

APPLICATIONS FOR NEW CONVEYANCE AND/OR SUPPLY LICENCES IN NORTHERN IRELAND

In April 2002 the Director General of Gas for Northern Ireland (the Director), at the request of the Minister for the Department of Enterprise, Trade and Investment (DETI), sought expressions of interests from parties regarding natural gas distribution and supply opportunities outside the current licence area of Phoenix Natural Gas. Following discussions with those who expressed an interest and having taken into account the issues which arose from those discussions, the Director and DETI (the Department) now invite formal licence applications from those who have already expressed an interest, or any other company with appropriate expertise and resources, for gas distribution and/or supply activities for these potential new areas¹. (By distribution we mean the transportation of natural gas through local or regional pipeline networks with a view to its delivery to consumers).

This paper sets out more information on the application process and explains the award and selection criteria.

Appendix 1 of this paper lists other documents/information sources that applicants may find useful.

The prospective licence area

The possibility of new natural gas distribution networks outside the area already covered by the Phoenix licence has been created by the issuing of a gas conveyance licence to Bord Gais Eireann (BGE) in January 2002 (Note - the licence is subsequently in the process of being assigned to BGE (UK)) for the development and operation of a gas transmission network. BGE (UK) plan to build this network in two phases:

¹ Although this paper invites applications for gas supply licences outside the current Phoenix licence area to tie in with the new gas distribution opportunities, companies can of course apply for supply licences within the Phoenix area for eligible customers at any time.

- a) A high pressure transmission pipeline to be constructed by BGE (UK) running between a connection point on the Ballylumford to Torytown pipeline and an off-take at Coolkeeragh Powerstation. This pipeline will be known as the Northwest Pipeline.
- b) A high-pressure transmission pipeline to be constructed by BGE (UK) running between Republic of Ireland's network and the Northwest Pipeline. This pipeline will be known as the South North Pipeline.

Potential applicants should note that the Northwest pipeline is planned to be operational by 4th Quarter 2004 and the South-North by 4th Quarter 2006.

This paper invites licence applications for potential distribution and/or supply projects for any area in Northern Ireland outside the existing licence area for Phoenix Natural Gas. It is envisaged that viable opportunities for these activities are most likely to lie in the area adjacent to the route of the planned BGE (UK) pipelines. Appendix 2 of this paper contains maps showing the planned routes of the two new BGE (UK) pipelines. The pipeline diameter is planned to be 18" which we understand should provide more than sufficient capacity for distribution network requirements.

Application Procedure

Applicants are requested to submit formal licence applications in accordance with the Gas (Applications for Licences and Extensions) Regulations 1996 (the Regulations), a copy of which can be obtained from HMSO offices. Under the current regulatory framework, distribution activities are regulated through conveyance licences and hence distribution applicants should apply for a conveyance licence.

These Regulations set out:

- The prescribed format for applications.
- Required Information
- Application Fees
- Requirements for publishing applications

These Regulations require the submission of detailed information including financial information about the applicant and the proposed licence activities, details of an applicant's relevant expertise, and a proposed development plan, which is necessary to permit the Director and Department to assess licence applications and, if applicable, decide between the merits of competing applications. The Director may also request clarification or further information during this process and may invite applicants to submit revised applications to take account of new considerations which emerge during the course of the process.

Applicants should submit proposals for one or more town distribution networks in a single licence application, e.g. ten separate towns can be included in one proposal with the licence area then defined as to include those ten. As much of the information as possible requested both under the Licence Applications Regulations (e.g. section 10 – development plan) and via this paper should be separately provided for each individual proposed town distribution network. Ideally, the information underlying the application should be presented firstly in the form of information for the entire proposal; then information sub-dividing the overall package into the individual town networks. This will be necessary for Ofreg and DETI to form a view as to the appropriateness of including each town in the overall proposed package.

DETI/Ofreg are aware that applicants may need to balance between the costs associated with their proposed networks and customer coverage, both with respect to the density of customer coverage within towns as well as the number of towns. Applicants may therefore submit if they wish more than one option within their application. However, as discussed in the award/selection criteria section below, Ofreg and DETI will be seeking to maximise the potential for gas industry development subject to viability constraints.

Applicants may take the opportunity within this process to demonstrate the need for financial assistance in order to make gas distribution in certain areas viable. However the allocation of European or central government grant to any gas project is not a matter for the Director, rather it is a matter for Government. Likewise, any assistance from for example District Councils, is a matter for the relevant District Councils.

Therefore submitted financial calculations should be shown gross, without any assumption of financial assistance.

Applicants should be aware that any financial aid to their projects is likely to require state aid clearance from the European Commission.

We request that the assumptions underlying any forecasts included in applications, are clearly explained in the proposals – these include information on potential customer base and volume requirements, penetration rates, population growth, etc. We also request that each applicant’s financial information makes clear the desired rate of return included in their development plan and the justification for it.

Exclusivity

Applicants who wish to apply for distribution and/or supply exclusivity should include the following information within their applications. (By exclusivity we mean a period in which no other company would be entitled to convey gas in the licensed area or, with regard to supply licenses, to supply gas to all or specified categories of customers).

- The duration and extent of the exclusivity they require.
- Their reasons for requesting exclusivity.

Applicants who request exclusivity should demonstrate why exclusivity is essential to their development plans. We are especially interested in understanding the potential benefits to consumers of allowing supply exclusivity. Applicants should express how the granting of supply exclusivity would have a beneficial impact on their proposals and development of the natural gas industry.

When judging any request for exclusivity for either distribution or supply projects, the Director General and the Department will take into consideration their duties under the Order and the appropriate European legislation.

Gas Supply Licences

Gas Distribution and supply activities are inevitably inter-dependent. It is vital for the development of a business in the supply of gas that there is a pipeline network in place. It is likely to be a requirement for the awarding of any supply licence that there is also a viable distribution proposal for that prospective area. The evaluation of applications for conveyance and for supply licences will be interdependent and the requirements of the most attractive distribution proposal(s) may be taken into account in awarding supply licences.

“Spurs” to the BGE (UK) Transmission Network

In conjunction with the licence application process for distribution networks, the issue of which company will build the pipes connecting the main BGE (UK) transmission pipeline to the start of the town distribution network (the so-called “town gate” point), will need to be determined. These connecting pipes are described in the BGE (UK) licence as “spurs”.

Applicants, when detailing their proposed configuration of the pipeline systems, must clearly define the location of each “town gate” for their proposed distribution networks. Applicants should also state whether they would, if the opportunity was offered, wish to build and operate the connecting pipeline from the town gate to the BGE (UK) Transmission Network. It is possible under BGE (UK)’s conveyance licence for the Director General to request BGE (UK) to provide proposals for the construction of a spur to any town or customer(s) and to require BGE (UK) to build the spur, subject to condition 1.15.5 of their licence.

The question of whether BGE (UK) or a distribution licensee will build a spur will be decided by the Director General, in consultation with the Department, in the light of their statutory objectives (see below).

Any applicant wishing to construct and operate the spur(s) associated with their proposed distribution network should provide details on:

(a) Estimated capital and operating costs. (We are assuming that the AGI infrastructure/valves connecting any spur to the main BGE (UK) transmission pipe will be built and operated by BGE (UK)).

(b) The proposed route of the spur(s) and details of its proposed connection point to the relevant town distribution network.

(c) The proposed diameter and capacity of the spur(s)

This information should be completely separately identified within the application.

The Department has decided that, in order to help the development of as many towns as possible, the costs of construction and operation of a spur from the BGE (UK) transmission pipe to a point around 5 km from the new distribution area may be postalised (postalisation is discussed in detail below) and hence such costs will be included in the postalisation tariff calculations. This will be relevant to the overall financial viability of proposed distribution projects.

When deciding which spurs should be included within the postalised tariff the Director General and the Department will take into account the projected costs (net of any third party contribution e.g. a grant from a large energy user) and associated volumes of the spur in order to evaluate the incremental impact of that spur on the overall postalised transmission tariff. Before deciding that an individual spur should be included within the postalised tariff, the Director General and the Department will wish to satisfy themselves that the spur costs will not cause the postalised tariff to rise to an extent which would have a material adverse effect on existing gas consumers.

In the event that DETI and Ofreg agree that the cost of the spur from the BGE (UK) pipe to the 5km point is postalised, applicants should note that all costs from the 5km point on towards the towns will be included in the normal distribution cost base. For

completeness, it should also be noted that for any distribution area within 5km of the main transmission pipe, the total spur costs will be in the distribution cost base.

Where the postalisation of the cost of a spur is approved, the 5km distance will be measured from a point within the distribution area chosen by the Director General in consultation with the Department. Applicants are welcome to express their opinion on where that point should be.

Postalisation

Postalisation of gas transmission tariffs describes the situation where gas is delivered to exit points from the postalised transmission network at uniform tariffs, irrespective of the location of that exit point. Ofreg and the Department in collaboration with the relevant transmission pipe owners are working to develop and implement such a system in Northern Ireland. We envisage that postalisation of tariffs will be in place by the time of the first operation of the Northwest pipeline. DETI/Ofreg intend to issue an initial postalisation consultation document (to be available on the Ofreg web site) within the next 2-3 weeks which should give applicants more information on the proposed postalisation regime, and further information on postalisation will be placed in the public domain in the coming months as the postalisation proposals develop.

Award and Selection Criteria

In assessing applications under this invitation and granting licences, the Director General and the Department must exercise their statutory powers in the manner best calculated to fulfil the duties outlined in Article 5 of the Gas Order. These are:

- (a) To promote the development and maintenance of an efficient, economic and co-ordinated gas industry in NI; and

- (b) To secure that licence holders are able to finance the carrying out of their licensed activities.

Subject to these primary duties, the Director General and the Department are required to:

- (a) Protect the interests of consumers of gas supplied by licensees in respect of-
 - (i) the prices charged and other terms of supply;
 - (ii) the continuity of supply; and
 - (iii) the quality of the gas supply services provided (having particular regard to the interests of the chronically sick, disabled and pensioners);
- (b) Protect the interests of licence holders in respect of the prices at, and the other terms on, which any services are supplied by one licence holder to another.
- (c) Promote the efficient use of gas supplied to customers.
- (d) Protect the public against the dangers arising from the conveyance, storage, supply or use of gas.
- (e) Facilitate competition between persons whose activities consist of or include conveying, storing or supplying gas.

They must also take into account, in exercising their functions, the effect on the environment (whether by way of pollution or otherwise) of activities connected with the conveyance, storage or supply of gas.

Applicants should be aware that that these duties may be amended by the proposed Energy Order. A copy of the proposed amendments to these duties are attached in Appendix 3.

The Director General and the Department will interpret their statutory duties as requiring the applications to show clear evidence of the following:

- (a) For all licence applications:-

- (i) Probity, financial security and ability to secure required funding. This is a threshold criterion; only applicants that satisfy this will be evaluated further.
 - (ii) Relevant experience, expertise and management capability.
- (b) For conveyance licence applications:-
- (i) Firstly, viability of proposals for distribution networks.
 - (ii) Secondly, optimisation of customer coverage subject to overall proposal viability - to be assessed with reference to:
 - (a) Number of connectable customers – domestic and I&C customer forecasts to be separately identified in the applications.
 - (b) The speed of rollout of the proposed network.
 - (c) The geographic extent of the proposals.
- (c) For supply licences applications:-
- (i) Firstly, volume of gas sales
 - (ii) Evidence of an intention to contribute to the development of the natural gas market in particular developing the domestic customer base.
 - (iii) Expertise in the areas of billing and customer service.

Further Information required as part of the Applications

Applicants should provide the following information where relevant to their applications:

- (a) assumptions about take up of condensing boilers, CHP and Domestic CHP.
- (b) assumptions about rate of switching of social housing to natural gas.
- (c) a short synopsis of the environmental gains expected from developing gas opportunities in their proposed networks.
- (d) any assumptions about carbon trading and its value, if any, to their project.

Assessing the viability of any proposed distribution network

An important element of the evaluation of applications for a conveyance licence will be the assessment of the viability of applicants' proposed distribution network. As part of this assessment the Director General would like to gauge applicants' opinions on the degree to which the final distribution charges generated by their proposals would lead to an environment in which gas supplies would be attractive to potential customers of all types. Applicants should provide their views on the viability of their projects and describe the factors behind such viability. (It would be useful if applicants could model the likely final gas supply prices generated by their proposals and the degree to which these then lead to viable supply businesses). Applicants should base their views on the following assumptions:

A Swing weighted cost of gas delivered at Moffat of 18p² per therm.

A Northern Ireland Postalised tariff (gas transportation cost from Moffat to within 5kms of the town) of 5 pence per therm.

The ending of the Climate Change Levy exemption on 31 March 2006

BGE (UK) requirement to co-operate with any potential distribution operators

In their licence, BGE (UK) have a requirement to co-operate with any potential distribution operators regarding developing gas supply from their transmission network. Co-operation should include the provision of non-confidential information available to BGE (UK) that would facilitate the development of distribution networks.

Applicants are free to contact:

² These figures are in current prices.

Mr Ger Breen
C/O BGE (Northern Ireland)
3 Orchard Close
Newpark Industrial Estate
Greystone Rd, Antrim
BT4 2RZ

The application process

1. Closing date for the submission of applications: **12 noon, Friday 7th February 2003** – applicants should ensure they place a notice in the press as described in Section 6 “Manner of publishing applications” of the Gas Licence Applications Regulations and pay the appropriate fees.
2. Possible clarification meetings with applicants.
3. Selection of one or more preferred bidder.
4. Enter into detailed licence(s) negotiations with preferred bidder(s).
5. Draft licences for statutory consultation.
6. Award of licences.
7. Notify European Commission of reasons for refusing unsuccessful applications.

Standard Conditions

The standard licence conditions for conveyance and supply licences will form the basis of future licence negotiations. The Regulations seek information from companies on those standard licence conditions they wish to modify.

Rejection of Applications

The Director General and the Department reserves the right to reject from consideration as part of the current award process any application which has not been submitted in the prescribed form, does not contain the minimum stipulated information or which is shown to be false or inaccurate in any material respect.

Applications may be rejected at any time if the applicant is ineligible by reason of previous malpractice or circumstances which call into question the suitability of the applicant to be awarded a licence. Applications may also be rejected on grounds of inadequate financial standing.

Applications which satisfy the threshold criteria will then be assessed in accordance with the remaining criteria. Applications may be eliminated at the initial stage if they fail to achieve the minimum scope. One or more applicants will be selected as preferred bidders and detailed negotiation with those bidders will be taken forward.

Any unsuccessful applicant will be advised as soon as possible and informed of the basis on which their application has been rejected.

In accordance with Directive 98/305 the European Commission will be advised of the rejection of applications and the reasons after completion of the award process.

Appendix 1

Additional Available documents:

- NI 1996 Gas Order – HMSO
- BGE 2002 Conveyance Licence – Ofreg
- Gas (Applications for Licences and Extensions) Regulations 1996 – HMSO (ISBN 0-337-92407-4)
- Standard Licence Conditions - Ofreg

Appendix 3

Proposed amendments to the duties of the Director General and the Department

The principal objectives and general duties of the Department and the Authority in relation to gas.

12.-(1) The principal objective of the Department and the Authority in carrying out their respective gas functions is to promote the development and maintenance of an efficient, economic and co-ordinated gas industry in Northern Ireland.

(2) The Department and the Authority shall carry out those functions in the manner which it considers is best calculated to further the principal objective, having regard to—

- (a) the need to protect the interests of consumers of gas;
- (b) the need to secure that licence holders are able to finance the activities which are the subject of obligations imposed by or under Part II of the Gas Order or this Act;
- (c) the need to secure that the prices charged in connection with the conveyance of gas through designated pipe-lines (within the meaning of section 56) 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; and
- (d) the need to protect the interests of gas licence holders in respect of the prices at which, and the other terms on which, any services are provided by one gas licence holder to another.

(3) In performing that duty, the Department or the Authority shall have regard to the interests of—

- (a) individuals who are disabled or chronically sick;
- (b) individuals of pensionable age; and
- (c) individuals with low incomes;

but that is not to be taken as implying that regard may not be had to the interests of other descriptions of consumer.

(4) The Department and the Authority may, in carrying out any gas functions, have regard to the interests of consumers in relation to electricity.

(5) Subject to subsection (2), the Department and the Authority shall carry out their respective gas functions in the manner which it considers is best calculated—

- (a) to promote the efficient use of gas;
- (b) to protect the public from dangers arising from the conveyance, storage, supply or use of gas;
- (c) to secure a diverse and viable long-term energy supply; and
- (d) to facilitate competition between persons whose activities consist of or include storing, supplying or participating in the conveyance of gas;

and shall have regard, in carrying out those functions, to the effect on the environment of activities connected with the conveyance, storage or supply of gas.

(6) In this section "gas functions" means—

- (a) functions under Part II of the Gas Order; and
- (b) functions under this Act relating to gas.

Exceptions from the general duties

13.—(1) Section 12 does not apply in relation to functions of the Department under—

- (a) Article 40 of the Gas Order; or
- (b) section 58.

(2) Section 12 does not apply in relation to anything done by the Authority in the exercise of functions under—

- (a) Article 23(3) of the Gas Order; or

(b) section 6.

(3) The Authority may nevertheless, when exercising any function under Article 23(3) of the Gas Order, have regard to any matter in respect of which a duty is imposed by section 12 if it is a matter to which the Office of Fair Trading could have regard when exercising that function.

(4) The duties imposed by section 12 do not affect the obligation of the Authority or the Department to perform or comply with any other duty or requirement (whether arising under this Act or another statutory provision, by virtue of any Community obligation or otherwise).