4 October 2002

Elaine Wallace
Commission for Energy Regulation
Plaza House,
Belgard Road,
Tallagh,
Dublin 24

Re: CER 02117 Gas Market Arrangement Principles

Dear Elaine,

I would like to take the opportunity to comment on your recent paper on the Structure of the Irish Gas Market. Aughinish Alumina supports the CER's initiative of reviewing the principles and structures of the Irish gas market with a view to introducing improved competition, pricing and ultimately benefiting the competitiveness of Irish industry.

3.0 Gas Capacity

We believe that there is little advantage in developing the point to point trading system especially if the development of secondary trading is considered important. Because of the small size of the Irish market, development of point to point could lead to virtually no secondary trading. We encourage the CER to consider an entry/exit system.

We support the introduction of a short-term capacity sales mechanism, as it will help reduce inefficient capacity allocation.

Contract carriage is not itself a barrier to small players if other players are encouraged into the market, i.e. buy capacity long term then sell annually. However, to attract new players into the market, it is essential that the capacity pricing mechanism is stable, i.e. linked to investment costs, and not moving to auction prices as in the UK. We believe that CER should make a binding commitment not to introduce auctions over say the next 10-15 years.

We agree that all capacity trading should be bilateral, and that the Transporter should merely facilitate. Sales should be for up to as long as the capacity is held for.

4. Transportation Services

We believe that the proposals make sense for capacity holders. Sales of shorter-term unsold capacity are efficient, and we agree that a modest premium should be applied to encourage 12 month booking. However, CER should be very precise upfront as to the permitted range of premium, e.g. 10-50%. We understand that in the UK market, this premium would swing about greatly following a series of overlapping modifications, and can lead to a lot of uncertainty and confusion.

Interruptible sales are also efficient, and we agree that a fixed percentage of firm capacity should be booked first to prevent a flight from firm. However, the same point as above on defining the range of the firm percentages sold.

We agree the price floor for interruptible is the short run marginal cost, however an auction is probably the best way to price it on the day, rather than estimating fixed premia.

The relationship between short-term firm and interruptible sales needs more consideration. For example, in summer, why would any one buy monthly firm at say a 20% premium, if they could buy interruptible in the day ahead auction at a 50% discount to firm? At that price difference, most would take on the unlikely risk of interruption.

On overruns, we agree that a penalty for unauthorised overruns is required. Again, we understand that this was an area that constantly changed in the UK due to modifications, and was very uncertain. The CER should commit to a stable overrun premium for a number of years.

We disagree with the authorised overrun suggestion and believe it is confusing and unnecessary. If a party knows they will overrun in advance, they should trade secondary, or buy short-term firm or interruptible. As CER itself says, authorised overruns will discourage secondary trading, which is really more important to capacity holders in obtaining value. We strongly oppose the suggestion of authorised overruns.

We support overrun trading (i.e. retro trading) as this again supports the value of holding capacity. We are not sure of the logic of preventing retro trading on critical days, as by definition firm capacity rights were available for all the gas that flowed.

5. Nominations and Balancing

5.1 With reference to allowing retro trading of energy imbalances - this may be efficient if there are a small number of players, but in a bid market of say 20 players, the resource input to retro trading is very high for the volume being traded, i.e. 1-2% of system demand. At this point, it may be better to prohibit retro trading, and let the companies get the benefit of the neutrality payment.

However, we fully support participants being allowed to pre-trade gas without Transporters clearance.

5.3 The current nomination process does not permit within day renominations, and this should at least be permitted if matching downward “renoms” are made at entry and exit, as there will be no effect on the system.

5.4 We strongly support daily balancing and do not think that shorter balancing periods make sense, even if the UK goes that way. If arbitrage opens up because of the two different balancing periods, an ancillary service type storage contract should be available to the Transporter to deal with any diurnal variation, with the costs spread across all users in proportion to volume used.

5.5 The rolling imbalance tolerance regime seems fine, though again we strongly encourage the CER to commit to stability on the numbers, and not keep changing them year after year.

5.7 We have doubts that the additional mechanism for securing cash for system security can be cost effective at present, due to lack of potential liquidity. CER should produce a cost/benefit analysis for establishing this mechanism.

5.8 If there are pre-determined cash out prices, arbitrage will open up with the UK OCM prices. Some players (i.e. UK shippers) will be better placed to play this game. Why not just make all imbalance cash out the UK cash out prices, perhaps with a very wide cap and floor?

5.9. We agree that shippers should pick up **all** neutrality payments. The Transporter incentives to reduce over all balancing charges should be a separate mechanism, which is capped and floored.

5.10 Scheduling charges are an administrative and IT burden, the energy balancing penalties should give sufficient incentive to nominate properly. Consistent poor nomination performance should be dealt under compliance with the code, and the threat to withdraw the licence if nomination performance does not improve.

6. Shrinkage Gas / Line-Pack

In general, the idea that shippers inject additional gas to cover shrinkage is good, as it avoids the Transporter having to buy gas. However, there may be a difficulty if the percentage of additional gas is a forecast, if each shipper is not moving constant volumes each year, i.e. if reconciliation is performed on the following years percentage, a shipper may lose out.

To get around this, we could suggest that following the year-end, a reconciliation amount (therms) is calculated for each shipper, and this is applied to its shrinkage account in the following year.

We should also point out that a disproportionate amount of shrinkage comes from the low-pressure tiers, i.e. that is where most of the theft/leakage occurs. There is virtually no loss on the high-pressure (70 bar) system, only compressor usage. In the UK, we understand, there were always problems in allocating the shrinkage between pressure tiers, (i.e. business versus domestic), that may have led to business subsidising domestic. Could we suggest that customers on the high-pressure system are only charged for compressor/heating usage and metering errors, with all other cost applied to low-pressure tiers? If this is not accepted, the Transporter should be very transparent in how it allocates one shrinkage factor to high-pressure customers, and a higher number to low pressure customers.

Finally, we support as much transparency and availability of information on shrinkage as possible, and appropriate incentives for the Transporter to improve year on year.

On linepack, not allocating a proportion to each shipper means that the Transporter has more flexibility (or safety margin), which may not get used as efficiently. Over the longer term, we support allocating each shipper individual linepack, combined with removal of tolerances, i.e. each shipper will have an individual, variable tolerance which they manage efficiently. However, the value in the short term of this suggestion is not large.

Once again, we would like to thank you for the opportunity to comment on the consultation document and apologies for the delay in getting our submission to you.

If you have any questions on this submission please do not hesitate to contact me,

Yours sincerely,

John Ryan
Aughinish Alumina Ltd