Common Arrangements for Gas (CAG)

Gaslink response to Discussion paper on the options for the Gas Operational Regime

2nd July 2008

Introduction

Gaslink welcomes the opportunity to respond to the above discussion paper concerning the most appropriate gas operational regime for the Common Arrangements for Gas (CAG) project. For ease of reference this response follows the format of the discussion paper.

General Comments

Gaslink is the newly created independent system operator for the Republic of Ireland (RoI). The organisation, pursuant to Irish legislation, is due to have responsibility for the operation, maintenance and development of both the BGE transmission and distribution systems in RoI. As such, Gaslink will also have responsibility for the development and publication of the Code of Operations. (CoP)

Gaslink is highly supportive of the Common Arrangements for Gas initiative and looks forward to working with the regulators and all other industry participants to ensure the success of the project.

Accordingly, Gaslink supports efforts that aim to improve the efficiency and cost-effectiveness of gas operations in a combined all-island gas market. Gaslink considers that there are real potential benefits in developing a more integrated approach to the operation of the gas market and the associated operation of the transportation system on all-island basis. This is particularly true in terms of the following areas:

- a common shipper interface;
- the day to day scheduling of system gas flows;
- system balancing;
- system planning; and
- security of supply.
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The touch point between the Operator and shippers is a key interface in every gas market. Gaslink is particularly keen that existing interfaces are improved and simplified as part of CAG to ensure efficiency for existing shippers and new entrants.

We also consider that an appropriate balance between efficiencies and costs should be considered as a vital element of the CAG project. We feel therefore that the approach adopted toward the operational regime and other aspects of the CAG project should be pragmatic and sensitive to the balance of costs and benefits.

CAG Vision and Goals

We wholeheartedly agree with the statement expressed in the discussion paper that the safety, reliability and integrity of the gas systems will be central to any operational arrangements that are put in place. It is our view that the safety, reliability and integrity of the transportation systems should not be compromised under any circumstances and

that these should be overriding considerations when evaluating the options put forward in the discussion paper.

Apart from these fundamental pre-requisites, the discussion paper puts forward a set of criteria against which options will be evaluated and acknowledges that there may be certain trade-offs between these criteria under some of the options.

We consider that some additional evaluation criteria should be considered alongside those contained within the discussion paper.

We believe the new operational arrangements should be robust and should be evaluated against the level of certainty and stability that they offer. Particular issues that should be addressed would include:

- Certainty/stability of the industry structure ; and
- Certainty/stability and clarity and ease of operation of market arrangements.

Both of these issues will be of importance to new entrants and financing houses that may otherwise be wary of the level of regulatory risk and potential changes to the regime.

We fully support the goal relating to the establishment of 'customer friendly' arrangements. Current arrangements have been developed in an environment of multiple TSO/TO's, network codes and interfaces. In this regard, improvements and simplification of market facing arrangements can be readily achieved and accordingly must rank as a key deliverable of the project.

Gaslink recognises the rights and obligations that the asset owners have under law and licence and we acknowledge that these rights will need to be recognised and respected in the new regime. The asset owners should be satisfied that the operation, maintenance and development of their transmission assets is being carried out to ensure compliance with their legal obligations. This is particularly important with regard to any obligations that the asset owners may have concerning safety issues.

All-island system operation functions

The discussion paper offers a list of system operator functions which could be undertaken on an all-island basis. We consider that it is perhaps premature to prescribe a full set of functions at this stage before the structure of system operation has been determined. The ease with which a system operator could perform these functions will depend on the number and type of TSO's, the interactions between them and also the interactions with the TOs. However, Gaslink considers that the following system operation functions should be carried out on an all-island basis in order to achieve benefits of efficiency:

- Day to day operation of the transportation system;

- Balancing the system;
- Procurement of fuel;
- Planning and development;
- Measurement and end of day settlement and allocations[1];
- Long term management of the market transportation arrangements including product offerings;
- Capacity trading;
- Connections to the transmission system; and
- Congestion management.

We also consider that provision and development of IT systems that interface with shippers should be provided on an all-island basis.

The handling of any emergencies in an all-island gas market and the development of robust procedures is desirable. However, we are conscious that the current legislation in NI and RoI may complicate the handling of emergencies by a single party. At the very least, given the integrated system operation envisaged under CAG, management of any emergencies due to gas supply shortfalls should be carried out in a co-ordinated manner.

We consider that a single billing mechanism will deliver a real benefit to shippers. We also consider that a single financial security instrument will also deliver ease of operation for shippers. However there are issues that will need to be addressed in order to achieve this including VAT and currency issues. In addition to a single billing mechanism, procedures will be required for collecting transportation charges from shippers and subsequently distributing monies to the TSO/TOs.

Maintenance of the transportation system will not necessarily need to be carried out on an all-island basis, although scheduling of maintenance could be considered in order to minimise potential disruptions to transportation

Options for single system operation

Co-ordination between multiple TSO/TOs

We agree with the argument contained within the discussion paper that the multiple TSO/TO option would require complex contractual and operational agreements in order to deliver the envisaged benefits. This complexity is not just limited to the provision of IT systems but also to the co-ordination on a day-to-day basis between the TSO/TOs. One option not discussed in the paper relates to the creation of a joint venture company by the TSO/TOs which would be responsible for system operation. This option should be considered further to determine whether it could fulfil the

[1] We understand the term 'Measurement' to refer to the information that is collected via meter reads in order to determine gas flows and allocations.

relevant CAG requirements. Potentially, the TSO/TOs could be required to establish the JV via a licence condition.

In addition, the definition of capacity is different in NI and RoI, being point-to-point and entry/exit respectively. Unless the capacity offering is harmonised an additional level of complexity will be introduced for shippers. Whilst this issue is true for the other options also, we consider that harmonisation will be more difficult where there are multiple TSO/TOs. This issue is of fundamental importance as it determines the basis on which shippers contract for and trade capacity, trade gas, enter nominations, receive allocations and balance their inputs to and offtakes from the system.

Multiple TSO/TOs with a single service provider

We consider that this option has more merit than the multiple TSO/TO approach although it will still involve complex legal and operational arrangements. In fact this approach is more analogous to the current arrangements where BGE are contracted by Gaslink, PTL and BGE (NI) to operate the transmission systems. However, the current arrangements are not sufficiently robust in that some of the contracts are awarded via a tender process and there is no guarantee that the current arrangements will persist into the future to provide the required level of certainty for TSO/TOs and other market participants. In addition there is no guarantee that the terms of engagement between the SSP and TSOs will be consistent so that maximum efficiencies across the network as a whole can be achieved. In fact current arrangements do not permit day to day scheduling of system gas flows on an all-island basis as separate codes are in place.

The appointment of a SSP raises a number of significant issues which must be considered in full. In particular the appointment process and conditions of engagement are crucial to this approach. In order to achieve certainty and stability, the SSP should be appointed for a sufficiently long period to ensure continuity for the TSO/TOs and other market participants. We believe that the Regulators should have a direct role in the monitoring and regulation of the SSP if the SSP is to undertake an extensive role. This may require the SSP itself to be a licenced entity as a party who participates to a very substantial extent in the operation of the network. Becoming a licenced entity will also reduce some of the concern over volatility in industry structure as the SSP could be designated for a period consistent with its licence.

Again, under this approach the same issues remain concerning the harmonisation of transportation regimes and the provision of IT systems.

Single TSO

We agree with the view expressed in the paper that the single TSO is most likely to deliver a more efficient and optimal outcome than the other options. However, as the paper outlines there are significant issues to be considered including set up costs, legal consideration and further operational arrangements. Prior to any decision to proceed with a single TSO, therefore, we should undertake analysis of these issues. We must also consider and recognise the obligations that all asset owners have under their respective licences.

We do not agree that a regular competition via a tender process is the optimal method in which to appoint the single TSO. This may lead to a lack of stability in the industry and additional set-up, legal and IT costs. Rather, we believe that the TSO should be a licenced entity that is regulated by the regulators in order to deliver efficient services to the market.

We recognise also that each National Regulatory Authority (NRA) is obliged by legislation in its own jurisdiction to ensure that licenced entities deliver the most appropriate result for consumers. While progress is underway in Europe to place increased responsibilities on NRAs relating to issues outside of its own jurisdiction, Gaslink recognises that the NRA must retain a strong role in approving and directing arrangements which impact on consumers within its jurisdiction. Accordingly, the single TSO solution will require careful and perhaps relatively complex development and implementation in order to ensure sufficient control by all NRAs. This may include separate licences for the single TSO in each jurisdiction. In this case extensive co-operation and co-ordination will be required between the regulators. However structures have already been developed for the Single Electricity Market which could be of assistance.

Complexity in arrangements and contracts should clearly be avoided wherever possible. However, Gaslink believes that where it is decided, for overall benefit, that these cannot be avoided then such complexities should be focussed at the TSO/TOs and regulators rather at shippers and consumers.

Dual TSOs

We consider that the dual TSO approach is perhaps, on initial consideration, a pragmatic option, although it, like the other options, presents a set of issues that need to be tackled and overcome. Not least of these would be the appointment of a single TSO for NI and the accompanying licencing arrangements. We believe that he dual TSO approach would require significant effort and costs that could be better utilised toward the achievement of the single TSO.

Whilst the SEM provides a precedent for a similar approach and could provide a model for TSO interactions via a System Operator Agreement we do not consider that this approach will deliver the greatest benefits for the operation of the market. The co-operation between the TSOs will be critical to the success of this approach and will require suitable licence obligations to ensure that interactions are effective and efficient. This will significantly add to the complexity of the arrangements.

Gaslink conclusion on the options

The options presented in the paper could all be designed in order to achieve most of the relevant objectives, albeit to different degrees. There are trade-offs in each of the options , one of which relates to the level of effort and set up costs against ongoing and longer term operational savings.

We in no way underestimate the complexities and issues to be addressed in endeavouring to set up a single TSO model given that multiple TSO/TOs already exist in the market. As we explore the option further it may arise that the level of change required in the short term to adapt from the current structure to the single TSO is not achievable. Gaslink believes in this scenario the multiple TSO model with extensively improved market facing arrangements would then be appropriate.

Network Codes

The discussion paper presents three options for the structure of the Network Code:

- Multiple Network Codes;
- Dual Network Codes; and
- A Single Network Code.

We consider it important that prior to the decision on the structure of the Code that discussion takes place on the form of the transportation product definition that will be in place for the all-island market. Currently the CoP is based around an entry/exit regime which lays the foundations for capacity sales and trading, gas flow nominations, allocations and balancing. The various codes in the North are based on point-to-point principles which, whilst having consistency between codes, have different procedures from the CoP for each of the activities detailed above. It is vital that the transportation regimes operate on the same basis in order to maximise benefits to shippers and to enhance any efficiencies that might arise from the CAG project. We note that the view of the EU Commission is that adoption of an entry/exit regime would be the most suitable way to create a level playing field and to enable competition to develop.[2] We would therefore suggest that early clarification be obtained on the approach to this topic.

[2] Paragraph (12) of Draft Explanatory note of the DG Energy and Transport on Article 3 "Tariffs for access to the networks" of regulation (EC) No 1775/2005 of the European Parliament and of the Council of 28 September 2005 on conditions for access to the natural gas transmission networks.

We agree with the view expressed in the discussion paper that a single Code will provide the optimal solution, along with a single system operator. We also consider that a single Code would be suitable in an environment with dual or even multiple TSOs. As the discussion paper points out there is a precedent for a single Code with multiple operators as seen in the GB market, although this is based on one TSO and a number of DSOs. There is also a blueprint for the governance arrangements involving both regulators as evidenced by the SEM.

For these reasons we consider that the single Code should offer the best way forward.

However, we also consider it appropriate that in a possible environment with multiple or dual TSOs that one of the TSOs could be required by licence to develop and maintain the single Code. The other TSO(s) could then be required to operate in accordance with the single Code.

Scope of system operation and codes(s)

This section of the discussion paper considers whether system operation on an all-island basis should include both transmission and distribution and similarly whether the code should also cover both transmission and distribution. The harmonisation of retail arrangements is also considered here.

With regard to the harmonisation of the retail arrangements we agree with the suggestion that these can be considered on a longer timescale than has been initially envisaged. Whilst the benefits of common retail arrangements should not be underestimated we consider that it is important for the transmission issues to be fully developed as a priority.

As we have stated, we do not consider distribution and retail arrangements to be the most pressing priority. However, we are conscious that in developing CAG at the transmission level that we should not ignore distribution system issues and consider that foundations can be laid that will permit further detailed development of harmonised retail arrangements. We believe that the transmission arrangements can be made sufficiently flexible so that Distribution System Operators (DSOs) will be able to interface their codes with the single transmission code. In RoI this has already been achieved through the CoP and we consider that it will be important that the new regime does not prohibit the unified aspects of the CoP. We also recommend that the new arrangements would not prohibit the continuation of a separate distribution code. if a particular DSO considered this to be appropriate

Whilst not precluding a combined TSO/DSO, we are not convinced that operation of all distribution systems is necessarily a function of a single operator. The single TSO could interface with a number of DSOs as long as the arrangements for offtake by the

DSOs from the transmission system are consistent and do not present barriers to competition of supply.

Gaslink does not see a requirement for a 'xoserve' type function in the all-island gas market in the short term. Such functions could be facilitated within the new TSO model and the DSOs. The issue should be revisited when retail arrangements are to be further reviewed.

Conclusions

The views of Gaslink can be summarised as follows:

- Gaslink is highly supportive of the Common Arrangements for Gas initiative and looks forward to working with the regulators together with all other industry participants to ensure the success of the project.

- We believe that the new operational regime should result in ease of operation for shippers in the Irish gas market and deliver improved service to consumers. In this regard improvements and simplification of market facing arrangements must rank as the key deliverable of the operational regime.

- Safety, reliability and integrity of the gas systems must continue to be central to any operational arrangements that are to be put in place.

- Operation of the entire network on a wholly integrated basis should be undertaken resulting in improved efficiency and cost effectiveness to the benefit of shippers and consumers.

- Additional criteria against which to evaluate options might include certainty and stability of the operational regime and associated industry structure which will contribute to effective market operation and encourage new entrants.

- We believe that a single Code and a single shipper interface will give rise to increased efficiencies for existing shipper/suppliers and increase the potential for new entrants to the market.

- Gaslink recognises the obligations that all asset owners have under law and licence. We acknowledge that these rights will need to be accommodated and respected in any new operational regime particularly with regard to safety and integrity of the networks.

- The role of a single service provider is a means of achieving the single interface for shippers together with day to day integrated operation of the entire network.

- Recognising that multiple TSO/TO's already exist in the market there will be significant costs and legal considerations in moving to a single TSO. Subject to these issues being resolved, we believe that in the longer term the single TSO, potentially with separate licences in each jurisdiction, will deliver the greatest benefits and most integrated set of market arrangements.

- Complexity in arrangements and contracts should clearly be avoided wherever possible, however where it is decided for overall benefit that this cannot be achieved then such complexities should be focused on TSO/TO's and regulators rather than at the shipper and consumer level.

- The development of the operational regime for transmission should lay the foundation for further harmonisation of retail market arrangements. We support the view that retail arrangements in themselves should be addressed in phase 2 of the project.

- We recommend that the single Code if such arises should not prohibit the existence of distribution code requirements being fulfilled on a unified or separate code basis.

Finally, we acknowledge the extensive initiatives already underway in Europe regarding increased co-operation between TSO's and regulators on a cross jurisdictional basis. We believe that structures, policies and arrangements may emanate from this constituency which could be of major assistance to the CAG project.