

## Viridian Energy Limited

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Jill Murray  
Commission for Energy Regulation  
Plaza Hotel  
Tallaght  
Dublin 24.

**Ref: Comments on CER consultation titled “Implications for Ireland of the Planned Reforms of UK Gas Transmission Exit Regime” – CER document ref. CER/06/222 dated 20<sup>th</sup> October 2006.**

Dear Jill,

Please find below Viridians comments in relation to the above referenced document.

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### **SUMMARY:**

- Viridian supports the idea of a Single Party (SP) booking Flat and Flex capacity for the 3 jurisdictions downstream of Moffat as long as very strict rules about how this is achieved and costed are agreed by industry in advance.
- Viridian does not believe BGN are the only party who can act as the SP and ask CER to investigate other possibilities.
- Viridian does not believe the Moffat Agents role should be amended.
- Viridian supports the idea of booking all available Flat capacity at Moffat (a variation of the Option D approach)
- Stringent rules need to be drafted to deal with how Flex capacity is booked, used and paid for.
- Clear rules need to be drafted to fairly deal with the difference between what is actually used in terms of flat capacity and what is actually booked by the SP.
- Clear rules need to be devised as to how Medium or Short Term flat capacity is bid for in the pay-as-bid auction, and how flex capacity is bid for in the pay-as-bid auctions. This is especially needed if the SP is to perform these roles, and yet needs to take account of the different “value” parties will place on the products.
- **Shippers downstream of Moffat need to be assured they have Prevailing Rights for the capacity they have historically booked.**

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### **(1) Comments:**

#### **(i): The question of a Single Party (SP):**

The CER consultation paper appears to vastly simplify the whole issue of the UK Exit Reform and appears to propose that the solution is one of simply appointing a Single Party to perform a certain task for the 3 jurisdictions downstream of Moffat. The question of deciding whether the idea of a

single party (SP) is a good idea or not is vastly more complex than simply one of looking at how an SP would book firm capacity - which is basically the only issue either Option A or Option B would address.

What Option A and Option B essentially achieve is a mechanism by which the three jurisdictions downstream of Moffat can in most situations meet their “security of supply” requirements. However caution is advised on this notion in that it must be realized that supply is only secure if gas is off-taken at a flat consistent rate - it does not deal with the situation where one of these jurisdictions suddenly drops or increases load so that the gas offtake is not flat over the day – in this event security of supply is not guaranteed by either Option A or Option B as non-flat gas flows are dependent on the amount of flex capacity purchased.

The whole issue of security of supply and the UK Exit Reform are highly complicated by the need to book flex capacity, and as has been stated above this issue has not been mentioned in the consultation paper but which will not be resolved by either of Option A or Option B. Given this fact Shippers are not sufficiently informed on the topic so as to allow them to make informed comments in response to this consultation. It is extremely difficult for Shippers to provide a concrete response with so much of the necessary detail unknown. The fact is that it appears the unit cost of booking flex capacity, and the unit cost of using flex capacity, will be many times higher than the unit cost of booking or using flat capacity. As such it is the issue of flex capacity which from an economic point of view is the more important issue compared to flat capacity and yet no discussion has taken place in this regard and further the final date for comments on this issue is essentially the 24<sup>th</sup> November 2006 after which time it will be a “done deal” so to speak and the three jurisdictions will have to live with something they have not discussed between themselves yet and which then cannot be changed by Ofgem regardless of the arguments made as to the unique nature of Moffat. This said Viridian feels obliged to comment on the paper as drafted in the hope it assists the decision making process.

It is Viridians view the if a Single Party is responsible for booking FLEX CAPACITY then logic would suggest that this would minimize the economic burden on the 3 jurisdictions in relation to FLEX CAPACITY by;

- (a) eliminating or dramatically reducing the possibility of overbooking Flex capacity which is a real possibility if parties are left to book flex capacity themselves (assuming a prudent approach is taken);
- (b) eliminating the need for all shippers to invest in software systems to forecast and/or track the flex capacity usage at each of their individual sites;
- (c) minimizing the actual usage of Flex Capacity on each day by virtue of the fact that a Single Party could aggregate all gas flow nominations and devise a profile while will minimize or eliminate the usage of flex capacity on the day.

Due to the above Viridian is of the opinion that in order to limit the economic burden on gas consumers and limit the burden on shippers (assuming that extra burden will be reflected in extra costs to consumers) which is understood to be a major desire for all 3 jurisdictions downstream of Moffat, they appear to have no alternative but to appoint a Single Party to book and manage the usage of flex capacity.

The above shows that a Single Party is needed to deal with the flex capacity issue and thus it naturally follows that logically this party may as well act as envisaged under Option A for dealing with FLAT CAPACITY for the 3 jurisdictions. It therefore appears unreasonable to continue to consider Option B. This view is supported by the fact that NGG Transco has stated publicly that Option B is not workable for them – they would only consider this if Ofgem were to place an obligation on them to do so and Ofgem are not minded to do this at this time.

Another benefit of the Single Party approach is that it prevents unnecessary double booking of NTS Exit Capacity. If the booking of capacity was left to Shippers to do themselves then a particular problem may well arise in the retail gas market (non-wholesale). If Shipper A has booked 12 months worth of capacity for Customer X and the customer decides to switch supplier to Shipper B during the 12 months then for certain periods there is the real possibility that Shipper A and Shipper B will have both booked the same level of capacity for the same customer, thereby double-booking the capacity. This is economically not efficient and gives a very misleading indication to NGG Transco as to the level of capacity and thus investment needed at Moffat. By a Single Party performing the bookings the correct level of capacity can be booked such capacity can be transferred between Shippers when customers move Shipper/Supplier.

Viridian is concerned however to ensure that the CER does not underestimate the complexity of the work, or the considerable economic responsibility attached to, the role of the SP in relation to booking and using of both flat capacity and flex capacity. It is due to this complexity and economic responsibility that Viridian believes the Moffat Agency model as it currently exists will not work for the SP. Today the Moffat Agent performs purely mechanical activities with not commercial decision making involved. The SP would be expected to use its judgement in booking the capacities and also every day determining the usage of flex capacity – this is a vastly different role to the current Moffat Agency. Also it must be remembered that the Moffat Agent was appointed by Irish and UK Shippers solely to perform nomination matching and not by any other authority. Thus if the Moffat Agents role is to change Shippers who appointed the agent would need to agree to appoint such an entity to perform the envisaged role.

There may be a need for the Moffat Agent to continue to perform the roles it performs today but Viridian believes the SP should be a separate appointment which should be separate from the Moffat Agent, and BGN in its role as Irish Transporter. A detailed appointment contract will need to be agreed for the appointment of the SP detailing the strict regime under which it must operate and the manner in which it will make decisions with the main focus on minimizing costs to all users in the 3 jurisdictions. Concluding this contract is expected to be a long and complex process.

**(ii) Who will be the Single Party (SP):**

The CER has to date continually suggested that the SP would be Bord Gais Networks (BGN). While there may be some logic in this as they are the party with the most knowledge of the system downstream of Moffat, the fact is

- (a) BGN are a Transporter – they are not a UK NTS Shipper or Distribution Network Operator (DNO) – to become either would it is understood involve a complex process necessitating a change in its license and approval from the Irish Government. This is likely to take some time to achieve.
- (b) even if BGN did manage to get (a) above completed they would then need to go through the process of getting an exemption from UK DTI from the Ofgem Licensing process (to get a license). They would also need to agree with NGG Transco as to how it could “act” as a UK Shipper/DNO as so enable it to book Flat and Flex capacities. This is likely to take some time to achieve.
- (c) Bord Gais is still a monopoly provider in Ireland due to the fact that the supply arm of BGE is still a part of the same legal entity as BGN with the same board of directors, etc. The information the SP would have to deal with is likely to be highly commercially sensitive in nature and thus one may have legitimate concern in this regard if one was to consider appointing BGN to the role. The SP role should be managed by a party whom all Shippers and users in the 3 jurisdictions are certain has no commercial interest whatsoever in the gas supply activity.

Given that the SP must be in place at some appropriate time in advance of July 2007 to allow it time to ready itself to act as the SP in July 2007 it is appears highly unlikely (a) and (b) above would be completed by then even if there was some mechanism to ensure shippers/suppliers are comfortable in relation to (c) (which may not be the case). Hence Viridian questions if it is in fact reasonable to continue to consider BGN for the role of SP as currently envisaged given this time constraint?

Due to the above Viridian would ask the CER to seriously consider the suggestion of appointing an SP who might be an independent third party, who is also a UK Shipper/DNO or can act as either (depending on which the SP is required to be) who is appointed through a tendering process to perform the role of the SP as envisaged heretofore and who gets remunerated appropriated as per the tender process "bid". This party could book the Flat and Flex capacity as instructed by the appointer (who could be the CER or some other party). Then on a daily basis the SP could receive aggregate nomination information from the Moffat Agent from which the SP would generate a profile which would minimize the usage of flex capacity on the day (this could be seen as a variation of the OPN Agents role as performed by BGE (UK) today). This party could have in its contract (A) a stated overriding obligation to minimize costs and if it fails to do so its appointment could be terminated with certain notice or (B) details rewarding the SP for reducing the usage of flex and penalizing the SP for increasing the usage of flex (the latter is only likely to be possible after experience if the UK Exit Reform where a better understanding of the proper manner of setting the incentives and penalties would be possible). While the party appointed to the role of SP should ideally have no existing interests in gas shipping in ROI, NI or IoM, due to the fact he will be getting aggregated gas usage information there should not be a conflict here if the party did have existing shipping interests and so it could in theory be any UK NTS Shipper.

**(ii) If demand does not match booking:**

In either of Option A or B it is unlikely the booking made by the SP will exactly match the demand. An overbooking can occur if parties put prudent estimates in their response to the Joint Capacity Statement, and actually turn out to need less. Also an overbooking can occur if load growth forecasts are overly optimistic for domestic users or if customers go out of business or switch fuel. An underbooking can occur if parties are not prudent in their responses to the Joint Capacity Statement or if load growth for domestics exceeds expectations, or new I&C loads come in in the medium term. How will the jurisdictions deal with these variations?

Viridian believes it is too simple to just suggest a smearing over all customer usage. A more fair mechanism should be devised to more accurately reflect the extent to which a party has caused the under or over booking bearing in mind if the party are no longer in business then the cost will then have to be smeared.

**(iii) Booking Capacity in the Pay-As-Bid Auctions (Medium and Short Term Flat Capacity and Flex Capacity)**

To book Medium Term (1-3 years) Flat Capacity or Short Term (less than 1 year) Flat capacity (assuming in both the former cases there is not sufficient Flat capacity booked in the Long term (over 4 years) auctions), or Flex Capacity, the party wishing to reserve such products must participate in a Pay-As-Bid Auction. There are two options here (1) allow all Shippers to participate in the Pay-As-Bid Auctions by themselves or (2) the SP participates on behalf of the Shippers. Obviously with the Long term Flat Capacity booking, and the usage of flex capacity being decided by the SP (assuming Option A is chosen) it appears foolish to opt for Option (1) above, and thus the SP should be the party involved in the Pay-As-Bid auctions.

The question arises how does one decide at what level the SP should bid in these auctions given that different shippers will value the different capacities more or less than other shippers?

Viridian does not believe there is a simple solution to this and further believes there has not been sufficient consultation or debate on such issues. However one possible solution is for Shippers to send their bids to the SP who replicates the volumes and prices in the auctions and then whichever shippers are successful then so be it. The benefit of this approach is that the different volumes required by shippers and the various prices the shippers are willing to pay would be reflected in the actual auction. Further by the mechanism the SP could not be blamed for making bad decisions.

**(iv) Option C:**

Viridian does not accept that Option C is a real Option as to do nothing and hope for the best (which is what Option C appears to advocate) would be highly foolhardy and will very likely prove very costly. Hence Viridian does not support Option C.

**(v) Option D:**

The CER will be aware that an Option D was proposed by Ofreg as part of its consultation process on the UK Exit Reform. Viridian believes there is great merit in an extension of one of the ideas raised in this Option D and this is to propose the 3 jurisdictions book all the available capacity at Moffat and continue to do this on an on-going basis. The cost of doing this is small (less than £160,000) in relative terms but the benefits are huge

- (a) capacity hoarding is prevented
- (b) capacity switching/transfer/substitution away from Moffat is not possible
- (c) security of supply is more likely to be achieved
- (d) simplicity – there is no need to get the figure exact or match it exactly with the Joint Capacity Statement (just ensure what is booked exceed the JCC figures)

**(vi) NTS Capacity:**

If the SP is to book Flat and Flex capacity, the process by which the capacity is transferred from the SP to the relevant Shipper or to the relevant Shippers NTS counterparty needs to be fully understood.

**(vii) Prevailing Rights:**

Ofgem have confirmed that shippers downstream of Moffat who historically have used a UK NTS Counter-party shipper to book NTS capacity on its behalf will NOT have any “Prevailing Rights” as defined under the Exit Reform regime. This is a huge concern for most such Shippers as to book capacity they will be liable for a minimum of 4 years of charges 7 years in advance whereas if they had Prevailing Rights they would only be liable for 18 months of charges in advance. Viridian would ask the CER to pursue this issue to check if Ofgem would allow Shippers downstream of Moffat to have Prevailing Rights if they can prove they have used the ticket-to-ride certificates historically to allow their counterparty UK shipper to book Moffat NTS capacity on their behalf.

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**(2) Minor Points:**

(A) **Section 1 - Tailoring:** While Ofgem have moved from a position of not taking into account, or listening seriously to, comments from shippers and/or regulators downstream of Moffat Viridian believes it is not true to say that Ofgem has “*been quite open to tailoring the planned reform arrangements to accommodate*” “*the special role of Moffat*”. They have participated in the process of meeting with, and listening to, such parties to ensure they cannot be accused of not listening and taking all views into account BUT it must be recognized that not one single item of the proposed Exit Reform has been amended to “suit” Moffat or its unique nature – proposing a Single Party at Moffat to act as a pseudo DN Operator is simply a device to force the Exit Reform to work downstream of Moffat. Further Viridian does not believe any shipper in Ireland, Northern Ireland or Isle of Man, or it is understood any regulator in any of these jurisdictions, want the Flex Capacity product due to the highly complex nature of it, the potential risks and cost involved, and the costs of implementing and administering such a

regime which is a form of hourly balancing of sorts. Thus Viridian would suggest CER should not give Ofgem more recognition than they deserve.

- (B) **Section 1 – Schedule Date:** Viridian would like to clarify to the CER that the proposed Exit Reform will actually begin its processes from July 2007 (earlier than the date in the paper of Oct 2007) BUT will be effective only from October 2010. The CER have corrected this point slightly in Section 2.3 paragraph 1. The period from now until Sept 2008 is known as the Interim Period and the period from Oct 2008 to Sept 2010 is known as the Transitional Period – there are separate arrangements for both of these periods.
- (C) **Section 2.2 – 3<sup>rd</sup> paragraph –**
  - a. the comment “zonal maxima of 4.6 mcm” should have been attributed to the zone in which Moffat will operate. As drafted it appears the zonal maxima for all 17 zones are all 4.6 mcm.
  - b. In addition to the annual pay-as-bid auctions NGG Transco will auction Flow flex on a day ahead basis for any unsold flow flex or any additional available on the day.
- (D) **Section 2.3 – paragraph 2 –**
  - a. the Moffat Agent does not match capacity bookings upstream and downstream – the wording included here implies he does. The Moffat Agent Matches NOMINATIONS upstream and downstream of Moffat. If there is a Mismatch the Moffat Agent advises the Shippers upstream and downstream – he does not advise the Transporter. It is the Ticket-to-ride principle ensures capacity booking matching upstream and downstream of Moffat, and the Moffat Agent is not involved in this.
  - b. “*Only Shippers who have a counter-party on the downstream capacity register may acquire firm, long-term NTS exit capacity at Moffat*” should read “*Only UK NTS Shippers ..... Moffat*”.
- (E) **Section 2.3 – paragraph 3 –** Viridian does not believe that the “Moffat IT system” is called “Gemini”. Viridian understands the Moffat IT System is the Moffat version of the GTMS and that “Gemini” was the replacement system to the old “AT Link” used by NGG Transco Shippers for Nominations to the UK NTS system.

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Should the Commission have any queries in relation to the issues raised in this paper Viridian would be happy to answer any queries or meet with the Commission to explain its thoughts.

Yours sincerely,

*Derek Russell*

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