Decision on Tariff Arrangements for Short Term Daily Capacity and Virtual Reverse Flow products in Northern Ireland

29 June 2012

Contents

1. Purpose of this paper

1.1. This paper sets out the Utility Regulator's decision on the tariff arrangements for the short term daily capacity and virtual reverse flow (VRF) products in Northern Ireland.

1.2. These products have been developed in order to satisfy infringement proceedings against the UK under Regulation (EC) 715/2009 which replaced Regulation (EC) 1775/2005.

2. Background

2.1. The European Commission referred the UK and Ireland to the European Court of Justice on 26 January 2012 for a failure to fulfil certain obligations under Regulation (EC) 715/2009, which replaced Regulation (EC) 1775/2005 on 3 March 2011. Earlier in June 2010 the Commission issued a reasoned opinion to the UK for non-implementation of certain aspects of Regulation (EC) 1775/2005. These requirements were to be fulfilled as part of the CAG project by 1 October 2012.

2.2. The two Departments have jointly requested that the Utility Regulator and the Commission for Energy Regulation (CER) in Ireland urgently focus their resources, and the resources of the system operators, on ensuring immediate compliance with the Gas Regulation in the EU Second Package in their respective jurisdictions.

2.3. The short term daily capacity and VRF products have been developed in order to satisfy infringement proceedings against the UK under Regulation (EC) 715/2009 which replaced Regulation (EC) 1775/2005. The infringement alleged that the Transmission System Operators (TSOs) in NI do not make maximum capacity available on the Scotland to Northern Ireland (SNIP) pipeline or on the South-North pipelines (SNP) because they do not offer interruptible reverse flow.

2.4. The business rules for the short term daily capacity product were confirmed by the Utility Regulator on 6 April 2012. The business rules for the virtual reverse flow product and the south north entry point were confirmed by the Utility Regulator on the 10 May 2012.

2.5. The TSOs subsequently consulted on the code drafting to implement the business rules. The code modifications to be made were confirmed by the Utility Regulator on 29 June and will become effective from 1 July 2012.

2.6. The Utility Regulator published Gas Notices for BGE(UK), PTL, and BGTL and the consultation on these closed on 18^{th} June. The TSOs have subsequently given their consent to the modification of their licences and the modifications have been published on the Utility Regulator website.

3. Summary of issues consulted on

How to treat revenue from new products

3.1. A key question consulted on was whether payments for short term and VRF products should be fully postalised, i.e. paid into the PoT and therefore subject to all the postalisation requirements.

3.2. We were minded not to require revenues from VRF and short term capacity products to be paid into the PoT as to do so would trigger substantial changes to the TSO licences which would be difficult to formulate and agree in the time involved. The Utility Regulator being mindful of the need to meet the infringement as quickly as possible.

3.3. We proposed that any revenues forecast to be received by the TSOs from short term and VRF services should be paid directly to the TSOs. At the end of the gas year if revenue is received for the new products, then the cash amount received will be deducted from their actual required revenues before reconciliation take place.

3.4. We also proposed that the forecast revenues should be zero due to uncertainty about how the new services will be used and because their use may be difficult to forecast, particularly in the short term. However, shippers would be required to give the TSOs forecasts for their use of VRF and short term capacity and these would be used to determine the amount of credit cover required.

3.5. The postalised conditions of the TSO licences also contain provisions in the event of non-payment of postalised charges and which allow bad debt to be recovered, ultimately from all gas suppliers. We proposed that VRF and short term will not be subject to these provisions.

3.6. We also proposed to incorporate into the licence a trigger point (‘a threshold amount’) at which we would aim to fully postalise revenues from short term capacity and VRF.

Licence changes necessary to implement new tariffs

3.7. Alongside the tariff consultation the Utility Regulator consulted on changes to Part 2A of the TSO licences to differentiate the treatment of VRF and short term capacity within the postalisation conditions.

3.8. Briefly the licence modifications proposed would:

- Introduce any new definitions necessary into the licence
- Allow the TSOs to charge for VRF and short term capacity
- Introduce zero forecasting for short term and VRF revenues and allow the authority to subsequently give notice that the forecast should be other than zero.
- Require the TSOs to submit a charging methodology statement to the Utility Regulator for approval each year and to published any statement so approved
- Define the ‘Threshold Amount’ and the steps to be taken when this is reached.

- Any consequential changes required to other conditions of Part 2A.

3.9. The same changes are proposed to all the TSO licences as Part 2A of the licence is identical for BGE(UK), PTL, and BGTL.

3.10. Changes were also proposed to the revenue formulae of the TSO licences in order to specify how the actual required revenues will be calculated as a result of the introduction of these products. Specific changes are proposed to the revenue formulae of each TSO but these are intended to have equivalent effect.

Short term capacity tariffs

3.1. We proposed that the short term capacity tariff will be calculated using the multipliers consulted on for short term capacity products as part of the CAG project (set out below). The multipliers would be applied to that year's forecast postalised capacity charge.

3.2. Also, that the arrangements for short term capacity will be streamlined such that Shippers utilising short term capacity will pay once for that capacity - to the TSO at the final Exit Point at which the Shipper offtakes gas.

Table 1: Short Term Capacity Multipliers

Short Term Multipliers	M
October	0.66%
November	0.66%
December	1.18%
January	2.06%
February	2.35%
March	1.76%
April	0.66%
May	0.40%
June	0.40%
July	0.40%
August	0.40%

Virtual reverse flow tariffs

3.3. In order to simplify charging for VRF we proposed that the VRF product should initially have an annual charge of £5000 per exit point registration and/or per each extension of an existing exit point registration for VRF. This would be payable in advance of using the product and there will be no capacity or commodity charges for the VRF product.

Calculation and publication of charges

3.4. Because the charges will not be paid into the PoT the Postalised System administrator (PSA) will not calculate the short term or VRF charges. Instead we proposed that the VRF and short term capacity charges are set out in a charging methodology statement. This statement will be approved by the Utility Regulator and should be consistent with the Regulator's decision on tariffs.

4. Summary of responses received

4.1. We received four responses to the consultation from:

- AES Ballylumford
- BGE(UK) Ltd.
- Phoenix Natural Gas Ltd.
- Energia

4.2. AES indicated that at this time they are content with the preferred options and tariff proposals consulted on and specifically with the proposal that the revenues from VRF and short term products will not be paid into the PoT.

4.3. BGE(UK) highlighted the drafting in section 3.4 which states that the UR wishes to ensure that anyone utilizing the new short term and VRF products also pays a postalised charge on exit. BGE(UK) pointed out that anyone using the VRF service would pay the VRF registration fee.

4.4. BGE(NI) also stated that the NI multipliers should be designed to reflect the probability of incremental demand for capacity in a particular month and as a consequence, the short term multipliers consulted on for CAG although designed to achieve this may not be suitable in NI due to different tariff arrangements.

4.5. BGE(NI) also preferred a capacity and commodity charge for the VRF service being concerned that the approach could create cross-subsidies between forward-flow and reverse flow shippers and that the tariff proposed does not incentivise shippers to optimise their booking behaviour in order to sue the network efficiently.

4.6. Phoenix Natural Gas Ltd. restated their support for the Utility Regulator's attempt to address the issues in the infringement and their encouragement to continue to develop the products in future. Phoenix supported the proposal that VRF and short term will not be subject to the postalised conditions of the TSO licences in the event of non-payment of postalised charges and which allow bad debt to be recovered, ultimately from all gas suppliers.

4.7. Phoenix asked whether the proposal to forecast revenues for short term and VRF products at zero would ultimately lead to inaccuracies in the published commodity tariff. Phoenix also asked whether the short term multipliers consulted on might ultimately impact on longer term capacity bookings and so increase the overall postalised tariffs.

4.8. Energia stated its support for the necessary policy and product developments introduced by the UR in the context of the infringement and its commitment to the development of an all-island gas market. With respect to the short term multipliers Energia noted that new multipliers were recently proposed by the CER which could create an inconsistency between NI and Ireland but that this could be addressed in future work. In relation to VRF, Energia objected to an administration fee and stated that the product should have an associated capacity and commodity charge.

4.9. Energia also questioned the utility of the products offered and asked that they should be reviewed in the context of IME3 and the European network codes under development.

5. UR response and decision

5.1. In response to the points raised on the short-term multipliers raised by BGE(UK); we recognise that there are different tariff arrangements in Ireland and in Northern Ireland but in our view the multipliers proposed will provide a reasonable starting point given the short timescale to develop tariffs. They are also familiar to shippers having been proposed for CAG.

5.2. Energia noted that new short term multipliers were recently proposed by the CER and that these could create an inconsistency between Ireland and Northern Ireland. These were not available to us at the time the consultation was issued and we have been unable to take these into account given the short timescales to meet the infringement. In any case Energia appear content for this to be addressed as part of future work post 1 July.

5.3. In relation to the point raised by Phoenix, we have considered whether the short term tariffs will impact on long term bookings and ultimately increase the overall postalised tariff. We do not believe that this will be the case but we will keep the tariff arrangements under review and in any case they will need to be reviewed in the context of work that remains to be done to implement wider aspects of the third package e.g. to change the existing point to point codes to entry exit codes and to comply with EU network codes as they are developed.

5.4. In relation to the concerns raised by BGE(UK) and Energia on the VRF tariff proposals. This proposal was made to simplify charging so as to introduce the product as soon as possible and we intend to keep charging for VRF under review in the context of work that remains to be done to implement wider aspects of the third package.

5.5. In relation to the drafting in 3.4 BGE(UK) are correct that the proposal is that anyone using the VRF service would pay a registration fee, this point is made clearly elsewhere in the document but we recognise that the drafting in 3.4 could have been clearer.

5.6. Phoenix Natural Gas asked whether forecasting revenues for short term and VRF products at zero would ultimately lead to inaccuracies in the published commodity tariff. The published forecast commodity tariff and the end of year tariff may differ at present, as the forecast tariff is based on forecast volumes while the end of year tariff is based on actual volumes. If there is any divergence between forecast and actual commodity tariffs related to the introduction of the short term product, we expect it to be very small. But, as before, we will keep the arrangements under review.

5.7. Our decision is therefore to confirm the tariff arrangements and the tariffs themselves as consulted on. We will also continue to improve the products and will take on board the comments made by respondents as the products develop. But, in light of the infringement, it is important to publish the tariff arrangements as soon as possible.

6. Next steps

6.1. The Utility Regulator has separately confirmed the modifications to be made to the TSO licences and these will take effect on 1 July. We have also confirmed the changes to the codes of operation necessary to give effect to the new products and arrangements to meet the infringement. These will take effect from 1 July.

6.2. The TSOs should now submit a charging methodology statement to the Utility Regulator for approval so that the new tariffs for short term and VRF products are in place for 1 July.