Postalisation for the Northern Ireland Gas Transmission Network:- DETI/Ofreg decisions following June Consultation

Dear

Thank you for responding to our June Consultation Paper which sets out our recommendations for the operation and implementation of Postalisation. In light of the comments received and after further analysis we would like to take this opportunity to set out our decisions on some key issues regarding the financial mechanism. This paper details these decisions and provides updates on some of the other aspects of postalisation implementation.

Decisions

Payment of the Postalised tariff

Postalisation will operate as an exit point payment mechanism. Suppliers will pay the postalised commodity and capacity charges based upon their booked capacity and volumes transported at the point where they exit the transmission network (subject to any ship-or-pay or minimum revenue commitments). A supplier will not have to pay any transportation tariff for pipelines through which it is transiting (e.g. Coolkeeragh transporting gas through PTL pipeline).

Once their pipeline is designated, a transmission operator will be obliged under its licence to charge its exiting suppliers the postalised tariff. Suppliers – the users of the transmission network- will in turn be obliged to pay the postalised tariff. The obligation on suppliers to pay the tariff will be two–fold: they will be obliged under their own supply licence to pay the postalised tariff, and there will also be a contractual commitment under the transportation code with their primary TO. It is for suppliers to ensure that their contracts with consumers are consistent with their commitments to pay the postalisation tariff.

Capacity/Commodity proportions to the tariff

The postalised tariff will have two parts; a proportion recovered through a capacity charge and the remaining proportion recovered under a commodity (volume) charge. We have decided that the relative proportions will be those recommended in the June consultation paper.

Table one: Capacity-Commodity Split

Year	2005	2006	2007	2008	2009	2010	2011
Split	50:50	50:50	50:50	50:50	75:25	75:25	75:25

There will be no payment holidays for new distribution towns. Likewise capacity will be booked on an annual, not a monthly, basis.
Regarding the appropriate split post 2011, we are considering the requests to determine an explicit split now, as this would help the financial certainty facing consumers.

Tariff duration for postalisation; coping with under/over recoveries.

Ofreg/DETI has decided upon a system of annual tariffs with any under/over recoveries dealt with through an end-of-year reconciliation payment.
The concerns raised by some respondents should be eased by the fact that the financial system will contain mechanisms to improve the predictability of both the annual tariff and the magnitude of the reconciliation payments. An end of year reconciliation payment system should help to attract low cost debt finance into the Northern Ireland gas industry.

The system will have the following characteristics:

- Only allowable in-year variations in required revenues will be passed through at the end-of-year reconciliation.
- Indicative tariffs for the following four years will also be published when announcing the annual postalised tariff.
- TOs will circulate actual volumes each quarter (allowed variations in required revenue will also be calculated and displayed).

  This should give suppliers/ end-users plenty of forewarning on the magnitude of the bullet payments giving them time to factor the payments into their plans. Providing the quarterly updates will give the transmission operators an opportunity to also inform the suppliers of any events that impact on the indicative tariffs for the following four years
- There will be no shipwreck clause, instead there will be a 15% cap on the bullet payment.

  Ofreg has decided that in light of the complexities and difficulties in designing and defining a ship-wreck clause that were raised in your responses, it shall not go ahead with its implementation.

  Instead, there will be a 15% cap on the variation to the end-of-year revised commodity tariff for the passing through of under/over recoveries. Any excess above the 15% will be rolled through at the weighted average of the three transmission operators' allowed rate of return and included in the respective year three tariff.

Other aspects of postalisation

Costs associated with transporting gas to Northern Ireland through alternative entry point to SNIP

The postalised tariff will include an allowance for the costs associated with the delivery of gas to the Southnorth pipeline. Only costs associated with capacity required (and the associated volumes) over and above maximum SNIP capacity will be included into allowed postalised costs.

The details and methodology of how relevant costs are defined will require further analysis to develop an appropriate mechanism for such cost inclusion in the postalised system. Our current thinking is that the mechanism will work as follow:

In June before the postalisation year, PTL will inform Ofreg of the maximum capacity available on the SNIP. *(Need to think about the difficulty in defining this term)*

Following receipt from the three operators of their total exit point booked capacity, Ofreg will calculate the excess entry capacity required to meet total NI need above SNIP capacity.

An allowance to service this excess capacity (plus the associated volumes) will be calculated and included in the postalised tariff

It is important that this allowance is determined based upon the least cost option. The excess capacity can be satisfied either through the Irish Interconnector or through delivering Irish gas to the start of the Southnorth pipeline through the onland system. (*We had initial discussions with CER regarding the pricing of transit gas through the Irish system. We shared their reluctance to explore this concept in further details upon closer to the possibility).*

Northern Ireland suppliers will be free to book their entry capacity according to their own commercial reasons. However the allowance will be determined at the start of the year and will not be affected by the decisions of shippers.

Suppliers who transport gas into Northern Ireland via non-SNIP entry points will receive a share of the allowance at the end-of-year reconciliation. (*need to ensure that the appropriation method for the rebate will not create improper incentives)*

Proposed start date of postalisation

The Northwest pipeline (NW) is scheduled for completion around September/October 2004. With our intention for the postalised year to run from 1st October to 30th September each year, we are planning for postalisation to start on 1st October 2004. If the NW has not been completed and/or designated by 1st October 2004, Ofreg intends to begin postalisation without NW and include it into the postalised tariff as soon as it is commissioned. Coolkeeragh will be in the process of commissioning for six months following the completion of NW, and thus will consume below expected volumes initially. We are currently in talks with BGE on possible transitional arrangements to profile their first year allowed revenue in line with Coolkeeragh's contribution to postalisation in that year.

Timetable/next steps

Licence conditions relating to both TO and supplier licences will now be drafted up in line with these decisions and will be circulate in the coming weeks. Following consultation, we are aiming for the licence conditions to be finalised in end January.

In June, a number of respondents requested more detailed estimates for the postalised tariff. There are a number of issues that need to be determined to increasd the confidence of any estimates. Such issues include the appropriation of Phoenix transmission asset and the revenue determined licence formula for BGE.

Appendix one:

Timetable and detailed process for financial determinations during the postalised year

This section sets out the processes that need to be completed during the course of a postalisation year and the necessary timetable for a tariff to be in place at the beginning of the gas year - 1st October. For the purposes of this timetable 'Year 1' is the gas year for which the postalised tariff is set. The main steps in the process are described below.

Definitions:

Exiting supplier - For each TO, exiting suppliers are those who exit the postalised transmission system from their network.

Primary TO - For a supplier, its primary TO is the operator from whose network it exits the postalised system.

PSA - Postalisation System Administrator. It has been agreed that the PSA will be an independent body performing essentially an accounting task.

Step 1 – establishing the forecast postalised tariff for the Year

MID- JUNE (Year 0)

Exiting suppliers will be obliged to collect end-users' forecast volumes for the following five years. There will be no need to differentiate between firm and interruptible volumes. For Year 1, volumes must be profiled on a quarterly basis.

This information will be passed on to the primary TO of each exiting supplier. Each primary TO will have the ability to amend end-user forecast figures before submitting volume forecasts along with their own allowed revenue and capacity bookings for their exiting suppliers to Ofreg.

3rd week JULY (Year 0)

Ofreg will amalgamate the three TOs' submitted elements into one spreadsheet and publish this on its website as per the format outlined in appendix 2.

1st week AUGUST (Year 0)

Ofreg to direct the TOs on whether to submit to the PSA their original forecasts or to use figures as amended by Ofreg.

PSA to calculate the tariffs as per the approved model and to inform the TOs of the resulting tariff for the next five years.

3rd week AUGUST (Year 0)

TOs to inform suppliers and end-users of tariffs for following years and to publish figures on their websites.

Step 2 – In Year inter-TO revenue transfers

It has been agreed that the inter-TO transfers will take place on a monthly basis, based upon the formula detailed in the June paper.

Step 3 – Quarterly volume/cost update

On the first week after the end of each quarter the TOs will be obliged to produce a volume report detailing each end-user's actual volume during the postalisation year.

Step 4 – End of Year (EoY) reconciliation process

The sequence of the required actions under this EoY reconciliation will be:

October/November (Year 2)

- Volume reconciliation.

  Firstly TOs will notify the PSA/Ofreg of actual/deemed exit volumes (plus any extra capacity bookings and revenue earned under the interruptible service). The TOs will check whether power stations have met any ship-or-pay commitment deemed volumes and adjust the actual exit volumes accordingly.

- Allowed cost differentials pass-through

  TOs will notify Ofreg of any cost differentials in allowed operational expenditure which they are entitled to pass through at the end of the year. Ofreg will verify the cost differentials.

- Calculation of the revised postalised tariff

  Ofreg will notify the PSA of allowed cost differentials. The PSA will take the actual volumes (adjusted for any ship-or-pay volume shortfall); and the actual capacity and interruptible revenue figures and calculate the revised postalised commodity and capacity charge. The PSA will then notify Ofreg and the TOs of the revised postalised charges. There will be no financing rate applied to the end-of-year bullet.

- TOs will notify end users of additional credit/deficit payment based on the revised tariff plus any outstanding required payments arising from ship-or-pay shortfalls. (1st week December)

  At the same time, the PSA (or TOs) will calculate entitlements and receipts (based on out-turn volumes/deemed receipts) and notify each TO of the end of year inter-TO transfers.

Postalisation forecast tariff calculation: Inputs sheet template

A) Total Postalised System Allowed Costs

	Postalised year	year 2	year 3	year 4	year 5
Premier Transmission ARR					
Bord Gais Eireann ARR					
Phoenix Natural Gas ARR					
Irish Transmission Allowed costs					
TOTAL POSTALISED ALLOWED COSTS					

B) Operators Forecast Opex allowed to be passed through at end of year reconciliation in postalised year

	amount	category of cost
Premier Transmission		
Bord Gais Eireann		
Phoenix Natural Gas		

NOTE: it is still under consideration if any type of opex, where actual year amount differs from forecast, will be allowed to be passed through at the end of year reconciliation

C) Forecast volumes - MWhr

end customer	shipper	Postalised year	year 2	year 3	year 4	year 5
Ballylumford Power Station						
Coolkeeragh Power Station						
Phoenix distribution market						
New towns distribution market *Note: to decide whether to split new towns into each zone*						
Stranraer						
TOTAL FORECAST VOLUMES						

NOTE: we are aware of the possible significant interruptible volumes being supplied to Ballylumford. These volumes should be included when calculating the forecast commodity charge.

Profiling of the forecast volumes in the next postalised year - MWhr

end customer	Oct - Dec	Jan - Mar	Apr - June	July - Sept
Ballylumford Power Station				
Coolkeeragh Power Station				
Phoenix distribution market				
New towns distribution market				
Stranraer				

D) Exit Point (from the postalised network) booked capacity - maximum daily quantity (MDQ) MWh/day

end customer	shipper	Postalised year	year 2	year 3	year 4	year 5
Ballylumford Power Station						
Coolkeeragh Power Station						
Phoenix distribution market						
New towns distribution market						
Stranraer						
TOTAL FORECAST EXIT PT BOOKED CAPACITY						

NOTE: Future capacity levels should be based upon, not only the current allocations of capacity but also some estimation of possible capacity requests

E) Determination of Irish Transmission Allowed Costs

	Postalised year	year 2	year 3	year 4	year 5
Total Exit point booked capacity					
SNIP entry point max bookable capacity					
Shortfall in capacity =Irish Transmission booked capacity					
estimated load factor for IC throughput					
forecast IC volumes					
Interconnector entry tariffs -CER determined					
capacity					
volume					
Irish Transmission Allowed costs					
Capacity proportion					
Commodity proportion					

FORECAST POSTALISAED TARIFF	Postalised year	year 2	year 3	year 4	year 5
capacity charge					
commodity charge					

NOTE: The interruptible tariff will also need to be forecast at the start of year - we are assessing the options in light of the comments received for the June paper