

**Common Arrangements for Gas – Security of Supply
Phoenix Natural Gas Group Response
30th January 2009**

The Phoenix Natural Gas Group (Phoenix) welcomes the opportunity to provide comment on the Common Arrangements for Gas – Security of Supply consultation paper. The response includes specific comments provided by Phoenix Natural Gas Limited (PNG) as owner and operator of the distribution network in Greater Belfast and Phoenix Supply Limited (PSL) which supplies natural gas to around 120,000 homes and businesses in the Greater Belfast Licensed Area.

In considering this response Phoenix has assumed that the security of supply issues addressed in the consultation relate to the issues surrounding the transmission networks in both the Republic of Ireland (RoI) and Northern Ireland (NI) and any references to distribution networks are for information purposes only.

Detailed below are our comments on the specific questions asked in the consultation paper.

5.1 Network Security of Supply Standards

1. Should an obligation be placed on network operators to build and maintain the network to a 1-in-20 or a 1-in-50 peak-day?

Phoenix does not operate a transmission network and therefore does not feel it is appropriate to comment on what is required at transmission level. The decision for the level of security applied to transmission pipeline is best made by the transmission pipeline operators.

2. Is a period of five days appropriate for the period for which supplies to domestic customers must be protected in the event of a partial disruption to national supplies?

PSL Comments: As a supplier to around 110,000 domestic customers we consider that a period of five days for which supplies to domestic customers must be protected is inadequate. It is conceivable that there could be supply disruptions which last in excess of five days and we believe domestic consumers should be protected during these periods.

However, we do recognise the need to balance the cost of providing additional days protection with the likelihood of disruption occurring and the associated impact on domestic consumers and would recommend the

Regulators (the Utility Regulator (UReg) and the Commission for Energy Regulation (CER)) complete additional work in this regard.

We also note with concern the comment on page 21 of the Consultation document which notes that "*supplies to Moffat being cut-off only when supplies to domestic customers in GB can not be maintained*". We would request that the Regulators confirm if this means that supplies to Moffat could potentially be cut off to maintain supplies to domestic consumers in Great Britain (GB). If this is the case, we would recommend that the Regulatory bodies, both UReg and CER, address this issue with Ofgem to ensure that any decision regarding supplies to Moffat must take into account the potential for disruption to domestic consumers downstream of Moffat and ensures that domestic consumers in Northern Ireland and GB are treated on an equitable basis.

PNG Comments: The appropriate number of days for which supplies to domestic customers must be protected is very much dependant on the type of situation that arises. Two days may be appropriate to manage simple damages to the network, however, two days or indeed five days may be totally irrelevant when attempting to manage a major incident on any pipeline, particularly subsea, which could take months to resolve. We believe the number of days determined is a judgment call depending on the nature of the incident but would agree that the more days that gas is readily available for, the greater the level of comfort as a distribution operator we would have. Ultimately the cost of protecting supplies to domestic customers for more days must be weighed up against the probability of the relevant incident occurring and the magnitude of the impact of the incident.

3. Does a peak-period (as specified in 19A (1)(c)(ii) of the 2002 Act) need to be specified? Or does a 1-in-50/1-in-20 peak-day imply a sufficient period for this purpose?

PNG Comments: PNG would ask how peak-periods for transmission networks could be defined particularly when they are connected to Distribution networks that are expanding with new connections on a daily basis and will continue to do so for a considerable period of time.

4. Are there additional minimum standards required for other energy undertakings or offshore producers?

PSL Comments: There may be an opportunity to bolster the sources and the quantity of gas, albeit on a marginal basis, which may be available in Ireland in the event of a supply disruption by placing minimum standards on other energy undertakings. For example, it may be appropriate to ensure there is a minimum level of LNG which is 'stored' at any future LNG plant.

PNG Comments: It would seem appropriate that any minimum standard required to be met by either a gas operator or gas supplier should also apply to other energy undertakings or offshore producers.

5.2 Obligations on Shippers and Suppliers

1. Should shippers/suppliers be required to book peak-day/severe winter capacity for a 1-in-50 or a 1-in-20 for peak-day? What costs would be incurred by shippers/suppliers in order to meet such proposed requirements?

PSL Comments: Shippers/suppliers should be required to book capacity for a 1-in-20 peak day, the costs of which, in Northern Ireland, should be allowable under the Price Control mechanisms.

2. Should shippers/suppliers be required to secure supplies for a 1-in-50 annual demand or a 1-in-20 for peak-day? What costs would be incurred by shippers/suppliers in order to meet such proposed requirements?

PSL Comments: We do not believe this is a relevant condition as it would require suppliers to secure gas which they may not use and would therefore lead to increased costs for consumers.

However, we do believe that as a reasonable shipper/supplier, shippers/suppliers should have reasonable arrangements in place to ensure they can meet supplies for a 1 in 20 peak day.

PNG Comments: When the decision was taken to place an obligation on distribution operators in Northern Ireland to hold sufficient capacity to meet a 1 in 20 peak day, it had been further proposed to remove the obligation from supply licences to secure gas supplies for a 1 in 20 peak day. It appears that this has never happened. The reason for its proposed removal from supply licences was that to secure supplies to meet a 1 in 20 peak day or a 1 in 50 severe annual demand would require suppliers to secure gas they may never use and therefore possibly lead to increased costs to consumers. The ways in which suppliers secure gas today is very different to the long term contracts in place when the supply licences were originally drafted.

3. Should obligations be placed on shippers/suppliers ensuring minimum levels of diversity in their contracted sources of supply?

PSL Comments: We do not believe the consultation paper has identified or made the case as to why this would be an appropriate condition to place on shippers/suppliers.

By the nature of competitive markets (and where there is no competition, the potential for competitive markets) ensures that shippers/suppliers are incentivised to source their supplies from what they perceive to be the lowest cost source. In some cases this may result in the shipper/supplier having available to them a range of sources of supply, depending on their relative size.

An obligation on shippers/suppliers to have available a range of contracted sources of supply would in all likelihood lead to increased cost to consumers. There are sources of supply which are technically available to shippers/suppliers but which would not be economical for a small supplier (in GB context) to utilise.

As the Consultation paper also identifies, any such condition does not necessarily reduce the risk of an interruption to supplies occurring at Moffat. For example, a shipper/supplier may well have diverse sources of supply by, say, purchasing gas at NBP, from Rough storage and also from LNG sources in GB, however, this would provide no advantage in the event of supply disruption at Moffat or downstream or on the NTS.

Furthermore we do not believe shippers/suppliers should be required to underwrite the investment required to develop LNG or storage facilities in Ireland which would be the effect of requiring shippers/suppliers to hold minimum diversity levels in their contracted sources of supply.

The existing NI licence obligations are sufficient in respect of security and continuity of supply.

4. Should obligations be placed on shippers/suppliers relating to long-term contracts?

PSL Comments: GB has one of the most liquid and freely traded natural gas markets in Europe, if not in the world. Natural gas supplies are available to shippers/suppliers on future markets from one day to many years in advance. Each shipper/supplier makes purchasing decisions based on their assessment of market trends and when they perceive they are able to secure natural gas at the lowest possible price. On some occasions this may result in purchasing gas on the prompt market, as this may be perceived to offer the best value.

An obligation on shippers/suppliers to enter into long-term contracts could well result in consumers paying more for their natural gas than they would otherwise need to. In addition, as the market in the Greater Belfast area is fully opened to competition a shipper/supplier would have exceptional difficulty in determining the level of gas requirements they need to secure on a long-term basis as they have no indication what market share they will hold at that time.

The imposition of such an obligation would therefore require the shipper/supplier to recover the costs of any such long-term contract in the short-term as they have no guarantee they will have the customer base from which to recover these costs in the long-term.

5. Are shipper/supplier obligations best provided for through licence conditions or through the Code(s) of Operations?

PSL Comments: Shipper/supplier obligations are best dealt with through licence conditions, however, PSL believes the existing NI licence obligations are sufficient in respect of security and continuity of supply.

5.3 Gas Storage

1. Should storage operators be required to hold minimum levels of storage?

It is most likely that any storage facility developed on the island of Ireland will be owned and operated by a commercial enterprise. A storage operator by the nature of its business will be incentivised to hold storage as it is only by parties making use of storage facilities that a storage operator can earn a return on its investment. Therefore to place obligations on storage operators to hold minimum levels of storage for strategic purposes may not work in a commercial environment. The key question is:-

Is a storage facility a commercial enterprise or is it a strategic storage facility?

2. Should shippers/suppliers be required to hold minimum levels of storage?

PSL Comments: PSL disagrees with the assertion on page 13 of the Consultation paper that commercial storage leads to reduced prices for consumers. This section of the paper is an over-simplification of how gas storage operates and the utilisation of gas storage does not always lead to consumers paying lower prices and will in some cases result in gas consumers paying higher prices.

We therefore do not agree that there should be an obligation on shippers/suppliers to hold a minimum level of storage. Again we do not believe that shippers/suppliers (and ultimately consumers) should be required to underwrite the investment cost of developing storage facilities in Ireland which would be the effect of shippers/suppliers being required to hold a minimum level of storage.

It may be more appropriate for a minimum level of strategic storage to be underwritten by government.

PNG Comments: The key to this question is that if there is an obligation on shippers/suppliers to hold the minimum levels of storage which shipper/supplier should have this obligation? In a competitive supply market where there is the possibility of suppliers' portfolios changing on a daily basis does it seem appropriate to place obligations on suppliers to hold a level of storage when they could find a significant proportion of their load has been lost to a competitor? However if it was deemed necessary by the Regulatory Authorities for suppliers to hold minimum levels of storage then it may be considered more appropriate for the Regulators to appoint one supplier whose costs for fulfilling such an obligation are underwritten for this purpose. Alternatively the requirement to hold a minimum level of strategic storage could be undertaken by government.

3. Should storage stocks in GB storage facilities be considered an appropriate security of supply measure?

Storage stocks in GB storage facilities can be considered as an appropriate security of supply measure for the island of Ireland. The main reason why they would not be based on the view that if there was an incident at the Moffat facilities, gas may not be able to be transported to Ireland. Therefore if there is a need for GB facilities to be considered appropriate for security of supply reasons for Ireland a view must be taken as to the likelihood of an incident occurring at Moffat which prevents gas flow to Ireland and to look at how to mitigate against this and what the costs would be. It is not reasonable in the real world to always plan for the ultimate disaster as in all operations proper risk assessments that calculate the likelihood of the risk occurring and the magnitude of the impact of it occurring must be taken into consideration when making any decisions i.e. spending money in Ireland to deliver localised Strategic Storage, whatever the cost, is not acceptable based on the view that GB storage is not appropriate because an incident may happen at Moffat which may prevent gas flows to Ireland.

4. Would obligations in relation to storage distort the Irish gas market?

Phoenix believes that any obligation placed on industry has the potential to distort the gas markets.

5. Are there sufficient incentives in place for the commercial provision of adequate storage?

Given that there are two interested parties currently considering the Larne storage project and that there are continuing considerations in developing further storage facilities in RoI would perhaps suggest that there are sufficient incentives in place.

Phoenix has detailed below several general comments it has regarding certain sections of the consultation paper.

Emergency Procedures – Any agreed arrangements at Transmission level need to take in to account the emergency procedures set out in Distribution Operator's Network Codes.

4.1 Emergency procedures in the event of a supply disruption

Is the production of a list of natural gas loads that will be the last to be shed an obligation for a transmission or distribution operator in RoI? In Northern Ireland this is an obligation for the distribution operators.

5.2 Obligations on Shippers and Suppliers

Definition of 1 in 20 peak day: When referencing the requirement for Distribution Operators in Northern Ireland to hold transmission capacity on a 1 in 20 basis the definition given refers to the 1 in 20 peak day criteria as the availability of a supply of gas for a defined peak period. The distribution licence does not require the operator to have available the supplies of gas but rather requires them to have an amount of capacity required to ensure that sufficient gas can be conveyed to meet daily firm demand.

On page 29 of the Consultation Paper it is noted that it is necessary to ensure consistent obligations on RoI and Northern Ireland shippers/suppliers in relation to security of supply. We do not understand why this should be the case and would welcome further clarification of the basis of this statement from both Regulators.