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Gas Transmission
Utility Regulator
Queens House
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Implementing the European Gas Regulation (EC) 715/2009 in Northern Ireland

Dear Roisin

Mutual Energy Limited (MEL) is grateful to have the opportunity to respond to this consultation on behalf of its two wholly owned subsidiaries Premier Transmission Limited (PTL) and Belfast Gas Transmission Limited (BGT), which hold licences to convey gas granted pursuant to the Gas (NI) Order 1996.

The mutualisation of the Scotland to Northern Ireland Pipeline and the Belfast Transmission Pipeline is delivering savings to Northern Irish consumers of approximately £8m per annum on the operation of our gas pipelines in Northern Ireland. This incorporates both the cost of capital savings and the operational savings achieved under Mutual Energy's ownership.

These savings have only been made possible by obtaining 100 per cent bond debt financing of PTL and BGT at very low costs of capital. This low cost of finance has been secured by having a stable regulatory environment and successful operational model. PTL and BGT have a duty to their fund providers to ensure a continued secure regulatory environment and successful operational regime and can only support changes that will not have an adverse effect on these critical areas. The recognition that the investors in Northern Ireland infrastructure are also important stakeholders should be explicit in any project to change the regulatory environment.

General comment

Moving to a single system operator for Northern Ireland (NI) is intuitively attractive, with an inbuilt structure to reach agreement on key issues between Transmission System Operators (TSO) theoretically allowing faster implementations and ideally a single view for Northern Ireland. Notwithstanding these attractions, the setting up of these arrangements is also likely to be a time consuming process with potentially high up-front costs. The Common Arrangements for Gas (CAG) initiative was the method chosen by the two Regulatory Authorities to comply with the European Union (EU) requirements, and its hiatus since October 2011 has left Northern Ireland TSOs in limbo and non-compliant with EU requirements. Whilst it would appear logical to try to set up a new structure before implementing the widespread EU changes, the reality is that trying to do so will further delay

EU compliance and risks substantial fines on Northern Ireland that would dwarf any potential cost savings from a single TSO.

Therefore while we are fully supportive of the principles to move to a single system operator for NI at some future stage, we strongly believe that from the current starting position that the only realistic and prudent option to minimise the risk of EU fines is to allow the existing TSOs to commence and implement changes to secure full compliance with the EU Gas Regulation 715/2009 (Gas Regulation), rather than waiting for a new structure to be instituted first.

The consultation paper fails to provide timelines and project plans. As these are an important aspect of any decision, their inclusion would have been helpful for stakeholders to provide more informed and constructive responses. In the absence of timelines, our response assumes that the aim is to implement compliance as soon as possible and that all EU network code implementation deadlines are to be met.

Questions

Section 3: Moving to single system operation in NI

Have we adequately described what single system operation would deliver or are there other elements which would need to be delivered?

The consultation paper provides a sufficient description; however, considerations should be made for health and safety requirements, more specifically a clear definition of roles and responsibilities and the satisfactory discharge of these. Currently there are obligations on both asset owners and asset operators of the transmission system such as the requirement to complete and maintain a safety case. The deliverability of these obligations would need to be reviewed if a Single System Operation (SSO) was introduced.

Do you agree that, in the absence of CAG, single system operation would deliver benefits for NI over the current operational regime?

In line with the question, our answer assumes that CAG does not proceed. However, we understand that there still is a possibility that CAG will proceed and in this case creating a SSO in NI could well be a waste of time and resources.

As with all regime changes, there are potential benefits and costs. The concept of a SSO does deliver a number of benefits as detailed in the consultation paper. One of the driving forces behind the proposal is the potential to save costs on areas such as IT systems. The only quantified saving outlined in the consultation paper is an estimated £212,000 by moving to one IT system. It is important to note that changes to IT systems will depend on the outcome of Gas Regulation compliance, which may lead to very high costs. However, given the timescales and deadlines it must be recognised that a single system of operation and IT system may only be possible after costs are already incurred on two legacy systems in order to meet the EU deadlines. Given the magnitude of the proposed changes, it is important that all potential costs and savings be quantified.

The paper is less clear on the potential costs, whether they be set up costs, legal costs for new agreements, inefficiencies in splitting operations from maintenance etc. As noted above, because of the way MEL is funded, MEL delivers year on year savings for Northern Irish customers. The move to a SSO may affect investor confidence, which in the long term may lead to higher costs, eliminating the short-term cost benefits achieved in the initial setup and

streamlining. It is also worth considering that potential cost savings could be lost if NI is subject to fines for failing to implement the third package.

One of MEL's key objectives under CAG was to ensure that changes did not have a negative impact on Northern Irish consumers. In developing a SSO, consideration needs to be made over the long-term effects and assurances that there will be a focus on making sure the changes are to the benefit of NI rather than a potential steer to change operations to mirror neighbouring regimes.

Do you agree with the proposed list of system operation functions which would be delivered on a single basis in NI?

As noted above, health and safety obligations need to be considered.

Section 4: Overview of single system operation in CAG

Are there any other advantages/disadvantages of the single TSO and CJV options which we have not considered?

Single TSO

Another advantage of the single TSO is that it may be better placed to represent NI's interests, this is especially important when representatives are in discussions with neighbouring regimes over issues and changes, especially at the Moffat and Gormanston interconnection points. However, we are concerned that the length of time it will take to set up a single TSO may impede work on compliance with EU requirements. The implementation of the Capacity Allocation Mechanism network code will require changes to the rules at Moffat. These rules cover areas vital to operations in NI such as the introduction of capacity auctions, the amount of capacity available and interaction between systems. As noted above, the length of time setting up a single TSO creates the risk that NI's influence in the discussions between neighbouring regimes is restricted.

The introduction of a new single TSO may require a change in contracts that are currently in place. The impact of this needs to be assessed as to how those shippers with long-term capacity bookings will be affected.

The consultation paper identifies that the creation of a new entity would be expensive to set up because of costs such as staff and premises. These costs should be identified to determine whether they eradicate the estimated cost savings in other areas such as a single IT system.

Contractual Joint Venture

As ACER and ENTSOG continue their progress in implementing the third package, the NI TSOs and industry will be under considerable pressure to deliver the required changes in a relatively short time period. If a Contractual Joint Venture (CJV) were to be successfully created, the shorter time scale in setup in comparison to the setting up a new entity would be advantageous in delivering the new structure to then implement further changes to achieve full compliance with the EU requirements. The key to delivering the benefits associated with a CJV is ensuring that an effective, efficient and representative structure is agreed upon from the outset. The CJV would need to represent the interests of the three TSOs with a unified focus on delivering benefits for the NI gas market and stakeholders.

Do you agree with the criteria proposed to assess the options for single system operation?

Given the significance and impact of the proposed changes, MEL believes that the assessment criteria should be expanded. There are clear timelines and deadlines identified in relation to the EU network codes therefore the speed to implement the proposed options should be assessed. Consideration also needs to be made as to how the options would interfere with other IME3 implementation activities. As noted above, the development of a SSO may have an impact on investor confidence. The impact on financing must be considered it may lead to higher costs in the long term.

Do you agree with the assessment of the single system operation models against the criteria?

Under the cost effective section, the paper refers to the costs of co-ordination between multiple TSOs. To assess the two options fully, it would be useful for the Utility Regulator (UR) to quantify these costs. The creation of a single TSO will be licenced and regulated by UR allowing UR to control its costs. Presumably, this will be in the form of a price control. The impact of this on MEL's funding needs to be assessed to ensure that MEL can continue to deliver significant savings to NI consumers as noted above. Any negative impact could result in the Single TSO option becoming more expensive in the end.

Which options for single system operation in NI do you prefer and why?

MEL strongly believes that the co-operation approach should not be dismissed. There are a number of advantages to this approach and with some changes to the current regime; further improvements could be made in terms of efficiency and deliverability both in an EU and NI customer context.

With a co-operation approach, it is still possible to deliver a single code and IT system. An example of this is the German model, where fourteen TSOs operate within two entry/exit zones. The individual TSOs retain operation of their own transmission systems but they share the same network code known as the General Terms and Conditions. The TSOs are all party to the Cooperation Agreement, a contractual agreement which enables them to work together to deliver a single network code. With regard to systems, the German TSOs use their own systems however; they are based on a common platform. Given the amount of changes required, the utilisation of Gas Regulation compliant capacity and nominations systems that are already in use and have been market tested may be more efficient and cost effective than designing a single all-encompassing system.

An approach similar to the German model will deliver Gas Regulation compliance in a more timely fashion than effectively starting from scratch and introducing a SSO.

NI TSOs have a positive history of working together with UR direction and oversight. For instance, in 2004 to deliver the postalised system and in 2007 to rationalise the NI codes and deliver a single balancing zone. Considering the fact that the current arrangements are between three transmission TSOs and service two Distribution Network Operators and two power generators, it should not be underestimated how homogenous the current arrangements are to shippers and how little marginal effort and co-operation could deliver many of the aspirations of the paper.

TSOs to include any further thoughts they may have on their CJV models in the NI only context.

The TSOs believe that the focus for the EC715 implementation project in NI should be on developing arrangements for EU Gas Regulation EC715/2009 compliance as a priority. To this end, following the recent EU stakeholders' workshop the NI TSOs have jointly established a working group to review compliance work streams to implement the requirements of Gas Regulation EC 715/2009. The initial output of this working group will be the development of proposed high-level principles/objectives for the project as well as development of a basis of determining a structured work program/project milestones for discussion with NIAUR and industry. The NI TSOs will continue work on this process whilst keeping the Utility Regulator informed.

With regard to the CJV, the NI TSOs under CAG were of the view that the CJV was the preference for single system operation and propose to review the work done under CAG in an NI only context under the joint working group.

MEL gave a lot of consideration to the optimum structure of a CJV as part of CAG. In this project, MEL proposed a structure whereby Bord Gáis Éireann and MEL would come together at a corporate level to form a governing committee through which each TSO would deliver its operational responsibilities. Consequently, the governing committee would control / manage a common pool of staff and other resources supplied, where efficient to do so from the respective TSOs but with the objective of delivering the SSO functions to the committee and not the respective TSOs. To ensure parity for the TSOs and to a single view to Shippers and industry an absolute fundamental of this structure would have need to be full management control on behalf of all TSOs. An individual TSO's delivery of any of the SSO functions would be via the joint governing committee. There would at least need to be a dedicated General Manager (and perhaps a small executive team) to act on behalf of the governing committee on a day to day basis but MEL would be content that other staff in the structure could, if required, also carry out asset management roles for their employing TSO provided that for their SSO functions role they are directed by and report only to a line of management ending at the governing committee – not within the respective TSO.

Our preliminary view is that as the CJV is no longer to be considered in an all island context, the CJV staff and office should be based in NI. However to deliver cost savings, the operation of the control room should be tendered, which may result in the most appropriate counterparty being based outside of NI. This view may be amended as a result of on-going discussions with BGE (NI) if a better structure can be identified.

An NI Single System Operator would have very different TSO interfaces than the previously proposed all-island Single System Operator. Namely, the NI Single System Operator would interface with BGE and BGE (UK) as well as to a much less extent National Grid whereas the proposed all-island Single System Operator only interface would have been with National Grid. This is a very important difference between the CAG proposal and the NI Single System Operator proposal and would most likely mean structural differences in the setup of any CJV so that there would be effective representation for NI shippers and customers at NI interfaces with neighbouring systems.

Do you agree with our proposal to implement a single transmission code of operations and a single IT system in NI?

MEL and BGE (NI) currently work closely together to develop streamlined network codes. MEL is supportive of building upon the work already carried out and developing a single network code. Although some of the work on the CAG process could be reused, there will be

a number of differences, notably the alignment with upstream arrangements contained in the Transportation Agreement. The consultation paper lists a number of benefits of a single network code for UR, the TSOs and most importantly the customer.

MEL believes that to deliver Gas Regulation compliance, the starting point should be the development of a single code. We anticipate that the development of a single transmission code of operations would be a lengthy process and require significant resources from the TSOs and UR. The development of the code will require significant input from the wider industry, similar to the CAG process during summer 2011. Given the small size and limited resources of a number of regulated businesses within the market, the development will put pressure on market participants. This process could further exacerbate that issue if UR decides to implement the SSO as well as the single code and IT system.

The next stage after developing a single code should be the introduction of a single or common IT system(s). With a code in place, it will provide the basis for development of the IT system. The TSOs use different IT systems for nominations on their networks, meaning shippers who use both networks have to incorporate the differences in their training and procedures. A single IT system would be appropriate in a regime where a fully functioning Gas Regulation compliant SSO was in place, however given that the development of a SSO will take a number of years to properly implement it may be more appropriate for the TSOs to focus on using a common IT platform, rather than one IT system. As mentioned above, this is what takes place in Germany and works effectively. The development of, or even the use of an existing platform such as those used in continental Europe would be an improvement over the current situation.

Section 5: Gas Regulation compliance proposed scope of work

Are there any other services not mentioned which suppliers require?

The consultation adequately describes the services.

Do you agree with how we propose to tie in the development of the single code with the EU network code process?

MEL strongly believes that in developing a single code, it is important to consider the current regime but also to incorporate EU requirements from the outset if feasible. Even though there are a number of codes still to be developed and finalised, the EU directive, ACER Framework Guidelines and ENSTOG draft codes provide guidance on the changes required. Where possible, proposed changes with a high possibility of implementation should be considered when developing the single code. Given the significant changes, which will be made to the NI market over the next few years and the resources required, it would be advisable to incorporate changes as part of the initial work stream rather than duplicating efforts a few years down the line. It is important when developing a code for NI that the assumption should not be made that NI will automatically adopt and adapt a neighbouring regime's network code. Other options such as adapting the current codes and developing a brand new code should also be considered.

Conclusion

MEL welcomes UR's focus on delivering compliance third package compliance and looks forward to working with UR and BGE (NI) to deliver it. However, MEL has concerns over the introduction of single system operation. The primary concern is the length of time it will take to make such substantial changes to the NI market. NI's Gas Regulation compliance has been considerably delayed by the reliance on the CAG project to deliver the required

changes. To avoid infringements MEL believes that the focus needs to be on what can realistically be achieved and will deliver compliance. Therefore, the emphasis should be on achieving compliance on time with existing systems unless there is certainty that a single code and system can be implemented in time. The delivery of a single code and common IT system or systems should follow in a way designed to meet the longer dated EU compliance deadlines. Finally, after these have been delivered, and then if required, the focus could turn to the single operation of the systems. As noted above, the co-operation approach adopted in Germany should be considered as a method to deliver what is required for Gas Regulation compliance within a realistic and achievable timescale.

Should you wish to discuss any aspect of our response please do not hesitate to contact me.

Yours sincerely



Stephen English
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