Consultation on Harmonised Transmission Tariffs for Gas

Phoenix Natural Gas Ltd. Response

15 August 2018

Introduction

Phoenix Natural Gas Ltd. (PNGL) welcomes the opportunity to respond to the Utility Regulator's (UR) consultation on Harmonised Transmission Tariffs for Gas. PNGL has several comments regarding the detail of the proposal which we would be keen to explore further with UR as part of this consultation process.

Capacity Commodity Split

PNGL has a licence obligation (Condition 2.13) to book sufficient exit capacity on the transmission network for a 1 in 20 peak winters day scenario. PNGL believe it is worth remembering why the introduction of this obligation was considered appropriate. Reasons included:

- Supporting the introduction and development of supply competition by removing complexity from the capacity booking processes;
- Prevent the hoarding of capacity by incumbent or larger shippers;
- Prevent the double booking of capacity which would increase costs to gas consumers; and
- Ensure sufficient exit capacity is held on the Northern Ireland (NI) transmission network to facilitate distribution network growth and increase the use of natural gas in NI.

PNGL believe all of these reasons are still applicable. With the above points in mind, PNGL do not believe that the UR proposal in section 5 of the consultation paper to amend the capacity commodity split from 75:25 to 95:5 supports the regime principles and we envisage the following negative impacts if implemented:

- **Damage to Gas Distribution Network Growth:** As a network operator, PNGL recognises the need for cost reflectivity when considering an appropriate capacity commodity split but we have consistently argued that cost reflectivity cannot be allowed to take precedent over provision of a regime which encourages and supports the development of a growing natural gas industry in NI. We have consistently argued that the current 75% of revenue recovery attributed to capacity was too high in relation to supporting network growth and therefore this proposal to further increase the capacity element is not considered helpful in this context.

- In paragraphs 5.24 and 5.26 of the consultation UR estimates that the amendment to the capacity commodity split will:
    - Move 3-5% of transmission services from power stations to gas consumers; and
    - Increase a domestic consumer's gas bill by around £2-4 per year.

PNGL analysis supports these figures but it should be noted that if the actual capacity and volume figures deviate from the forecasts used to determine the tariffs then this has the potential to exceed the estimates published by UR in the consultation. Increases in end prices to consumers such as this have the potential to impact growth especially at a time when Distribution System Operators (DSO) are investing in network extensions and entering new towns which have no previous gas usage experience.

- **Credit Support Arrangements:** PNGL accepted a licence obligation to book transmission exit capacity on behalf of gas suppliers on the understanding that the distribution business would bear no financial risk. We agreed to undertake the many requirements of the role with no allowed costs for resourcing the activity or financial benefits received. The requirements include providing credit support with GMO NI for the exit capacity booked as per section 18 of the NI Network Gas Transmission Code (NINGTC). Currently PNGL are able to satisfy the Required Level of Credit Support with their credit rating but our analysis shows that with the proposed change to the capacity commodity split the Required Level of Credit Support will exceed the Maximum Allowed Unsecured Credit as detailed in paragraph 18.5.8 of the NINGTC. From reviewing the other credit support options in the NINGTC, the only viable option would be a standby Letter of Credit. It is our understanding that this is charged on an annual fee basis which is c1.75% of the outstanding amount. There has been no allowance in PNGL's GD17 price control for this financial cost and there is no other cost recovery mechanism in place to address this.

  This new proposal now places additional financial obligations on PNGL and adds risks to the activity which cannot be facilitated. A solution to this negative aspect of the changes proposed could be mitigated with a review of the Maximum Allowed Unsecured Credit amounts as detailed in paragraph 18.5.8 of the NINGTC. We do however understand that that as part of a recent NINGTC Code modification, GMO NI reviewed the levels of credit support offered using unsecured credit methods and deemed the current levels as appropriate.

  Power Generation Connections to DSO Networks: PNGL has recently received enquiries from parties interested in connecting to the PNGL distribution network to provide power generation during periods of peak usage on the electricity grid. Projects of this type have large firm capacity requirements but low annual gas volumes and it is PNGL's understanding that they will become increasingly necessary to support the electricity grid. PNGL recover monies paid for transmission exit capacity through a commoditised charge but potential projects like this will require exit capacity bookings to be increased which will not be adequately recovered from the individual customer through the commoditised charge as their annual volumes are estimated to be low. This means that the additional costs could be recovered from other consumers notably domestic consumers picking up costs associated with power generation requirements. The proposed change to the capacity commodity split from 75:25 to 95:5 will only increase the scale of this issue. PNGL has commenced discussions with UR on the impact of these network connections and in particular the implications they have for the exit capacity booking process especially with regards how charges are passed on but would welcome more detailed dialogue before any decision is taken with regards this consultation.

The consultation paper also considers, in paragraphs 5.16 to 5.19, applying the capacity commodity split of:

- Great Britain (GB) – 97:3 (subject to consultation); and
- Republic of Ireland (RoI) – 90:10

PNGL note that UR justifies its decision in part with reference to GB which is a fully mature gas market and is therefore an inappropriate comparison. We also note that RoI, which would be considered a much more mature gas market than NI, will be operating on a 90:10 capacity commodity split. It would be useful to understand the costs associated with gas throughput in RoI which has determined this higher commodity element.

Proposed Reference Price Methodology

In paragraphs 4.2 to 4.7 of the consultation paper, UR explain why they believe the Postalised tariff regime meets the requirements of a Reference Price Methodology (RPM) in the Harmonised Transmission Tariff Structures for Gas ("TAR NC"). PNGL note that UR are required by the Regulation to compare the resulting indicative reference prices for any approved tariff structure to a capacity weighted distance ("CWD") counterfactual which is included in paragraphs 4.32 to 4.34 and Annex 2 of the consultation paper. From this analysis we see that the CWD RPM demonstrates that gas consumers in the PNGL distribution network area significantly subsidise other gas consumers under the Postalised tariff regime and in some instances power generation, i.e. electricity consumers. While PNGL continue to believe that the use of a Postalised regime in NI is an appropriate approach and support its ongoing application, we believe the TAR NC requirement of ensuring non-discrimination and limiting cross subsidy across transmissions network users must apply to all elements of the NI transmission tariff regime and any decision which alters the approach to apportionment of costs has to take into consideration all aspects of cost recovery, i.e. amendments to capacity commodity split should not be considered in isolation of all other regime components.

EU Legislation Compliance

PNGL notes that in paragraphs 3.4 and 3.5 of the consultation UR anticipates the need to comply with the European Union (EU) Regulation 715/2009 by the 31st May 2019 even though the UK is expected to leave the EU by this date. PNGL would request a fuller explanation of why the UR believes that the NI gas industry needs to comply with this regulation? The TAR NC is another example where the requirements do not recognise the uniqueness of the NI gas industry, within the EU context, where the gas industry is still being developed and has to recognise significant growth particularly in the domestic and small business sectors.

In the past decisions to implement EU requirements have been necessary due to the integration of the NI Network with GB where a NI regime out of step with GB was unavoidable, however it would appear to PNGL that the requirement for a revised capacity commodity split is an area where integration issues do not exist. Any decision in this area could be taken based on NI only requirements.

Compensation for Interruption

PNGL note that the consultation paper discusses potential discounts to capacity products, in paragraphs 4.11 to 4.16, with UR's intention to use the ex-post discount meaning that network users would be compensated after an actual interruption for each day the interruption occurred. PNGL would like to understand how UR envisage this being applied at DSO exit points as the current regime has not been developed to support this type of initiative?

Summary

PNGL continue to support the use of a Postalised transmission regime in NI and recognise the requirements for UR to consider any proposed legislative changes relating to its operation. However, we strongly believe that the proposals contained in this consultation and in particular the suggested change to the capacity commodity split will have a detrimental impact on gas consumers and the continuing development of the gas networks and therefore do not support the proposal. We believe any solution must consider the overall Postalised regime in the context of the legislation requirement for non-discriminatory practices and therefore strongly encourage UR to use its regulatory discretion to deliver the most cost-effective solution for all NI gas consumers which continues to support the growth of an efficient and economic natural gas industry.