15th July 2013

Mr James McSherry
Commission for Energy Regulation
The Exchange
Belgard Square North
Tallaght
Dublin 24

Re: Access Tariffs and Financing the Gas Transmission System CER/13/122

Dear Sir,

It is very disappointing, particularly after two very significant gas transportation tariff increases within the last 12 months, to have to respond to a consultation paper for which the stated rationale is to "reduce the amount of flexibility offered to system users". The combined effect of the tariff increases with the two proposals in this consultation paper will mean paying significantly more for a much diminished product.

Aughinish Alumina is a large manufacturing complex operating a high efficiency Combined Heat and Power plant ("CHP") and alumina manufacturing calciners on natural gas. The CHP primarily produces steam and electricity for alumina production. Surplus electricity is sold into the Single Electricity Market and this brings Aughinish into the power sector. The consultation proposal in effect obliges the power sector and therefore Aughinish manufacturing to book much higher amounts of primary gas capacity than at present, by removing the right to transfer secondary exit capacity. Most gas generators including Aughinish already have the capability (and indeed the obligation) to be able to use alternative fuels. To place a further obligation (and cost) on the sector may well be highly discriminatory and will no doubt be vigorously opposed by power generators. If such an implicit obligation were to be imposed it would be indefensible not to allow full recovery of such gas capacity costs though complimentary changes to BCOP (discussed briefly below).

Restriction on Capacity Transfers vs Trading

It the first instance we consider the distinction made to between capacity Trading and capacity Transfers (page 8) to be insufficiently justified and potentially discriminatory. If there are sound economic benefits to be achieved by re-allocating exit capacity between shippers (or a single shipper's supply points) at a single geographical location then surely these benefits must also exist for re-allocations between different geographical locations? The paper states that there is surplus capacity on the system (indeed this is the root cause of the problem), hence system constraints cannot be argued to be relevant to re-allocations of exit capacity between different geographical locations.

The fact that re-allocations of gas exit capacity will ***in practice*** be still be available to a small number (perhaps only one) participant, i.e. those with multiple gas generator units on the same site, could amount to significant discrimination, particularly considering the other market mechanisms adopted to counter market dominance.

Entry and Exit Tariff Recovery

We are also concerned that the consultation paper is addressing only half of the underlying problem of tariff under-recovery, i.e. lower exit capacity bookings. The paper presents cash flows relating to exit points though fails to present any data on the changes in entry bookings. However, it would appear logical that shippers to the power sector would balance entry and exit bookings, and hence reductions in primary exit bookings would have a matching impact on entry booking (principally Interconnector revenues). This is supported by the following extract from the letter dated 23rd January 2013 from Bord Gais to CER[1];

"BGN is also forecasting a significant reduction in 2012/13Moffat bookings to the extent that they will be 17% lower than the 11/12 outturn. The reduction in the capacity has been caused by lower demands at exit......."

The consultation paper in effect presents the issue as an exit capacity only problem and hence restricts discussion of solutions to exit based modifications. It would therefore be helpful if CER could publish and equivalent version of Table 1 for entry/Interconnector System bookings so that participants can assess whether consideration on entry based solutions would also be relevant. If so, we believe that equal focus should be placed on addressing any tariff under-recovery issues which may be associated with under recovery from entry bookings, i.e. principally due to sunk Interconnector investments costs.

Industry in Ireland (and also the power sector) does not ***have*** to use gas or book gas transportation capacity. Industry can retire, relocate to more attractive locations or use

[1] CER13034a.pdf

alternative fuels and/or processes. As far as I am aware there is no obligation for Irish gas power generators to remain operational and if the delivered cost of gas increases too much then alternative fuels may be used instead, or generation plant may be mothballed (as has occurred in recent times in GB).

While Aughinish is not arguing that Interconnector assets should be stranded we urge deferring recovery of the cost of the interconnectors until such time as utilisation again increases. This would allow Bord Gais to recover its costs, while at least limiting cost increases for end users whilst maintaining the current flexibility to transfer exit capacity.

It would therefore seem to be time for CER to address a core problem underlying this proposal, i.e. under recovery due to the previous over-investment in gas Interconnection capacity. It is not a given that just because the excess Interconnector assets exist that they should continue to be underwritten by all transmission customers, and they may have to be written off over time. Indeed such decisive action, reducing delivered gas prices and stimulating Industrial gas demand, may be the only way to avoid a self-perpetuating circle of increasing gas transportation costs and falling network utilisation.

Legislative Basis

Section 3 of the consultation paper provides background on the legislative basis for adopting the proposal and the reasons why CER considers it to be compliant. Aughinish has not taken any legal advice so far, although on an initial reading the arguments made supporting compliance of the proposal appear very weak. In particular, stating that article 16 “deals with” cross border trades is an eccentric interpretation of the in intent of the clause, i.e. implementation of congestion management procedures. If appropriate congestion management procedures are not adopted in Ireland this can in any event have an impact on cross border flows to Northern Ireland and GB and hence through to continental Europe.

The suggested removal of secondary exit capacity transfers is undue interference in what could be a liquid tradeable market. To remove the ability to transfer capacity at exit runs counter to the other Europe wide market initiatives to improve liquidity, competition and transparency in energy markets, and will lead to further sub-optimisation of expensive assets.

Further, there would be very little point is adopting this proposal if it becomes subject of a costly legal challenge and has to be reversed, leading to further regulatory uncertainty in combined gas and electricity markets which are already subject to a very high degree of regulatory uncertainty. If CER is confident in its legal advice then we invite it to publish any independent legal advice that it has obtained so that consultation respondents do not have to incur additional expense seeking their own legal advice.

Unintended Consequences

A further consideration is whether the proposed changes will have the desired effect, i.e. an increase in primary capacity bookings. Based on previous experiences of the unintended consequences of rushed and ill-considered regulatory changes there must be considerable doubt of this occurring. The proposal in the recent consultation paper[2] on the treatment of gas capacity costs in SEM bid prices ("BCOP paper") assumes that a liquid secondary within day gas capacity market exists. However, Proposal 2 in this consultation paper proposes to remove the within day capacity market, which runs counter to the proposal in the BCOP paper. Market participants could be forgiven for thinking that there may be a lack of clarity and forward thinking in the decision making process in this area.

Consider the case of a generator which decides not to purchase any primary gas capacity, and offers to SEM based on distillate price alone. The BCOP paper proposal, combined with this proposal, will oblige such a generator to offer on the basis of wholesale gas purchase costs plus the price of (any) secondary within day gas capacity (par 4.32, BCOP Paper). In our response to consultation paper SEM-12-089 we stated;

"... we maintain that for a dual fuelled gas generator the level and durations of its gas capacity bookings must be entirely its own commercial decision. Back up fuel requirements mean that security of supply and hence eligibility for capacity payments are not at risk. For Regulators to prescribe an "optimum" strategy for gas capacity booking would be undue interference in the market and would inhibit innovation. Therefore a dual fuelled gas generator should be free to purchase no annual gas capacity, 100% annual gas capacity or any other percentage in the range, and will take the commercial consequences of its decisions."

It would clearly be discriminatory and undue influence on the generation market if a generator was obliged use gas and gas transportation capacity when using distillate would be its preferred commercial choice. Aughinish is an industrial customer of gas and the operator of an embedded high efficiency, We cannot therefore support consideration of mandatory bookings for the power sector, as raised in the "Alternative Proposals" section of the consultation paper. It should be noted that NDM users are not obliged to use gas, as they can substitute to electricity, small scale renewable/heat pumps or other fossil/biomass fuels to meet their energy needs. Further, the BNE reference plant is distillate only, and any change to the market rules which mandated the use of gas would have clear impacts on the BNE price and associated CPM payments.

[2] SEM-13-039, Gas Transportation Capacity Costs

In conclusion, we believe that instead CER should consider a more fundamental approach to rebalancing and tariff revenues versus allowable regulated income, e.g. deferment of cost recovery related to previous over-investment.

Yours faithfully,

Sent via email and accordingly not signed.

Mike Ronan