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Subject: SN Consultation

Dear Brian,

PNG welcomes the opportunity to respond to the SN consultation paper.

The circumstances of the NI transmission network whereby pipeline ownership is split amongst three companies makes it more difficult to adapt when new developments, such as "Postalisation" or "South North", arise. Our experience of regime change is that it is complex and this leads us to the conclusion that the changes to integrate South North should be "fit for purpose" and should go "no further than is necessary". This is particularly relevant given that any South North solution is expected to be overtaken by the development of an "all island gas regime" within the foreseeable future.

Against this background Phoenix is not persuaded that the radical and far reaching changes that would be necessary to implement a full blown "TSO" are justified. We understand the principal features of a TSO to be:

- i) a separate legal entity, jointly owned by the DPOs or independent
- ii) activities covered by a new licence
- iii) a single code covering all DPOs
- iv) the provider of daily operations for all DPOs
- v) the administration of credit, invoicing, payment etc. for all DPOs
- vi) the responsible party for HSE, maintenance and new connections/investment

"Phoenix does not support developing a full blown TSO"

Phoenix objects to the development of a TSO at this time for three reasons:

- 1) First, there would be a major impact on the current financial arrangements (credit, invoicing, payment etc.) which were agreed only recently through an extensive process of consultation and negotiation. There is no need to reopen these arrangements assuming South North is owned by BGE (NI). Although the arrangements are indeed complex, South North is unlikely to remove the barriers to simplification, for example, the reluctance of DPOs to share in the credit risk of the other DPOs.
- 2) Secondly, Phoenix would be reluctant to transfer control of activities such as maintenance or new connections to a TSO. As pipeline asset owner, Phoenix has ultimate responsibility for health & safety and, in law, these responsibilities cannot be delegated. In the case of an incident, the HSE investigate all parties (the asset owner, the TSO and relevant contractors) and can be expected to instigate criminal proceedings in cases of serious negligence.
- 3) Finally, there is a simpler solution which addresses the issues identified in the Consultation Paper and could be implemented much more easily and cheaply; this solution is summarised below.

“A single operator to undertake NI transmission services”

Ofreg is correct that the complexity and cost for Shippers to deal with 4 codes and 3 balancing areas is excessive; especially so when compared with the size of the NI market. Such a regime could be seen as a barrier to supply competition and may impose unnecessary costs on NI gas consumers.

In Phoenix’s view, this problem can be addressed if one of the DPOs is appointed to carry out transmission services on behalf of the other DPOs, covering:

- i) network analysis and planning,
- ii) tendering of interruption rights (and other comparable rights) to reduce the requirement for IC capacity,
- iii) determination of NI’s capacity requirements,
- iv) capacity booking and capacity allocation on behalf of Shippers,
- v) physical operation and balancing to manage pressure and flow,
- vi) sourcing balancing gas requirements from Moffat (or Rol production)
- vii) receiving nominations and allocating gas (including gas from Rol production)
- viii) maximising utilisation of SNIP and nominating excess requirements via IC
- ix) determining code charges (balancing, scheduling, capacity overrun, interruptible capacity)

The transmission services operator would provide a “one stop shop” for NI shippers in all areas apart from credit, invoicing and payment which would remain the responsibility of the Existing DPO under the existing arrangements.

Because gas flowing to a particular exit point may have flowed into the NI network at either Twynholm or Gormanston, post South North, all Shippers will need to be party to all the NI

codes. Accordingly, it may be desirable if a Shipper could accede to all the NI codes by signing a single framework agreement (we assume North West / South North will be covered by a single licence and code).

“PTL should fulfil the transmission services function”

Under current arrangements, PTL already carry out the transmission services function on behalf of the Phoenix transmission pipeline. In large part, the change to a single operator can be achieved if the North West / South North pipeline simply adopts similar arrangements as those which already exist between PTL and Phoenix.

The Phoenix Code is structured so that it sits within the umbrella of the PTL Code. All the Phoenix daily processes such as capacity booking, nominations and allocations are already carried out by PTL under the PTL Code processes. This is a considerable simplification for Shippers (and for Phoenix). The only major process carried out under the Phoenix Code is invoicing at the Belfast Exit Point. PTL’s activities on behalf of Phoenix are set out in a bi-lateral agreement covering the physical balancing of the Phoenix pipeline and the provision of information to Phoenix (capacity allocations and gas allocations) so that Phoenix can carry out its invoicing process.

These same principles could be readily applied to a new North West / South North code along with integration of the Phoenix / PTL bilateral agreement provisions into the terms of the existing NINOA (NI Network Operators Agreement).

Phoenix’s initial view of the changes that would be needed to accommodate South North is:

- i) provision for bi-directional flows within each code,
- ii) review of the PTL capacity regime to provide appropriate incentives to book firm capacity and interruptible capacity to promote capacity utilisation (we suggest it may be possible to retain the existing point-to-point capacity regime),
- iii) provision for shippers to nominate gas entry & exit at Gormanston (to source RoI gas production or to supply RoI consumers)
- iv) update of the PTL balancing rules to enable sourcing of balancing gas requirements from RoI, as and when cost effective,
- v) update of Scada and associated systems,
- vi) negotiation of a transmission services agreement amongst the DPOs to provide for sharing of information, consultation and participation in decision making.

The benefits of this approach are that it addresses the South North issues identified by Ofreg but does not require:

- i) changes to DPO licences or development of a new TSO licence,
- ii) changes to the financial arrangements amongst the DPOs which would be complex and costly to negotiate and very disruptive; for example, impacts on the PSA and trustee account banking arrangements
- iii) major negotiations with the HSE and revisions to DPO safety cases,

- iv) DPOs to delegate HSE, maintenance and new connection/investment responsibilities, which Phoenix would be reluctant to agree to.

In conclusion, Phoenix proposes that PTL is appointed as transmission services operator. Phoenix would like to discuss BGE (RoI)'s involvement, as agent to PTL, with the other DPOs before reaching its conclusion on this matter.

“Existing arrangements with BGE (RoI) should be extended to cover IC”

When Suppliers nominate gas at Moffat they should not be concerned whether their gas is transported on SNIP or IC. This should definitely be a DPO responsibility on the grounds of simplicity for Shippers (and the DPOs) and because PTL is best placed to maximise SNIP utilisation and minimise IC costs.

The best approach to contract with BGE (RoI) for transportation on IC is by extension of the existing operator-to-operator arrangement between PTL and BGE for transportation from Moffat to Twynholm (where the gas enters the SNIP for transportation to NI). It is important that the operational arrangements for IC are the same as Moffat-Twynholm, to avoid the need for PTL to operate dual arrangements.

Moffat-Twynholm transportation is provided for by a condition in the Irish Interconnector Treaty which was entered into by the Irish government and UK government in the early 1990s. The transportation arrangement is on “non code terms” and is described in the Executive Summary of BGE (RoI)'s Code of Operations. PTL is not bound to the BGE (RoI) Code and does not require a RoI Shipping Licence. It is stated that the technical and operational arrangements applying to PTL do not adversely affect the Code of Operations, do not impose a financial burden on RoI Shippers and do not materially affect BGE (RoI)'s ability to comply with its obligations under the Code.

There exists a further recent precedent for this approach - the arrangements for supply to Stranraer have been updated to accommodate the sale of NGT's Scottish distribution network which was bought by Scottish & Southern (“S&S”) earlier this year. S&S contract with PTL for transportation between Moffat and Stranraer but they do not sign the PTL Code and do not have an NI Supply licence; the applicable tariff is the same as the postalised charge.

“Consideration of RoI as a new source of gas for NI”

An important aspect, which the Consultation Paper mentions only briefly, is the significance of South North in providing access for RoI gas production to the NI market. In addition, the Paper does not confirm if South North will be able to flow gas from NI to supply the Irish market. Provision for flow from North to South is very important and must be confirmed. These considerations have economic implications for the NI and RoI gas markets and are also relevant to the security of supply of the gas network.

From the perspective of the RoI gas producer, NI should provide an attractive new market opening; likewise NI suppliers will be interested to diversify their supply options by contracting for gas supply from RoI producers. On the other hand the BGE (RoI) tariff structure is such that RoI gas may need to be priced at a discount to GB gas, if it is the case that IC gas bound for NI will not bear the Irish Exit Charge whereas RoI gas does bear this cost (please see Appendix A for BGE (RoI)'s 2004-05 tariffs).

Direct connection to the RoI gas market is also very significant from an NI transportation perspective as it gives rise to the possibility that NI postalised costs can be reduced. There are three ways this might be possible:

- i) Gas delivered from RoI (instead of via IC) would save the IC commodity charge, equal to 0.23 pence per therm.
- ii) Gas contracted from RoI on a firm basis (instead of booking firm capacity on IC) would (in addition to the commodity charge) save the IC capacity charge, equal to 543 pence per peak day therm.
- iii) On days when SNIP is not fully utilised, surplus SNIP capacity could be made available on an interruptible basis to deliver gas at Gormanston for the RoI market. The market value of this NI capacity would be capped at the level of the IC commodity charge.

Finally, a key rationale supporting the South North pipeline investment is the contribution which the pipeline can make to the security of gas supply on both NI and RoI gas networks. However there is no discussion in the Consultation Paper about this important issue. The key questions relate to how security measures in circumstances of a supply failure affecting the Irish Interconnector, SNIP or Inch, are to be delivered; are they to be left up to market forces or are they to be mandated by regulators (or some combination thereof)?

Consultation Paper Questions

We respond below to the questions posed by the Consultation Paper:

Booking Capacity

1 How should offtakes from SN in RoI be treated?

The investment in South North is underwritten by NI; therefore it is reasonable that any additional volumes to RoI consumers should benefit NI.

We suggest that BGE (RoI), as the downstream operator owning the RoI distribution assets, should contract for supply from South North without being required to hold an NI Supply Licence.

This approach to RoI offtakes is consistent with:

- i) PTL's arrangement with BGE for Moffat-Twynholm transportation,
- ii) S&S's arrangement with PTL for supply to Stranraer and,
- iii) Phoenix's proposals for arrangements for Moffat-Gormanston transportation.

The applicable tariff should be equivalent to the standard postalised charge, which is consistent with the Stranraer tariff. However, in terms of the tariff charged to the end consumer, BGE (RoI) may wish to be consistent with tariffs charged to other RoI consumers, in which case any under or over recovery could be spread amongst its customer base. This is how S&S treats gas consumers in Stranraer.

There may be an incentive to supply Moffat gas (as opposed to gas produced in the RoI) to RoI consumers offtaking from SN to avoid payment of the BGE (RoI) exit tariff.

2 Should NI Shipper's RoI transmission costs (other than IC) be postalised?

RoI transmission costs should not be postalised in the same way that GB transmission costs should not be postalised.

Nonetheless, consideration should be given to whether there is economic benefit to the postalised regime because of gas supplied from the RoI entering the NI network.

Benefit is derived where gas entering the NI network from RoI reduces the amount of gas sourced through IC which, in turn, reduces the IC transportation costs which are postalised.

It may be possible to reduce the IC capacity costs as well as the commodity costs if it is possible for Suppliers to secure firm obligations to deliver gas from the RoI.

In certain well defined circumstances it may be appropriate for the postalised regime to offer a credit in return for RoI gas supply.

Identifying IC Capacity

3 How should required IC capacity be determined?

Phoenix proposes the amount of IC capacity and the period for which it should be reserved should be determined by PTL as the transmission services operator. The assumption that there is adequate spare capacity headroom on IC should be reviewed each year by PTL in consultation with the other DPOs and Ofreg. Assuming adequate capacity headroom exists, IC capacity should be determined annually and reserved for the next 12 month period commencing 1st October. There are certain circumstances where PTL may need to increase the capacity booking within year, for example if a large new load is connected during the winter period.

4 Should factors other than NI demand and SNIP capacity be used to determine required IC capacity?

Yes. It may be possible to reduce the requirement for IC capacity in two ways:

- i) PTL securing rights to interrupt large consumers in NI
- ii) Suppliers securing a firm obligation to supply from RoI producers
Phoenix proposes there should be an annual tender to RoI Suppliers to invite:
 - i) demand side interruption and,
 - ii) firm obligations to supply gas from RoI.

The quantity of offers accepted should be capped at the quantity of IC capacity required and the price paid should be capped at the IC transportation cost.

A further consideration is that there may be operational requirements whereby gas must be sourced via IC even where SNIP capacity is not fully utilised. This could occur if Phoenix constructs a fourth transmission offtake at Lisburn (from the South North pipeline) to alleviate distribution constraints in the Greater Belfast supply area or if

offtakes are built from South North to consumers within the RoI. In these cases, PTL will need to conduct network analysis to confirm if there are any circumstances where IC gas is needed to maintain pressure and flow, and whether this will add to the IC capacity requirement.

In the past it has been suggested that the opportunity cost of distillate as a consequence of a large load being interrupted should be charged to postalisation; Phoenix rejects this approach in favour of the market based approach outlined above.

There has also been concern expressed about the environmental consequences of using distillate instead of gas. We suggest these environmental consequences are insignificant given the short duration of the interruption, which, in normal years, may only be a few hours over a few days.

Booking IC Capacity

Option A: Shippers book IC capacity

5 Should Shippers book IC capacity?

No, this would be too complex for everybody. It might be seen as a barrier to supply competition.

Shippers would need to obtain a RoI Supply Licence and sign the BGE (RoI) Code together with the ancillary agreements.

There would need to be complex processes within the NI Codes to advise how much IC capacity each individual Shipper should book.

There is no provision in the BGE (RoI) Code for Shippers to use each other's IC capacity rights, other than through secondary trading of rights which may be administratively cumbersome.

6 How would shippers be reimbursed if they pay the IC tariff?

Phoenix does not support Shipper involvement with IC capacity booking or daily operation. However, if Shippers did perform these functions, we propose they should submit proof of charges to their Exiting DPO, who would pass the cost through to the PoT and reimburse the Shipper. This would require some amendments to the PNG and NWP licences, but it would avoid the need for Shippers to have a direct relationship with the PoT, which would be very complicated indeed. Alternatively Shippers could seek reimbursement from PTL, although this would also require amendment of the PTL licence.

Option B: a DPO books IC capacity

7 How problematic would it be for a DPO to sign the BGE RoI Code?

A DPO should not be expected to sign the BGE (RoI) code, which would also require the DPO to obtain a RoI Shipping Licence.

There are precedents for a connected operator to contract for transportation services without the requirement to sign the upstream code. These are:

- i) PTL's Moffat-Twynholm transportation arrangement with BGE (RoI)

- ii) S&S's transportation arrangement for supply to Stranraer with PTL

We should seek to contract for IC transportation on a similar basis as the existing Moffat-Twynholm arrangement. This should enable a consistent approach and avoid duplication of operational systems.

8 Which DPO should perform this role?

To ensure a co-ordinated approach it is important that only one party is responsible for determining the IC capacity booking and for managing the contractual relationship with BGE (RoI) at Twynholm and Gormanston.

For the reasons set out in our response to question 20, Phoenix propose that PTL should fulfil the NI transmission services function, including determination of the IC capacity booking.

IC Operation

Option 1: Shippers told when to nominate on IC

9 Should shippers be obliged to make all nominations through SNIP first?

Yes, as this will minimise postalised costs. However, Shippers nominating on IC is too complex. Shippers will be ambivalent whether their gas travels from Moffat on SNIP or on IC. It should be PTL's responsibility to nominate on IC.

10 How easy will it be for NI and RoI code timings to work together?

First of all we should review the timings which apply to the Moffat-Twynholm transportation arrangement, which form the basis on which the NI regime code timings have been determined. It may be simplest to extend these timings to the IC transportation arrangement.

Generally, It would assist the consultation process if BGE (RoI) and PTL agreed to grant access to the terms of Moffat-Twynholm transportation arrangement which Phoenix understands is subject to a confidentiality clause.

A chart comparing the deadlines and the renomination lead times in the relevant codes is attached as Appendix B. This demonstrates that:

- i) At D-1, BGE's nomination deadline is 2 hours later than the NI regime deadline.
- ii) On D, the deadline for BGE's last renomination is 45 minutes later than the NI regime deadline.
- iii) The only conflict appears to be in circumstances of a renomination change exceeding 50% very late on D, which could be rejected by BGE but accepted by PTL.

Option 2: Shippers free to nominate on IC even when SNIP is not full

11 Should shippers nominate on IC no matter how much capacity is available on SNIP?

No. This would add to postalised costs by 0.23 pence per therm, the current IC commodity charge.

12 How should IC code charges be recovered through Postalisation?

IC charges should be recovered in the same way that PTL recovers charges arising from the Moffat-Twynholm transportation agreement.

There should be complete transparency about the charges, and PTL as the transmission services operator should be accountable for the charges and publish a detailed account, explaining its performance.

A single transmission services operator is essential to manage and optimise code costs which arise at Twynholm and Gormanston.

The code charges negotiated for IC transportation should be compared with existing precedents, namely:

- i) Moffat-Twynholm code charges,
- ii) BGE (RoI) code charges,
- iii) PTL code charges applicable at Stranraer.
- iv) NGT code charges at Moffat

Option 3: a DPO nominates amounts on IC which are above SNIP capacity

13 What agreements will need to be in place to facilitate option 3?

The main agreements are as follows:

- i) an IC transportation agreement,
- ii) an agreement amongst DPOs, setting out the terms for appointment of PTL as transmission services operator,
- (iii) accession of all NI Shippers to all NI transmission codes, possibly through signature of a single framework agreement.

Various amendments will also be required to the existing transmission codes and agreements amongst connected operators (some possible changes are summarised on page 3).

There may need to be some limited amendment to one or more of the DPO licences.

14 What agreements should we seek to put in place with CER/BGE (RoI) for shipping gas on IC?

To ship gas on IC we need to negotiate an IC transportation arrangement between PTL and BGE (RoI). This should be on a similar basis to the Moffat-Twynholm transportation arrangement, in that PTL should not require a RoI shipping licence or have to sign the BGE (RoI) code. At the same time, we should review the terms of the Moffat-Twynholm transportation arrangement to ensure consistency with the IC transportation arrangement.

Other areas for discussions with CER/BGE (RoI) include:

- i) Review of the BGE (RoI) tariff regime to consider if gas produced in RoI can be competitive with GB gas for supply to the NI market.
- ii) The use of spare SNIP capacity to supply the RoI market.
- iii) Consideration of the role of South North to enhance supply security for the NI and RoI gas markets and the rules that will be needed to underpin this.
- iv) The arrangements for offtaking gas from South North for consumers inside RoI

Single TSO

15 What are the costs to Shippers of having to deal with four codes, three balancing areas etc.?

These costs are unacceptable; they could potentially represent a major barrier to supply competition. There is a much simpler solution as described on pages 2 and 3 of this response.

16 What obstacles do DPOs see to creating a single TSO?

The introduction of a “full blown TSO” is not required to meet the requirements of South North. The main obstacles to a full blown TSO are:

- i) major changes to DPO licences and the creation of a new TSO licence,
- ii) major negotiations with the HSE and revisions to DPO safety cases,
- iii) changes to the financial arrangements amongst the DPOs which would be complex and costly to negotiate and very disruptive, for example, impacts on the PSA and the trustee account banking arrangements,
- iv) the requirement for DPOs to delegate HSE, maintenance and new connection/investment responsibilities, which Phoenix would be reluctant to agree to.

There is a much simpler solution which avoids these obstacles and meets the requirements of South North; it is described on pages 2 and 3 of this response.

17 What contracts will have to be drafted/amended?

A full blown TSO would require

- i) major changes to DPO licences and the creation of a new TSO licence,
- ii) major negotiations with the HSE and revisions to DPO safety cases,
- iii) major changes to the financial arrangements amongst the DPOs, including contracts with the PSA and the trustee account,
- iv) development of a single transmission code for NI,
- v) renegotiation of DPO arrangements covering engineering and maintenance.

18 What structure should the TSO take?

Instead of a full blown TSO, Phoenix proposes that PTL should carry out a more limited transmission services function on behalf of all the DPOs. Under current arrangements, PTL already carry out the transportation services function on behalf of the Phoenix transmission pipeline. In large part, the change to a single operator can be achieved if

the North West / South North pipeline simply adopts similar arrangements as those which already exist between PTL and Phoenix.

19 How should the TSO be financed?

The cost of PTL's existing transmission services function is funded from the postalised PoT. If PTL took on a wider transmission services role covering South North and IC transportation this should not impact operating costs very much, although there may be some IT set up costs. We envisage PTL would recover one off costs and any additional operating costs from the postalised PoT.

20 Who should be the TSO?

PTL already carry out the transmission services function on behalf of the Phoenix transmission pipeline. If PTL was chosen as the transmission services operator, in large part the change to a single operator can be achieved if South North / North West pipeline simply adopt similar arrangements as those which already exist between PTL and Phoenix. It also helps that PTL already carry out the network analysis and capacity planning function on behalf of all the DPOs.

In conclusion, Phoenix proposes that PTL is appointed as transmission services operator. Phoenix would like to discuss BGE (RoI)'s involvement, as agent to PTL, with the other DPOs before reaching its conclusion on this matter.

Interruptible Service

21 Do parties want to see an interruptible service continue?

The purpose of interruptible capacity services is to encourage utilisation of the transportation system at off peak times and generate additional revenue, which is used to reduce the tariffs paid by firm capacity holders.

However, the risk inherent to interruptible capacity is that it is used in preference to firm capacity and that this results in a revenue deficit which has to be funded by the firm capacity holders.

At present the PTL Code capacity provisions do not incentivise the booking of firm capacity so there is a risk that users will see interruptible as a cheap alternative to firm. This gap in the PTL capacity provisions should be addressed. A possible remedy is that an interruptible service is not offered unless firm capacity has been sold out.

Assuming there are appropriate measures in place to assure that interruptible capacity produces net benefits to firm capacity holders, then Phoenix would support interruptible services.

22 What charge do Consultees think appropriate for an interruptible service?

In a scenario where the NI regime is obliged to book IC capacity to meet its firm requirements, then the value of interruptible service is capped at the IC transportation cost.

Ideally, the price of interruptible capacity should be set by market forces to ensure it is fully valued. However it is likely that the NI market will not be sufficiently liquid to provide the competition needed for market based pricing to work.

If this is the case the DPOs should seek to understand the drivers behind the market value of interruptible capacity and design a pricing regime which, as far as possible, maximises revenue.

23 What additional costs would a 100% load factor tariff bring?

Phoenix understands this question to refer to the set up costs associated with changing the existing interruptible tariff.

The consultation paper references impacts on IT systems, modifications to licences, codes, the PSA and possibly to ancillary agreements. It would appear these costs may be quite significant.

Phoenix suggests a cost benefit analysis is undertaken by the DPOs to decide if changing to an alternative pricing methodology can be justified. This analysis would consider the use of interruptible capacity in 2004/05, additional market openings for interruptible capacity and how interruptible capacity should be priced for each market. The costs to make the necessary changes would also be estimated.

BGE Tariffs (2004-2005)

		IC/SN	IC	Inch
Entry	p/peakday/therm	543	543	118
	p/therm @ 100%LF	1.49	1.49	0.32
Exit	p/peakday/therm	nil	804	804
	p/therm @ 100%LF	nil	2.20	2.20
Com	entry p/therm	0.23	0.23	0.07
	exit p/therm		0.37	0.37
	Total	0.23	0.60	0.42

Diagram showing Code timings

