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Introducing entry charges into the NI postalised regime

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Sections of this presentation

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Common tariff requirement

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- *Article 59 of the Energy Order:*
  - *.. the prices charged in connection with the conveyance of gas through designated pipe-lines (within the meaning of Article 59) are in accordance with a common tariff which does not distinguish (whether directly or indirectly) between different parts of Northern Ireland or the extent of use of any pipe-line*
- Postalisation means that the charge for transporting gas along designated pipelines will be the same irrespective of where the gas is offtaken for final use.

Summary of current postalised regime

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- Common tariffs for designated pipelines as required by legislation
- Exit point payment mechanism – shipper relationship is with the TSO at the exit point
- Shipper payments go into a bank account held in trust (PoT) and there is a PSA to administer the process
- Revenue transfers between the TSOs to and from the PoT
- TSOs are not exposed to capacity or volume risk as shippers pay based on their actual volumes/capacity at the end of the year
- Under or over recovery is dealt with by end of year reconciliation – shared by all gas users
- Bad debt ultimately recovered from all gas suppliers – credit committee to manage this
- PTL and BGTL actual costs are recovered via the end of year reconciliation thus facilitating the underwriting of MEL pipelines by all gas users
- Detailed legal and financial structure underpins the postalised system

Summary of EU requirements to be implemented in October 2015

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- The inclusion of entry capacity in the NI tariff regime
- Entry capacity to be offered as yearly, quarterly, monthly, daily and within day capacity. Therefore the new tariff methodology needs to generate tariffs for these products
- Entry capacity to be auctioned. Therefore the tariff methodology needs to consider how auction reserve prices will be set and take account of the clearing price from the auctions, deal with over/under recovery of revenues etc.
- The EU network code on tariffs does not need to be implemented until 2017. But, in devising proposals for the new entry tariff methodology for 2015, we propose to take account of the draft tariff code where it seems sensible to do so.

Considerations in the design of the new tariff regime

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- Implement European legislative requirements
  - Article 13 of Gas Regulation
  - Entry charges for the new CAM capacity products
  - The requirement for auctions at entry
- Implementation by October 2015
- Consistent with the common tariff requirement
- Maintain the underwriting of MEL pipelines

Overview of entry charging proposals

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- Cost allocation method between the points on the network
- Capacity commodity split at entry and exit
- Split of revenues between entry and exit
- Reference price calculation
- Multipliers/seasonal factors for non-annual products
- Commodity charge
- Revenue collection arrangements
- Reconciliation process

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Cost allocation method

- We have considered all 4 cost allocation methodologies in the draft tariff code against the common tariff requirement
- Propose to apply the postage stamp methodology
- All other result in locational signals that are not consistent with the common tariff requirement
- Postage stamp results in one uniform tariff at entry and one uniform tariff at exit
- Key inputs are revenue and capacity
- The tariff at entry can be the same or different from the exit points
- Our proposal would result in the same tariff at entry and exit points for annual capacity

Capacity-commodity split at entry and exit

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- Existing capacity-commodity split is 75:25
- No requirement to change this in 2015
- There will be rules on the capacity-commodity split in the network code on tariffs
- The draft indicates that commodity charges may be applied for the purpose of recovering variable costs driven by the volume of gas flow
- Propose to maintain the existing capacity-commodity split at entry and exit for 2015
- When the tariff code is finalised we will assess whether this is compatible with the code and consult on any changes necessary for 2015

Split of revenues between entry and exit

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- The entry – exit split can be decided ex ante <u>or</u> it can be an output from reconciliation
- Concerns are under forecasting and large bullet payments as a consequence
- Therefore may not be appropriate to limit the amount of revenue recovered at entry or exit
- We propose that the entry-exit split is an output from reconciliation
  - Total postalised system required revenues are recovered from all gas users
  - PTL/BGTL actual required revenues are underwritten by all gas users
  - Annual capacity prices are the same at the entry and exit points

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Reference price calculation

- Reference price = price for annual firm capacity at the entry and exit points derived from the cost allocation methodology
- Assuming the postage stamp with the capacity and commodity split above and no ex ante entry-exit split - determining the reference price is straightforward
  - Input the data into largely existing formulae with the forecast capacity/volume information
- Timing of the calculation? Propose to apply the current timings in place for postalisation and review when tariff code is finalised
- Tariff setting process next summer will result in reference price for annual capacity (1st CAM auction for annual capacity in March 2016) and reserve prices for non-annual products (auctions for these commence in November 2015)

Multiplier/seasonal factors for non-annual products

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- A multiplier is a factor applied to the reference price in order to calculate reserve prices for non-annual products
- Seasonal factor may be applied in addition to the multiplier
  - Both mitigate the risk of under recovery
  - Sharpen prices for short term capacity at times when demand is greater (e.g. higher multipliers in winter)
- Risk is of under recovery where multipliers/seasonal factors are non-existant or low and there is under forecasting by suppliers
- Under recovery would impact on TSO cash flows and result in large bullet payments for suppliers

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Multipliers/seasonal factors

- Minded to make full use of flexibility to apply seasonal factors and multipliers
- Therefore the price of capacity is highly likely to be higher in winter than in summer.
- We believe this will also help to:
  - incentivize suppliers to make more use of the network in summer;
  - shift demand away from the winter peak, thereby requiring a smaller network than would otherwise be the case; and
  - ensure that tariffs reflect the costs of providing capacity to meet peak demand as this is the basis on which the network has been built.

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Commodity charge

- Our proposal is that the commodity charge would recover 25% of the overall required revenues
  - Could continue to be billed at exit points largely as now
  - Depends on no ex ante entry exit split
- However if we apply an ex ante entry exit split then the commodity charge will differ between entry and exit and will need to be billed separately at entry and at exit.

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Revenue collection

- Not proposing any change to how revenues collected at exit
- Entry the approach based on exisiting process where possible
- Assumed that each TSO will bill for their respective entry point
- Propose to use a single PoT for entry and exit revenues

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Reconciliation

- Two broad options:
  - Reconcile entry and exit separately, i.e. Under recovery at entry recovered only at entry
  - Reconcile them together, i.e. Any risks shared by all users
- Concerns similar to those with the entry-exit split (forecasting error resulting in large bullet payments as revenue must be recovered)
- In NI context only one entry point is effectively used (Moffat). Reconciling entry separately would effectively result in targeting the under recovery at one point. Question of whether this is complaint with the tariff code as currently drafted
- We propose to reconcile entry and exit together
  - Basis of the current postalised system
  - Under recovery at the entry point shared by all gas users

Overview of changes proposed at Exit

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- No requirement to offer CAM products and auctions at the NI exit points.
- Therefore the postalised process at exit can largely remain unchanged in 15/16.
  - this includes the fact that the GDNs will continue to book transmission exit capacity.
- Proposing two changes in relation to the regime at exit for October 2015:
  - To remove the daily capacity product at exit.
  - To change the charging regime at exit to ensure that a supplier nominating above the level of booked capacity at an exit point will be charged an appropriate rate for capacity in addition to the commodity charge.

Overview of proposals related to entry charges

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- Postage stamp
- No ex ante entry-exit revenue split
- Capacity-commodity split as now
  - Same price for annual capacity at the entry and exit points
  - Single commodity charge
- Prices for non-annual products:
  - Flexibility to apply seasonal factors and multipliers
  - Therefore the price of capacity is highly likely to be higher in winter than in summer
- Reconcile entry and exit points together
- Satisfies the common tariff requirement
- Sits comfortably the draft tariff code
- In line with current postalised system here risks shared by all gas users and all gas users underwrite MEL pipelines
- Achievable for October 2015

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Illustrative tariff process

- Calculation of the reference price and the auction reserve prices
- Capacity auctions and the invoice payment cycle
- End of year reconciliation

Calculation of the reference price and the auction reserve prices

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- Collect information
  - TSOs FRR, Forecast Capacity (annual, short term & Interruptible), Forecast Commodity, Capacity-Commodity Split, Determine seasonal factors and short term multipliers
- Calculate reference price
  - Reference Price = Total FRR (allocated to capacity charge)/weighted forecast capacity bookings for all products at entry and exit
  - Weighted capacity because revenues are split by product weighted according to the product's portion of the TSOs' revenues
  - Tariff is applied to entry and exit points (i.e. tariff is same at Entry and exit)
- Calculate reserve price for short term capacity products
  - Reserve price for each short term capacity product determined from the reference price by applying relevant equation (set out in tariff network code)
- Commodity tariff
  - calculated the same as current i.e Total FRR (allocated to commodity charge)/total forecast volumes

Capacity auctions and the invoice payment cycle

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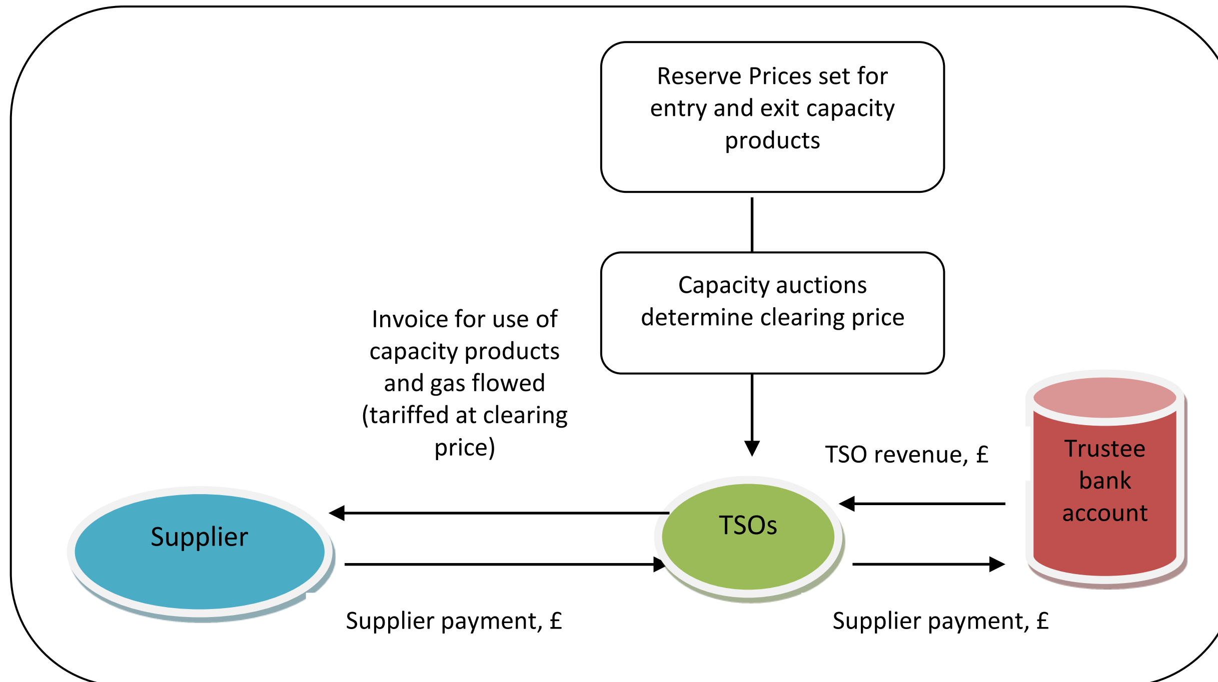

- Auctions held through out year via PRISMA.
- If clearing price of auction > than reserve price shippers invoiced at clearing price
- Suppliers pay TSOs, revenue held in trustee bank account (as now)
- TSOs revenue is split according to their share of the total revenue

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End of year reconciliation

- Finalise data
  - TSOs finalise suppliers' volumes, expenditure (where applicable), actual capacity bookings
- Calculate year end tariffs
  - TSOs calculate year end capacity tariff and year end commodity tariff.
  - Year end capacity tariff determines short term year end tariffs
- Determine reconciliation payments for each shipper
  - Quantity used during year x (difference between forecast and year end tariff) for all capacity products and commodity
  - Propose single reconciliation payment
  - TSOs allocated rebate/payment based upon their portion of total required revenues

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Next steps

- Consultation published today
- Publish illustrative postalisation model next week
- Consultation period ends 27th November
- Tariff conclusions in Dec/Jan
- Development of the licence modifications in Nov-Q1 2015
  - Workshop on licence modifications as needed in January
- March licence conditions in place
- Finalise the postalisation model ready for tariff calculations in the summer of 2015

CAM – capacity bundling at Moffat

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- NI is connected directly to GB facilitated by a TA between BGE(UK) and PTL and a Treaty between the Irish and UK Governments
- Consequently PTL offers a service from Moffat into NI
  - Suppliers to NI therefore do not book capacity with Gaslink from Moffat to Twynholm
  - Twynholm is not a bookable point for suppliers to NI
- Issue of bundling options in Scotland has been extensively discussed between the NRAs and the TSOs
- We wish to preserve the direct connection to GB as we implement EUNCs
- Consequently UR's view is that PTL unsold capacity will be bundled with that of NGG at Moffat and Twynholm is not an IP
- The TSOs are progressing bundling at Moffat and are working well to put arrangements in place
- However, the question of Twynholm's status has not been resolved
- The TA ends in 2021 but there is an option to renew and the TSOs are discussing post 2021 arrangements

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SNP bundling

- CER presented slides containing bundling options to industry in Ireland earlier in the summer and Gaslink has consulted on these
- UR and CER have had detailed discussions on these bundling options subsequently.
- UR's preferred option is a bundle between BGE(NI) and Gaslink at Gormanston
  - i.e. no VIP or bundle combining Moffat capacity
  - this is in line with what the NRAs have been discussing at Moffat
  - Achievable for October 2015

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SNP exit charge

- CER published an exit tariff for the SNP in Aug. 2012
- We presented our view at an industry meeting in Jan. 2013
- CER and UR have commissioned joint legal advice
- This indicates that the EUCJ is likely to conclude that the tariff is not compatible with EU law
- CER has indicated that it is working on new tariff and that they expect publish their views later in October
- We have written to the CER to express our view on the new tariff

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