



Commission for Energy Regulation

An Coimisiún um Rialáil Fuinnimh

Proposed Operating Agreement between BGÉ and Gaslink

Consultation Paper

CER/08/072

25th April, 2008

Operating Agreement between Gaslink and Bord Gáis Éireann

The Commission for Energy Regulation “the Commission” is today publishing and inviting comments on the Operating Agreement reached between BGÉ and its newly established subsidiary company, Gaslink, which the companies have submitted to the Commission for approval. The Operating Agreement is designed to enable Gaslink discharge the functions of independent transmission and distribution system operators as provided for in Directive 2003/55/EC

Background

The legal and *de facto* independence of the system operator is a key principle of EU liberalisation of both the electricity and gas industries. This principle applies to both the transmission and distribution networks.

It does not mean that the system need necessarily be *owned* by the system operator. This is evidenced in Ireland, for example, where EirGrid is the operator of the electricity transmission system but not the owner. The principle does mean, however, that where the system is owned by an incumbent player who also trades in a related contestable market - e.g. gas supply – the system operator function is discharged by a distinct legal entity (such as a subsidiary undertaking) who “shall be independent at least in terms of its legal form, organisation and decision making” from other activities not relating to system operation.

In Ireland’s case **Directive 2003/55/EC** has been transposed into domestic law by **S.I. No. 760 of 2005** as amended by **S.I. 377 of 2007**. These Regulations provide, among other things, that

- BGÉ shall establish an independent subsidiary company (Gaslink) to discharge the functions of TSO and DSO in a manner consistent with the 2003 Directive and the Minister will approve the memorandum and articles of association of Gaslink.
- BGÉ, as owner, and Gaslink, as operator, shall negotiate and enter into an **Operating Agreement** providing for the terms on which each will fulfill its respective functions regarding the BGE transportation system (i.e. the transmission and distribution networks). This Operating Agreement will then be submitted to the Commission for approval.
- BGÉ and Gaslink shall separately prepare and submit to the Minister for approval a **Transfer Plan** covering assets, rights and liabilities and employees as are necessary to enable Gaslink to discharge its responsibilities.

Since these Regulations were made, Gaslink has been established and the Minister has approved its memorandum and articles of association. The two companies have negotiated and agreed an Operating Agreement and submitted it to the Commission for approval. This is the subject to the present consultation exercise. A Transfer Plan is also being currently considered by the Minister.

In considering the request to approve the Operating Agreement, the key questions for the Commission are (i) whether the Agreement is compatible with the letter and the spirit of the Regulations and (ii) whether it provides the basis for an efficient and sustainable relationship between the two companies for discharging their obligations and meeting the needs of the Irish gas industry in the coming years.

The Respective Functions of System Operator and Owner

The core provisions in the Regulations on the respective functions of Gaslink and its parent BGÉ can be summarised as follows for the present purpose:

Regulation 11 provides that responsibility for the operation of the BGÉ transportation system is vested in Gaslink, who shall operate that system in a manner consistent with Article 8 of the Directive 2003/55/EC. That responsibility includes (but is not limited to) identifying works necessary for the effective operation of the BGÉ transportation system. As soon as practicable after identifying works necessary for the effective operation of the BGÉ transportation system, Gaslink shall give directions to BGÉ with respect to carrying out those works. BGÉ shall take all practicable steps to ensure that these directions are complied with by the date, or within the period, specified in those directions or by such later date as Gaslink may allow.

Regulation 12 provides that Gaslink is declared to be independent of BGÉ as regards its organisation and its power to make decisions with respect to carrying out its responsibility for operating the BGÉ Transportation System and that Gaslink is entitled to make decisions, independently of BGÉ, for the operation, maintenance and development of the BGÉ Transportation System. It also provides that BGÉ shall not engage in any conduct that interferes with or is likely to prejudice Gaslink as regards its responsibility for the day-to-day operation, maintenance and development of the BGÉ Transportation System nor make any decision about the construction or improvement of the BGÉ Transportation System that is within the ambit of the annual plan prepared or approved by BGÉ.

Regulation 12 further provides that nothing in that Regulation affects the right of BGÉ to take appropriate steps to ensure the protection of the economic and management supervision rights of BGÉ with respect to securing a return on assets, whether owned by BGÉ or Gaslink. It also allows BGÉ to require that Gaslink complies with an annual financial plan prepared or approved by BGÉ for the purposes of the Regulations and to impose global limits on the amount of debt that Gaslink may incur at any specified time or during any specified period.

Some General Points to Bear in Mind

In considering making submissions on the Operating Agreement, interested parties should bear the following general points in mind.

Firstly, it is clear from the arrangements described in the Agreement that many of the functions to be discharged by BGE in its capacity as licensed owner of the systems will, in practice, be discharged by BG Networks which will continue to act as a separate division within BGE whose staff will be bound by strict ring fencing licence rules regarding non-disclosure of information etc. Examples of such functions include carrying out Gaslink's Development Programme, managing all contracts with subcontractors etc.

Secondly, the inclusion of BGE (UK) limited as a proposed party to the Operating Agreement arises from certain technical legal questions relating to the ownership of BGE Interconnector System. It does *not* affect the essential relationship and separation of functions between Gaslink and BGE as embodied in the Agreement. Comments on this aspect of the Operating Agreement are *not* being sought by the Commission.

Thirdly, the Commission will shortly be circulating revised draft transmission and distribution operator and owner licences for Gaslink and BGE respectively as part of a separate public consultation exercise. This is required by the Regulations. We envisage that these licences will confine themselves to providing that, with regard to the Operating Agreement, the parties shall comply with its terms. In other words, it is not envisaged that the licence consultation exercise will affect the outcome of the current consultation exercise on the terms of the Operating Agreement itself.

Consultation on Proposed Agreement

The proposed Operating Agreement issued jointly by BGE & Gaslink is included as a separate document CER/08/073 accompanying this paper.

The Commission welcomes comments from interested parties on this proposed operating agreement. Please submit all comments, preferably in electronic format to John Melvin (jmelvin@cer.ie) by close of business on Friday 23rd May 2008.