification proposals appear to accommodate an SP capacity aggregator role but the construction of the rules seems to assume an exclusive NTS capacity booking role, in that the “overrun user” (i.e. the SP) becomes responsible for all overruns at an exit point at this stage of consultation in the Irish Gas Industry, it is not clear if the single party should act in an exclusive capacity. We think it important for now that the regime should accommodate “independent” bookings as well as an SP aggregator role. Indeed, both Ofgem and National Grid NTS have confirmed in recent discussions that any NTS shipper will be able to book NTS exit capacity at Moffat and this inevitably points to a non-exclusive NTS capacity booking role for the SP.

Assuming this important principle is necessary and accepted, there will need to be consequential adjustments to the proposals to enable the appropriate allocation of responsibility and exposure between the SP and independent NTS capacity bookers, in particular in relation to overrun rules. BGN is available to engage with NG to discuss suitable options.

Initial prevailing rights

UNC shippers booking NTS Exit Capacity on behalf of shippers downstream of Moffat did so under a Capacity Register and 'Ticket to Ride' process at Moffat. Under the current 116 Flat Capacity proposals, this would grant the UNC shippers at Moffat Prevailing Capacity Rights. However the shippers downstream of Moffat who entitled the UNC shippers to book the NTS Exit Capacity from NGG (through the 'Ticket to Ride' process) would be granted zero Prevailing Rights. We believe that initial prevailing NTS exit capacity rights at Moffat should not be confined solely to NTS shippers but should rather recognize the downstream market participants.

As we are proceeding with a Single Party (SP) solution downstream of Moffat, we also believe it important that initial prevailing rights be conferred on the SP.

Decreases to prevailing rights

We believe that under the proposed rules prevailing rights decreases could in certain circumstances reduce the capacity available at Moffat at short notice (14 months), and the SP would not have an opportunity to step in and make good the reduction. For example, if allocations were above baseline at Moffat and a subsequent prevailing rights decrease (by NTS shipper(s) other than the SP) reduced allocations below baseline, then National Grid NTS would only be obliged subsequently to make available capacity up to the baseline. There appears to be no release mechanism whereby capacity allocations can be restored to the previous above baseline level through capacity applications by the SP (or any other NTS shipper).

This is a concern for us as the SP may be responsible for ensuring aggregate capacity availability at Moffat remains at a particular level. We believe that the rules should be amended so that in these circumstances the previous above baseline capacity level is made available for release.

Flat capacity charge proposals and exit capacity release methodology

We have reviewed the charging proposals for flat capacity set out in National Grid NTS documents NTS GCM01, NTS GCD01, NTS GCD03 and the Exit Capacity Release Methodology Statement and make the following points:

Capacity prices for prevailing rights

We are concerned that under the user commitment approach, NTS shippers (and in the case of Moffat the SP) will be required to financially commit to requested levels of capacity for a period of years, but at an uncertain price. We recognise that the exit capacity release methodology attempts to address this by couching the user commitment in terms of a monetary sum based on exit capacity prices at the time the commitment is made, but this falls short of providing the certainty required, and is in contrast with the entry capacity arrangements where all long term bookings are made at a known price.

An important principle here is that when users request increases or notify decreases in prevailing rights then the price payable is known and fixed, because both quantity and price are equally important parameters in the decision processes relating to capacity. However, the proposals appear to favour National Grid NTS (by requiring fixed quantities) but leave users with the risk of price movements. We believe it would be appropriate to fix the price payable for at least the first year of prevailing rights increments at the time the commitment is made. Likewise, when prevailing rights decreases are notified on 14 months notice, the price that would otherwise be payable should be fixed.

Capacity reserve prices for annual and daily auctions

We agree that reserve prices should not be discounted in the interests of ensuring, as far as possible, a limited need to address under-recovery through TO commodity charges. However, we believe that under the proposed methodology reserve prices and prices payable for prevailing rights may differ because prevailing prices are updated immediately prior to the year of usage, whereas some reserve prices are set earlier based on estimates of what the prevailing price will be. This creates inconsistencies and should be addressed through amended rules.

We are also concerned that interruptible capacity will be made available at zero reserve price as this could lead to significant under-recovery that would need to be addressed through an untargeted TO commodity charge and could undermine the provision of forward capacity signals. An alternative would be to offer interruptible capacity only once all firm baseline had been sold, thus avoiding any concern about capacity hoarding without creating unnecessary revenue uncertainty.

Cost recovery

More generally, we are concerned at the proposals to move towards an exit regime that to some extent mirrors the entry regime, under which cost recovery has been a significant issue. Both over and under-recovery have at different times been evident in the entry regime and we are very concerned that similar uncertainty (involving largely arbitrary recovery mechanisms) could become a feature of the exit regime.

Charging methodology

In our view key factors in relation to charging methodology are transparency and stability of the resulting charges. The “Option 1 – Transportation Model approach” appears to better meet the transparency requirement but we question the degree of stability given that the indicative Moffat NTS exit capacity charges increase by a factor of 21 over the course of a year.

SO NTS exit (flat) commodity charge

We believe that the SO NTS exit (flat) commodity charge should not be reduced, consistent with our view (set out in section 3) that there should be no SO NTS exit (flexibility) commodity charge.

Information provision

Throughout the various consultation processes relating to NTS exit reform we have sought information to assist us in making a proper appraisal of the proposals. We have generally been disappointed at the reluctance of National Grid to make more information available. In the context of the flat capacity product it would be extremely helpful if the following could be provided:

- Details of baseline derivation methodology employed;
- Historic and forecast flat capacity availability and usage at Moffat;
- Historic and forecast flat capacity prices for Moffat (under all charging methodologies being considered);
- Details of transfer/ substitution methodology to be used to derive exchange rates; &
- Indicative forecast exchange rates for capacity substitution to and from Moffat from and to all other exit points.

3. Flexibility capacity product

Overview

We believe the flexibility proposals as they stand may have serious adverse impacts on operations at Moffat and for the downstream markets. Again, NTS shippers are not best placed to book flexibility requirements for the Moffat exit point so the intended benefit of improved efficiency in NTS operation is unlikely to be realised. This concern is compounded by the additional problems presented by the proposed flexibility capacity product. There is hence an even more pressing need for a single party aggregator for NTS flexibility capacity at Moffat to mitigate the adverse impacts and to facilitate the planning and operational processes necessary for the efficient onward transmission of gas downstream of Moffat. However, the proposed rules do not properly accommodate this role and we discuss the significant and complex amendments that would be required later.

We are not persuaded that within-day NTS exit flow rate variations need to be addressed. The tried and tested Network Code arrangements currently in place have now operated satisfactorily for a period of more than ten years and we see no reason to change them. We accept that Distribution Networks (DN) may require services similar to those currently provided under the UNC and we address this point in a later section.

We believe the distinction between flat and flexibility capacity is artificial and our view is reinforced by the following:

- Flat baselines and prices appear to be unaffected by the introduction of the flexibility product, whilst flexibility capacity will be auctioned at zero reserve price – we would expect baselines and prices to be “shared” between the two products if product distinction reflected economic principles
- Flat capacity is proposed as a nodal product whereas flexibility capacity is offered as a zonal product – we would expect that (in the absence of persuasive explanation to the contrary) capacity products generated from the same assets would have the same spatial parameters

We are not aware of any network utility that has attempted to disaggregate capacity in this way. We also note that the entry capacity proposals, debated extensively during the TPCR process, still comprise a single capacity product rather than a dual product approach, despite the fact that any concerns about within day rate of flow variations might apply just as much at entry as at exit.

Even if there were a clear rationale for distinguishing between flat and flexibility capacity the practical implications of implementing arrangements based on within-day flows requires very careful consideration. In our view the enormous complexity of this exercise, particularly at multi-shipper exit points such as Moffat, will carry considerable cost with no material prospect of offsetting benefit.

Furthermore, we believe the manner in which the flexibility product rules have been constructed imposes unwarranted uncertainty and exposure on NTS shippers:

- There is no concept of assigning prevailing rights to shippers based on historical usage (in contrast with the flat capacity product) and it will be very difficult for users to forecast future requirements because of the lack of historical data.
- The availability of the product is limited, being subject to a series of national, area and zonal caps, and there is no provision for increasing availability in response to shipper signals

- Shippers will be expected to compete via price auctions to fulfill their uncertain requirements at an uncertain price and with no knowledge of the historical demand for such a product in the market.
- Where they fail to acquire the product shippers are exposed to uncertain levels of overrun charge that may be triggered by product usage at a different node to which they are operating.

In summary, NTS shippers and the Moffat single party would be exposed to significant uncertainties relating to requirements, availability, prices and overrun charges for the flexibility product. Furthermore, there is no means of mitigating these exposures by ensuring product availability through forward investment signals. We note in passing that this inability to request incremental flexibility capacity undermines the original stated objective – to improve investment signals.

Two further flexibility product design flaws are highlighted in the recent draft modification proposal "Change of Definition of Flow Flexibility Capacity" put forward by National Grid itself, through its Gas Distribution arm. The proposal cites concerns that the current flexibility product rules under modification 116.

BGN regard the proposed means of addressing these issues as unworkable. Firstly the "correction" to flexibility usage is based on demand forecasts notified to National Grid NTS by the user. There is clearly scope here for notifications to be made to minimise flexibility product usage rather than being a true reflection of forecast demand. Secondly, the proposed amendment would layer further complexity onto what is, in our view, an already complex set of rules.

Nevertheless the concerns highlighted in this modification are very real, and reinforce our view that implementation of the flexibility product would likely have serious adverse impact on operations at Moffat and for the downstream markets.

We are therefore very concerned at the implications of the flexibility product, both in terms of physical operations at Moffat and the potential additional costs imposed on the downstream markets. We believe the current arrangements whereby an equivalent service is made available subject to certain ramp rate and notice period restrictions set out in the Network Exit Agreements and in the case of Moffat, the Connected Systems Agreement, adequately deal with the issue of flexibility usage.

Amendments to proposed flexibility capacity and overrun rules

Reconciling the role of an SP aggregator with the proposed rules relating to the flexibility product is a much more difficult exercise because of the zonal nature of the product and the varying drivers for flexibility usage (shipper nomination changes and downstream pipeline operational requirements). Not only must independent flexibility capacity bookings at Moffat be taken into account, but the impact of overruns being triggered at nodes other than Moffat must be addressed.

Flexibility capacity charge proposals

Our concerns over the proposed auction arrangements for flexibility capacity, with zero reserve price, are covered in the commentary above.

We also believe it inappropriate to apply an SO commodity charge in respect of flexibility capacity usage. Both National Grid and shippers will need to develop systems to calculate daily charges using hourly rate information. In our view any perceived benefits in improved cost reflectivity are likely to be small (given that the costs associated with this charge are relatively modest) and will be far outweighed by the set-up and ongoing costs of complex commodity charging arrangements.

Information provision

As with flat capacity we are disappointed with the level of supporting information provided by National Grid NTS to assist in consideration of its proposals. In the context of the flexibility capacity product it would be extremely helpful if the following could be made available:

- Details of the methodology used to derive the national, area and zonal caps
- The basis for drawing a distinction between flat and flexibility exit capacity and the basis for stating that NTS investment to provide flexibility capacity would likely be uneconomic
- Historic and forecast flexibility capacity availability and usage at NTS exit points and within Flexibility Zones (in particular with reference to Zone 1, which Moffat is a member of)
- Details of transfer/ substitution methodology to be used to derive exchange rates for flexibility capacity between zones

4. Summary of BGN position

BGN is concerned that the proposed NTS exit reforms will have adverse impacts on arrangements downstream of the Moffat exit point, in terms of security of supply and market foreclosure. Whilst it may be possible to mitigate some of the adverse impacts through the introduction of an SP capacity aggregator (with appropriate rule changes), we remain of the view that the existing arrangements better facilitate the UNC relevant objectives and more closely meet the requirements of the Moffat exit point.

We are particularly concerned at the implications of the flexibility product, both in terms of physical operations at Moffat and the potential additional costs imposed on the downstream markets, arising through the construction of rules which afford no certainty on the availability, price or exposure associated with the product. In addition to the market uncertainties, there are the significant costs of implementing and maintaining a regime whereby charges will be dependent on within-day monitoring of usage of what we would argue is essentially an artificial product.

We do not share the view that the user commitment approach to flat capacity will result in improved investment signals at Moffat because individual NTS shippers are not best placed to signal collective long term requirements. We have particular concerns over the nature of the proposed rules, particularly in relation to initial prevailing rights (which we believe should be conferred on the SP at Moffat), and in relation to the overrun rules which would require significant amendment to appropriately accommodate the SP concept.

Our other main concern relates to the dearth of information regarding historic and projected usage and prices for both flat and flexibility capacity, and indicative exchange rates for transfer and substitution. These are critical to facilitate proper appraisal of the proposals and we request that National Grid now addresses this as a matter of urgency.

Based on the arguments set out above the BGN position and relative preference for the five modification proposals in play is shown in the table below:

Proposal	BGN position	Preference
0116V National Grid NTS	<ul style="list-style-type: none"> ▪ Not supportive ▪ Does not better facilitate code relevant objectives 	
0116A E.On	<ul style="list-style-type: none"> ▪ Supportive ▪ Better facilitates code relevant objectives 	1 (of 5)
0116BV RWE	<ul style="list-style-type: none"> ▪ Not supportive ▪ Does not better facilitate code relevant objectives 	
0116CV British Gas Trading	<ul style="list-style-type: none"> ▪ Not supportive ▪ Does not better facilitate code relevant objectives 	2 (of 5)
0116VD Scotia Gas Networks	<ul style="list-style-type: none"> ▪ Not supportive. ▪ Does not better facilitate code relevant objectives 	

We would note however, that certain amendments to the proposals are required in the event that any one of Modification Proposals 0116CV, 0116BV, 0116V or 0116VD is implemented, in order to facilitate the planning and operational processes necessary for the efficient onward transmission of gas downstream of Moffat. These are discussed in more detail in the earlier sections of this document.